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Pursuing Small Liability Coverage Claims Without Losing Your Shirt

Finley Harckham

Reports about the daunting expense of high stakes, take no prisoners environmental and asbestos insurance coverage lawsuits have left some risk managers with the impression that once coverage has been denied, there is no point in pursuing their claims in court unless many millions of dollars are at stake. That is, of course, what the insurance companies would like their policyholders to believe, but nothing could be further from the truth. A policyholder's recovery on relatively small claims ($500,000–$5 million) can far exceed the percentage of recovery on larger claims, and those results can be achieved in a much shorter period of time and with far less litigation.

Success in these smaller cases is possible for the same reason that bigger actions can be so expensive—the damage or injury at issue for environmental, asbestos and other toxic tort claims often spans multiple coverage periods and therefore triggers a number of insurance policies sold by a number of different companies. In a big dollar "megacase," the insurance companies will pool their resources and fight a war of attrition against their policyholder. Their goal is to achieve a cheap settlement by making the litigation extremely expensive for the policyholder. However, in a case involving fewer coverage dollars, many insurance companies will quickly settle a good faith claim, rather than incur litigation costs which may exceed their exposure.

Look Before You Leap

The most important phase of any insurance coverage action, large or small, is the initial evaluation of the coverage claims. This requires basic information about the lawsuits and other actions in which the policyholder is exposed to liability, and a review of all liability insurance policies dating back to the year in which the first supposedly harmful activity began. Older insurance policies often prove to be very valuable in environmental coverage actions, and insurance archaeologists may be able to locate copies of policies that have been lost over time.

The insurance policy review will create a picture of the policyholder's coverage at relevant times, but may not, in itself, provide an answer to whether a coverage action is warranted. The coverage analysis is often complicated by the question of which state's law will be applied in an insurance coverage action, because the meaning given to relevant standard form general liability insurance policy provisions differs from state to state. For example, some states' courts have interpreted the standard form pollution exclusion introduced in 1970 as a mere clarification of the scope of "occurrence" based coverage. Other courts interpret it as excluding coverage for pollution claims that do not result from a quick and unintended discharge of contaminants. Any uncertainty is best dealt with by determining which states' laws a court might reasonably apply, and determining whether the suit is worth pursuing under the least favorable of those laws.

Use a Rifle, Not a Neutron Bomb

If the decision is made to bring a coverage lawsuit, the next important issue to address is which insurance companies to name as defendants. In high stakes coverage cases policyholders often sue on every primary, umbrella and excess insur-

ance policy issued to them for any year in which coverage may conceivably be triggered. That approach makes sense where the ultimate liability is unknown and may become astronomical—such as in cases involving many environmental sites for which remediation plans have not yet been approved. However, in a smaller case, such as an action involving a single environmental site where the policyholder has been allocated a small percentage of liability as part of a PRP group and has a fairly good idea of its exposure, suing insurance companies over policies which are not likely to be triggered to pay the claim can be a costly mistake, for two reasons.

First, the more insurance companies you sue, the more the case takes on the character of a megacase, and the greater the likelihood that the insurance companies will pool their resources and coordinate their efforts. This increases the likelihood of an active defense which will drive up your litigation costs. Second, insurance companies are becoming increasingly aggressive in seeking the dismissal of excess insurance policies from actions in which the policyholder's projected liability does not reach their layers of coverage.

In smaller cases the policyholder is often better served by suing only the insurance companies from whom he or she is likely to recover if the claim succeeds. This approach entails some risk that the policyholder's liability will ultimately exceed expectations, and that a settlement or judgment in the coverage action will leave insufficient coverage. However, in many instances the policyholder will be happy to pursue a smaller group of insurance companies in the hopes of keeping the litigation from taking on the life—and expense—of a megacase.

Settlement is Too Important to Trust to Lawyers

Often, a plaintiff's strategy is to aggressively litigate, both to prepare the case for trial and also to attempt to force a favorable settlement from the defendant. That strategy may be unsuitable in a small coverage action because it can be expensive and invite an aggressive response from the insurance companies, resulting in more expense.

The better approach in small coverage actions is to file the suit to show the insurance companies you mean business, and then immediately pursue settlement. The limited time the insurance companies have to answer the complaint creates a window of opportunity in which they can settle without incurring any litigation expense. During that period, some insurance companies may approach the policyholder about settlement, but it is no sign of weakness for the policyholder to make the first move when the stakes are small. Negotiations often proceed most smoothly when handled by the policyholders' risk manager or in-house counsel dealing directly with the insurance companies' claims personnel, without the direct participation of outside lawyers for either side. Although coverage counsel can play an important role in preparing the policyholder for settlement discussions, their direct involvement in negotiations will inevitably result in the participation of the insurance companies' lawyers, and what should be a business negotiation may turn into a legal debate.

Often, insurance companies will seek to settle a case through a "buy back" of certain coverages or all coverage under the policy. Such an agreement may be unwise for policyholders who do not know the full extent of their potential liability for present and future claims falling within that coverage. However, policyholders who are confident they will not need a policy's coverage in the future (or fear that there will be no coverage in the future due to the financial condition of the insurance company) may recover more through a coverage buy back with a single insurance company than the entire liability at issue in the case.

After an initial round of settlements, some insurance companies are likely to remain in the case. However, by making the earlier settlements the policyholder will have developed a "war chest" to finance the litigation (if necessary) and evened the playing field by reducing the economic advantage of the remaining defendants.

Often, the policyholder can make one or more strategic motions in the early stages of the case which will promote settlement with the remaining defendants by bringing into sharper focus the likelihood that certain insurance policies will be implicated by the coverage claims, and to what extent. For example, in an action involving damage or injury over many years, insurance companies are likely to assume, for settlement purposes, that liability will be spread across all coverage periods on a pro rata basis. Such an allocation may result in little or no exposure under umbrel-

la or excess policies. However, the policyholder may ask the court to adopt a "continuous trigger" of coverage, which requires all insurance policy periods from the first exposure to harmful conditions to respond to the claim, and seek application of the "pick and choose" theory of allocation, which allows the policyholder to select the triggered policy periods which will respond first to satisfy its claim. Resolution of that issue in the policyholder's favor will leave the excess and umbrella insurance company defendants with a larger potential exposure than anticipated, and therefore strengthen the policyholder's settlement position.

The amount of pretrial discovery needed by the policyholder in a small coverage action should not be great, and experienced coverage counsel should be able to pinpoint the important areas and avoid costly "fishing expeditions." Likewise, although the policyholder should expect to incur some expense responding to discovery requests, insurance companies are typically not inclined in small actions to propound burdensome requests and then incur the costs of litigating the propriety of their discovery and paying the copying charges for voluminous document productions.

Following this approach, the policyholder can make significant recoveries before incurring substantial legal expenses. The risk manager is then in a position to make litigation and settlement decisions without having to worry about losing his or her shirt. ■

FINLEY HARCKHAM IS A PARTNER IN AKO'S NEW YORK OFFICE. HE CAN BE REACHED AT (212) 278-1543 OR AT **fharckham@andersonkill.com**