RISK MANAGEMENT
INSIGHTS

by W. Brian Ahern, RPLU

Case Sends Message: *Cooperate with Your Insurance Carrier*

In a recent decision, a California district court resolved an issue that can create conflict between an insurance carrier and its insured: who picks the lawyers that will represent the policyholder when the insurer agrees to defend the case under a reservation of rights. In *Travelers Property v. Centex Homes*, C10-02757, the court found that a dispute over selection of the defense counsel relieved the carrier of both its duty to defend and indemnify under the policy. The decision illustrates the importance of cooperating with one's insurance carrier when facing a defense claim and to addressing the selection of counsel before the policy is bound.

In 2009, Centex Homes, a homebuilder, was sued for construction defect by multiple homeowners and tendered the defense of two actions to Travelers. Within one week, Travelers responded, requesting additional information from Centex. After a delay in receiving the information, Travelers subsequently accepted the tenders subject to a full reservation of rights and agreed that the law firm initially retained by Centex could continue as defense counsel.

Six months later, however, Travelers selected different counsel for Centex, which resulted in the homebuilder's refusal to accept the new legal team. Instead, Centex asserted its right to independent counsel under Cal Civil Code §2860 (which provides insureds independent counsel under a duty to defend policy) unless Travelers could show that there was no conflict of interest.

Centex did not receive any response from Travelers regarding the perceived conflict issue. Instead, Travelers filed a declaratory judgment action in the U.S. District Court for the Northern District of California alleging that it owed no duties to defend or indemnify because Centex's failure to accept its appointed counsel breached its duty to cooperate. The court agreed, deciding that "prejudice inherently existed" when Centex refused Travelers' appointed counsel. Regarding Centex's assertion of Civil Code §2860, the court found that Travelers' reservation of rights did not create an actual conflict of interest.

Policyholders do have many rights under Civil Code §2860 and may be entitled to independent counsel. However, policyholders must be mindful of their duty to cooperate under the policy or risk losing coverage entirely. According to local defense attorney Greg Garbacz, this case is an important one for California insureds. "The case points out the inherent dangers of an insured resisting the appointment of counsel by its insurance carrier where the policy clearly reserves this right to the insurance carrier. The Centex court quickly rejected the insured's arguments as to why it could not accept the appointed counsel, finding that the insured's objections were, at best, theoretical and rejecting the perceived conflicts of interest. As a result, the insured forfeited its right to a defense and right to seek reimbursement of defense expenditures, obviously a very painful result."

The best time to address any concerns regarding your policy or the right to select counsel is when the policy renews and before a claim arises. Some carriers may consider adding an endorsement which names a specific counsel/law firm to be used to defend a claim or a "mutual consent of counsel endorsement" which allows for both parties to mutually agree on defense counsel.

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