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New Day, Same Old Headaches

Navigating Coverage Issues Involving Multiple Insurance Plans

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INTRODUCTION

Modern professional liability insurance programs rarely consist of just a single policy. Sophisticated insureds frequently structure coverage through a combination of self-insured retentions, primary commercial policies, and one or more layers of excess insurance. Insureds may also manage risk using alternative risk financing such as interlocal government risk pools or risk retention groups designed to maintain predictable losses while transferring catastrophic exposure. However, as these programs grow more complex, so too do disputes regarding risk allocation, defense obligations, exhaustion, and ethical considerations. Add multi-year or long tail claims to the picture and the claim can become even more difficult to untangle. This is particularly true where an insured has changed its insurance portfolio over time.

This paper examines the commonly used insurance programs, challenges in addressing how risk is allocated among these programs, and attendant practical and ethical challenges that arise in multi-carrier and multi-year professional liability claims.

ONE OF THESE INSURANCE POLICIES IS NOT LIKE THE OTHER

Layered professional liability insurance programs are generally structured to balance risk management and transfer with cost controls. Some insureds manage risk largely through the commercial market with traditional liability insurance policies. Other insureds choose self-insured retentions (SIRs) or participation in insurance risk pools. Both groups may obtain excess coverage, attaching above defined points, for larger or less predictable exposures.

While these structures offer insureds flexibility and diversity in managing risk, they also depend on careful coordination to operate without conflict. Defense provisions, exhaustion requirements, and allocation language may, or may not, align across layers and over years. Where there is misalignment, disputes can arise concerning which entity bears the initial duty to defend, when excess coverage attaches, and how losses should be allocated across layers and policy periods.

A. Traditional Insurance

Traditional liability insurance is the primary product for managing third-party risk and operates, in its most basic form, by shifting the economic consequences of a loss from the insured to their insurer. This product is designed to protect insureds from financial loss in the event they are found legally liable for causing injury or damage to others that is covered under the policy.

Benefits of traditional insurance include its broad availability[1] for many types of liability, that it is generally protected by state guaranty funds if the insurer becomes insolvent, and it is typically backed by insurer capital, surplus and reinsurance. Downsides to traditional insurance include market unpredictability, pricing volatility, and the ceding of loss control and claims handling from the insured to the insurer.

Traditional insurance policies often include a deductible provision whereby the insurer undertakes to pay defense and indemnity owing under the policy up front and later seeks

[1] While traditional insurance has historically been the most readily available, social inflation and the onset of nuclear verdicts has hardened certain high-risk markets.

reimbursement from the insured up to the amount of the deductible. Other insureds choose to use self-insured retentions (SIRs) to allocate the risk of losses to the insured up to a certain dollar amount. Understanding this distinction is important for understanding the insured's and insurer's obligations regarding defense or indemnity when a claim arises. When a policy is written with an SIR, the insured must pay up to the specified dollar amount before the insurance policy will respond to a loss. After the SIR is reached, risk shifts to the insurer to pay for defense and indemnity up to the policy limits.

B. Risk Pools

Insurance risk pools are an alternative form of risk transfer wherein a group of similarly situated insureds pools their risk and share the cost of liability losses covered by the appliable insurance contract. Risk pools are non-profit, cooperative, member-owned and governed. They are typically governed by the federal Liability Risk Retention Act, state statutes, by-laws, articles of incorporation, and/or interlocal agreements. Risk pools will also often use reinsurance to transfer excessive, catastrophic, or volatile risks, ensuring the pool remains solvent.

Risk pools offer members benefits in the form of stabilized premiums, tailored coverage, and a focus on loss prevention. Also, with the member-governed structure of risk pools, members may have a greater say in decisions made in their claims and for the pool as a whole. However, risk pools often serve a limited geographic area and members bear the risk of insolvency and potential unexpected assessments if losses exceed program projections. Extracontractual concerns are also complicated by the fact that any attack beyond the limits of insurance has a direct impact on the members and the solvency of the organization itself.

Public entities, in particular, frequently utilize risk pools to manage risk. Data from the Association of Governmental Risk Pools (AGRiP) indicates that of the over 90,000 local governments in the United States, roughly 80% utilize risk sharing. https://ucip.utah.gov/post/pooling-insight-overview. Public entity risk pools also often have high retention rates, with some reporting annual retention above 90 percent. https://riskandinsurance.com/what-public-sector-risk-pools-can-teach-private-sector-risk-managers/. Public entity risk pools also often use manuscript policies and write and revise their coverage on a regular basis.

C. Excess and Umbrella Insurance

Excess and umbrella insurance are both types of secondary insurance that function similarly, but with notable differences. Excess insurance generally provides coverage for claims that exceed the limits of the insured's primary policy. Insurance provided by an excess policy will typically only extend to the same claims which are covered by the primary policy. It does not expand the terms of the primary policy; rather it provides higher limits in the event of a catastrophic claim or loss.

Excess insurance is often more cost-effective because it is limited to the coverage in the primary insurance policy, albeit with higher limits. It also aligns closely with and is subject to the same or similar terms as the underlying primary insurance.

Umbrella insurance is a form of excess insurance that provides coverage for claims that exceed the limit of primary insurance. Umbrella policies may also cover claims that are either not covered or are excluded from the primary insurance coverage. Insureds may choose umbrella coverage over excess where they desire more comprehensive coverage, gap coverage, or higher limits.

D. Reinsurance

Reinsurance, referred to as insurance for insurers, is designed to transfer excessive, catastrophic, or volatile risks from the insurer to third-party reinsurers. By purchasing reinsurance, pools limit their liability on specific claims, stabilize loss experience over time, and increase their capacity to cover high-risk participants without exhausting their surplus.

In purchasing reinsurance, the risk pool, cedes portions of its liability to an insurance company, the reinsurer. There are two main types of reinsurance: facultative and treaty. Facultative reinsurance offers protection for a specific individual risk or contract. A reinsurance treaty covers multiple policies over a defined period.

ALLOCATION HEADACHES

A. Duty to Defend

An insurer issuing a policy providing primary coverage must carefully evaluate whether its duty to defend has been triggered in a given lawsuit. This analysis is especially crucial in professional liability cases which can be expensive to defend and carry significant risk for the insured and insurer.

For example, in claims involving alleged damages that span multiple years, there may be a disconnect between available limits and claim value that makes providing a defense even more challenging. Older policies may have lower limits or eroding limits, each of which may ultimately be less than the prospective cost of defense. The length of time involved in the claim also opens up the possibility of there being multiple triggering events across a number of policies years.

The consequences of failing to provide a defense when it was owed are often steep. In many jurisdictions, a refusal to defend that is later determined to be incorrect obligates the insurer to reimburse the insured for the cost of the defense as well as to pay the amount of any reasonable settlement or judgement. See, e.g., *Nixon v. Insurance Co.*, 120 S.E. 2d 430 (1961).

Another consideration is the nature of the insured's obligations when coverage is triggered. Where the insured's traditional liability insurance policy includes a deductible provision, the insurer undertakes to pay defense and indemnity owing under the policy up front and later seeks reimbursement from the insured up to the amount of the deductible. Differently, SIRs may offer insureds more control over claims handling and their defense but come with up-front costs as the insured is responsible for defense and indemnity up to the limit of the SIR.

Understanding this distinction is important for evaluating the insured's and insurer's obligations regarding defense or indemnity when a claim arises. The difference in the insured's obligations

with an SIR versus a deductible can also have practical consequences when insureds lack the capacity or willingness to manage their own defense.

Risk pools can also include modified defense or defense-within-limits provisions that impact the duty to defend. Under a policy with a defense-within-limits provision, the cost of attorney's fees and expenses erodes the policy's limits. Such provisions are typically found in professional liability policies, while commercial general liability policies offer a defense outside of policy limits. However, several states have sought to regulate defense within limits provisions through mechanisms such as prohibiting defense within limits for certain types of coverages, confining their use to policies with limits under a certain amount, or through other means. See A.C.A § 23-79-307(5)(A), LSA-R.S. 22:1272; M.S.A. § 60A.08 Subd. 13; NAC R029-23 §2 and NAC R029-23; §3N.J.A.C. 11:13–7.3; N.M. Admin. Code 13.11.2.8, 13.11.2.9; and 11 NYCRR 71.2-71.3.

Yet another consideration is whether the applicable jurisdiction allows "targeted tenders." Where a targeted tender is permitted, an insured who has coverage under multiple policies has the right to submit a claim to only one of those insurers, demanding a defense and indemnification. See e.g., *John Burns Construction Company v. Indiana Insurance Company*, 727 N.E.2d 211 (Ill. 2000). Most jurisdictions have rejected the concept of targeted tenders; however, variations across insurance plans in limits, deductibles and SIRs can incentivize insureds to focus on certain entry points in their insurance program over others.

B. Trigger of Coverage

When a single claim implicates multiple insurance policies, the central coverage question becomes what the coverages attached and how coverage is allocated. In these situations, understanding the circumstances that trigger coverage under each policy is crucial to determining the allocation of risk. Disputes can arise when a particular loss implicates multiple policy periods, multiple lines of overlapping coverage with the same or different insurance companies, or both.

Which policies bear responsibility for the risk also depends on how courts approach the issue of trigger of coverage in the relevant jurisdiction. For example, in wrongful incarceration cases, courts typically apply one of three main approaches to the question of trigger (1) single trigger; (2) multiple triggers; and (3) damages-based trigger.

A majority of courts across the Country have rejected a "continuing occurrence" analysis and hold that occurrence-based coverage for wrongful conviction claims triggers when criminal charges are filed, or at the time of conviction. *See Royal Indem. Co. v. Werner,* 979 F.2d 1299 (8th Cir.1992) (Missouri law); *S. Md. Agric. Ass'n, Inc. v. Bituminous Cas. Corp.,* 539 F.Supp. 1295 (D.Md.1982) (Maryland law); *Ethicon, Inc. v. Aetna Cas. & Sur. Co.,* 688 F. Supp. 119 (S.D.N.Y.1988) (New Jersey law); *S. Freedman & Sons, Inc. v. Hartford Fire Ins. Co.,* 396 A.2d 195 (D.C.1978); *Am. Family Mut. Ins. Co. v. McMullin,* 869 S.W.2d 862 (Mo.Ct.App.1994); *Paterson Tallow Co. v. Royal Globe Ins. Cos.,* 89 N.J. 24, 444 A.2d 579 (1982); *Harbor Ins. Co. v. Cent. Nat'l Ins. Co.,* 165 Cal.App.3d 1029, 211 Cal.Rptr. 902 (1985); *Selective Ins. Co. of S.C. v. City of Paris,* 681 F.Supp.2d 975 (C.D.Ill.2010) (Illinois

law); *N. River Ins. Co. v. Broward Cnty. Sheriff's Office,* 428 F.Supp.2d 1284 (S.D.Fla.2006) (Florida law); *Coregis Ins. Co. v. City of Harrisburg,* 2006 WL 860710 (M.D.Pa. 2006) (Pennsylvania law); *Billings v. Commerce Ins. Co.,* 458 Mass. 194, 936 N.E.2d 408 (2010); *Town of Newfane v. Gen. Star Nat'l Ins. Co.,* 14 A.D.3d 72, 784 N.Y.S.2d 787 (2004); *Genesis Ins. Co. v. City of Council Bluffs*, 677 F.3d 806 (8th Cir. 2012) (Iowa law). But see *City of Hickory v. Grimes*, 814 S.E.2d 625 (N.C. App. 2018)(two alleged wrongful acts, committed approximately 16 years apart, were distinct wrongful acts triggering coverage under multiple policies).

A smaller number of courts apply a single trigger approach focusing on the date of arrest, because "there is no interval between arrest and injury that would allow an insurance company to terminate coverage." *North River Ins. Co v. Broward County Sheriff's Office*, 428 F.Supp.2d 1284, 1292 (2006) ("The better rule…is to consider the time of the arrest and incarceration the 'trigger' in both malicious prosecution and false imprisonment cases."). Even where the plaintiff alleges that law enforcement failed to disclose exculpatory evidence during an extended period of the plaintiff's incarceration, such "acts or omissions alleged to have occurred after the date [the plaintiff] was charged are really continuations of the same alleged harm." *Indian Harbor Ins. Co.*, 392 Ill. Dec. at 822, 33 N.E.3d at 623; *see also Sarsfield v. Great Am. Ins. Co. of N.Y.*, 335 Fed. Appx. 63, 67 (2009) ("[T]heories of continuing injury only apply in tort cases which concern injuries which may have existed but were unknown at the time the insured purchased insurance.").

A third approach which has been pursued more recently is an injury- or damages-based trigger approach. This approach has been used when a policy extends to damages occurring during the policy period even where the underlying tort occurred months or years before the policy period began. See *Travelers Indem. Co. v. Mitchell*, 925 F.3d 236, 241 (5th Cir. 2019); *St. Paul Guardian Ins. Co. v. City of Newport, KY*, 804 F. App'x 379, 381 (6th Cir. 2020) (unpublished); *Travelers Indem. Co. v. Forrest County*, 195 F.Supp.3d 890 (S.M. Miss. 2016).

C. Allocation of Available Insurance

Where multiple policies are triggered, the allocation of both defense and indemnity obligations must be evaluated. Courts typically employ one of three methodologies to allocate costs for defense and indemnity among insurers with available coverage: pro rata time-on-the-risk, pro rata by limits, or all sums.

Allocation under the pro rata time-on-the-risk method generally calculates what an insurer owes by dividing the number of years the insurer was on the risk by the number of total years of insurance exposed and multiplying the resulting fraction by the total amount of the loss. *Boston Gas Co. v. Century Indem. Co.*, 910 N.E.2d 290 (Mass. 2009); *Radiator Specialty Co. v. Arrowood Indem. Co.*, 383 N.C. 387 (2022). Where a pro rata approach is applied, insureds may be responsible for a portion of the loss for any uninsured time periods if the relevant jurisdiction applies the unavailability rule. *Keyspan Gas E. Corp. v. Munich Reinsurance Am., Inc.*, 31

N.Y.3d 51, 96 N.E.3d 209 (2018)(explaining the unavailability rule).

Other courts have applied a variation of the pro rata time-on-the-risk method that allocates based on limits. The pro rata by limits method allocates the loss based on the percentage of limits each policy bears to the total available limits, resulting in insurers with high limits being responsible for a greater portion of the loss. See e.g., *Hartford Underwriters Ins. Co. v. Hanover Ins. Co.*, 122 F. Supp. 3d 143, 145 (S.D.N.Y. 2015).

Yet other courts have allocated insurer costs pro rata by years and limits, a hybrid approach that factors in both time-on-the-risk and the limits of each applicable policy. *EnergyNorth Natural Gas, Inc. v. Certain Underwriters at Lloyd's*, 934 A.2d 517 (N.H. 2007)(encouraging allocation by pro rata by years and limits). In addition, some courts have observed that the method of insurance allocation can depend on the language used in the subject policies. Matter of Viking Pump, Inc., 27 N.Y.3d 244 (2016) (all sums allocation approach applies where policy contains non-cumulation language).

A minority of jurisdictions apply an all sums theory of allocation, depending on policy wording and the trigger theory applied. Under this approach, the insured can look to any insurer whose coverage is triggered to pay the entire loss up to the limits of that insurer's triggered policy. *State of Cal. v. Continental Ins. Co.*, 281 P.3d 1000 (Cal. 2012) (all-sums allocation in continuous loss setting).

Additional considerations involved in determining when excess coverage is triggered further complicates allocation issues. The question is largely one of whether a vertical exhaustion or horizontal exhaustion methodology will be applied. Horizontal exhaustion delays the trigger of excess insurance policies until the limits of all triggered primary policies have been exhausted. *Kajima Constr. Servs. v. St. Paul Fire & Marine Ins. Co.*, 879 N.E.2d 305 (2007); *Great Am. Ins. Co. v. Allied World Assurance Co.*, No. 22-12496, 2023 WL 3736878 (11th Cir. 2023). When a jurisdiction employs vertical exhaustion, once the primary policy in a given coverage period is exhausted, the excess policy above it during the same coverage period is triggered. *Chandler v. Liberty Mut. Ins. Group*, No. 2005–71, 2005 WL 5629027 (E.D. Ky. 2005); *St. Paul Fire & Marine Ins. Co. v. Am. Int'l Specialty Lines Ins. Co.*, 365 F.3d 263 (4th Cir. 2004) (predicting Virginia law); *Am. Indem. Lloyds v. Travelers Prop. & Cas. Ins. Co.*, 335 F.3d 429 (5th Cir. 2003) (predicting Texas law; indemnity agreement can shift priority); *Radiator Specialty Co. v. Arrowood Indem. Co.*, 881 S.E.2d 597(N.C. 2022).

D. Ethical Considerations

Where multiple insurance plans potentially cover the same loss, ethical dilemmas can arise because defense strategy, factual development, and settlement decisions can impact which policy years are triggered and how costs are allocated, sometimes in ways that benefit one insurer or policy period at the expense of the insured or another insurer. In cases of multi-year exposure, the development of facts in discovery that impact the timing, continuity or number of occurrences can impact the exposure of individual insurers.

In long-tail cases where multiple insurers may share defense and indemnity obligations, liability

defense counsel may feel caught between competing interests in early settlement, aggressive litigation or other disputes between the insurers. The structure of a settlement can also impact allocation among triggered insurance policies. In addition, insureds may raise concerns that retained counsel is "steering" the defense in a way that benefits one insurer over another, or over the insured. To guard against this, some jurisdictions require insurers to pay for separate, independent counsel for the insured when an insurer has retained panel liability defense counsel to represent an insured and reserved its rights under the applicable policy. See e.g., *San Diego Navy Federal Credit Union v. Cumis Ins. Society, Inc.*, 162 Cal. App. 3d 358, 208 Cal. Rptr. 494 (1984) (an insured has a right to be provided independent counsel by the carrier when a conflict of interest exists between the insured and the carrier).

Insurers faced with these situations can engage coverage counsel to assist them in navigating the legal and ethical issues. In doing so, an insurer must consider, and adhere to, its obligations of good faith and fair dealing. Communication with plaintiff's counsel and the insured should be done openly, preferably in writing, with coverage counsel's role clearly explained. Coverage counsel should also be mindful of the insured's interests when discussing the coverage issues and the existence, or lack thereof, of available insurance.

FROM MIGRAINE TO MANAGEABLE: PRACTICAL TIPS FOR SUCCESSFUL CLAIM OUTCOMES

Faced with a situation where multiple coverages are implicated, forming an early strategy is key. Coverage counsel will also benefit from cultivating a reputation for collaboration, where possible, and civility.

When the claim is initially tendered, counsel should carefully review coverage under the insured's policy and work with the insurer to craft timely and clear communication to the insured explaining the available coverage, or lack thereof, and reserving rights as appropriate. Also, proactively investigate whether other coverage may be on the risk and which carriers may be involved, especially for multi-year or long-tail claims. Communicate clearly with your insured about the potential for other insurance coverage and seek their cooperation to investigate where needed.

Regarding other potential insurers' responsibility for the risk, coverage counsel will want to determine all of the potentially applicable coverage at the earliest opportunity. It is useful for counsel to work with the insured to gather information about other coverage and seek its assistance to tender the claim to other insurers. Careful cataloguing of implicated policies at the primary and excess layers will help identify issues and information gaps.

For each potentially applicable policy, note relevant information such as the type of insurance, policy period, limits, eroding limits, and deductibles or SIRs. It is also important to note the triggering event for each policy and whether there are any exclusions which may significantly limit or eliminate coverage. For excess policies, note whether the governing jurisdiction has adopted a horizontal or vertical exhaustion approach.

As the total insurance picture for the loss begins to emerge, note areas of overlapping coverage, as well as potential gaps. Also, as other insurers become involved, start an initial dialogue to obtain their positions on coverage and whether they will provide a defense. If multiple insurers are obligated to defend, the insured will benefit from coordination among the defending carriers to develop a cohesive plan for the defense and cost sharing.

As the underlying case progresses, reevaluate the expected allocation of insurance among the carriers, including which may be primary, co-primary, secondary or excess. In addition, coverage counsel will also want to think creatively about the insurer's options to bring the claim to a successful resolution despite the challenge of having multiple carriers involved. For example, the case may benefit from an early mediation, settlement discussions, or declaratory judgment action to resolve disputed issues.

CONCLUSION

Multi-policy insurance programs pose a number of challenges for insurers concerning who defend, how insurance is allocated and exhausted. Multi-year and long-tail claims, in particular, present thorny issues that insurers must navigate alongside the defense of the underlying claim. Developing an appreciation of the complex issues insurers face in these scenarios, and how to proactively address them, will aid in developing more successful risk mitigation strategies.

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