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Insurance Companies Stopped From Seeking Reimbursement From Policyholders — Not Taking Reservations

By William G. Passannante and Darin J. McMullen

Under what circumstances can an insurance company seek extracontractual reimbursement from a policyholder? None, the Utah Supreme Court ruled early this year, in *United States Fidelity and Guaranty Co. v. United States Sports Specialty Association* (January 13, 2012). With the decision, Utah joins a growing list of jurisdictions, including Pennsylvania, Illinois and Wyoming, as well as several federal circuit and district courts, that prohibit insurance companies from unilaterally altering the terms of an insurance policy in order to seek reimbursement of defense costs and insurance proceeds. Emphasizing the paramount significance of the terms of the insurance policy sold by the insurance company, the Utah Supreme Court held that allowing an insurance company to seek extracontractual reimbursement under language contained in a reservation of rights letter would result in a "perverse manipulation of risk that has no place in [Utah] law."

Settlement Rejected and Reimbursement Sought

In *USSSA*, the United States Sports Specialty Association purchased a liability policy from USF&G that provided coverage with a policy limit of $2 million. After a seven-year-old boy was struck by a bat during a softball game sponsored by USSSA, his parents brought suit. USF&G refused to accept settlement offers within policy limits and subsequently a jury awarded a verdict of roughly $6.1 million against USSSA. USF&G moved to stay execution proceedings and block attempts to collect the judgment. The court stayed execution pending the outcome of the other post-trial motions on the condition that a bond for the entire amount of the judgment is posted within five business days of the hearing. USF&G initially posted a bond up to policy limits.

When USSSA demanded that USF&G post the entire amount, USF&G did so under "a unilateral reservation of rights." USSSA contended that it never agreed to any reservation. Ultimately, USF&G settled the judgment for $4.825 million "under a 'unilateral reservation of rights' that purported to allow USF&G to seek reimbursement from USSSA for the approximately $2.8 million of the settlement that exceeded policy limits."

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USF&G then sought restitution in the United States District Court for the District of Utah, which ultimately certified three questions to the Utah Supreme Court, including whether an insurance company has a right to reimbursement or restitution against a policyholder to the Utah Supreme Court.

No Extracontractual Right to Restitution Through a Claim of Unjust Enrichment

In rejecting USF&G's contention that its right to restitution was predicated upon the extracontractual and equitable theory of unjust enrichment, the Utah Supreme Court first noted that "[unjust enrichment] is designed to provide an equitable remedy where one does not exist at law" and that the remedy may be invoked "only when no express contract is present." The court further recognized that an insurance policy is the "exclusive authority that 'govern[s] the rights and obligations of the parties,'" and that allowing a cause of action for unjust enrichment "in the face of an enforceable contract governing the parties' rights would effectively add or modify terms for which they had not bargained."

Accordingly, the court sought to determine whether the right to reimbursement is "the type of right that should be expressly provided for in a policy had the parties intended." If that question is answered in the affirmative, "there cannot also be an extracontractual right to restitution through a claim of unjust enrichment."

The court analyzed portions of the Utah Insurance Code, which mandates that the parties to an insurance contract bargain for each term and express their agreement on such terms in writing. The Utah Code further prohibits any agreement or provision that is not "fully set forth in the policy" or "made part of the policy at the time of its delivery" in order to "ensure that the entire insurance contract is contained in one document so that the insured can determine from the policy exactly what coverage he or she has." Emphasizing the sanctity and importance of the written insurance policy, the court stated that the written policy "outlines the material terms and obligations that may be enforced under the policy, and it defines the risk relationship the parties have established."

The court further stated that the purported right of an insurance company to recover from its own policyholder "distorts the allocation of risk" between the parties and that such an "altered relationship" can materially impact the "motives, interests and incentives that arise" between the insurance company and the policyholder in the context of a claim for coverage. Accordingly, the court held that "an insurer's claim to an unbargained-for right to reimbursement from its insured presents a perverse manipulation of risk that has no place in our law" and that "an insurer's right to recover reimbursement from an insured may only arise, if at all, under the written terms of their insurance policy." Thus, USF&G's unilateral attempt to reserve the right to reimbursement was held illegal and unenforceable and USSSA was not required to pay any of the settlement funds paid in excess of policy limits. Anderson Kill filed an amicus brief on behalf of United Policyholders in the *USSSA* case in the Utah Supreme Court.

Similar Rulings in Other States

The significance of the *USSSA* decision extends beyond the dispute among the parties in that case. As noted above, several jurisdictions have barred insurance companies from seeking reimbursement from their policyholders in the absence of express bargained-for language in the policy that authorizes a right to reimbursement.

For example, in its 2010 decision in *American and Foreign Insurance Company v. Jerry's Sport Center* (August 17, 2010), the Supreme Court of Pennsylvania held that an insurance company cannot seek the reimbursement of defense costs from a policyholder unless the right to reimbursement was expressly provided for in the policy. Similar to Utah, Pennsylvania rejected an insurance company's attempt to alter the binding contractual obligations by way of a reservation of rights letter. The Supreme Court of Pennsylvania held that an insurance company cannot create new rights in a reservation of rights letter, but instead can only reserve those rights that were created in the insurance policy. Consequently, like Utah and other jurisdictions, the high court in Pennsylvania preserved and under-

scored the sanctity of the written policy sold by the insurance company.

Following the *USSSA* decision, policyholders can add Utah to the burgeoning list of jurisdictions that prohibit insurance companies from unilaterally altering the contract with its policyholder in seeking reimbursement. Because some jurisdictions still allow for such after-the-fact alteration of the relationship between an insurance company and policyholder, policyholders should be keenly aware of the state law which governs any right to reimbursement dispute. However, the recent decisions by the Utah and Pennsylvania Supreme Courts suggest that a trend may be developing in which the terms of the original insurance policy are honored, preventing after-the-fact changes. Perhaps, this is one instance in which "not taking reservations" is a welcome situation.

About Anderson Kill

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