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New York State Court Rules That Darwin Has Duty to Defend but AIG Does Not, for Same Risk, Based on Differing Policy Language

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New York state court Judge Shirley Werner Kornreich recently ruled that **American International Group, Inc. ("AIG") didn't have to pay certain defense costs** for various suits brought against QBE Holdings, Inc. and its affiliates (collectively, "QBE"), but that QBE's other insurer **Darwin Select Insurance Co. ("Darwin") did**, despite the apparent similarities in language of the policies issued by the insurers and the fact that both insurers promised to reimburse QBE's defense costs. So what was the difference? AIG's policies stated that AIG "shall have the right, but not the duty" to defend, whereas the Darwin policies stated that Darwin "shall have the right and duty" to defend. This seemingly small variation made a significant difference in both the scope of defense coverage available under the policies and what QBE would have to prove to obtain coverage.

In *QBE Americas Inc., et al. v. Ace American Ins. Co.*, QBE sought coverage for defense costs in approximately 40 lawsuits and a government investigation centered on QBE's alleged participation in kickback schemes involving property insurance policies it "force placed" on homeowners to protect its secured interest when the homeowner failed to purchase its own property insurance. When the first of the suits arose in 2011, QBE provided notice to its professional liability insurers AIG and Darwin. Both insurers refused to advance defense costs to QBE. In the coverage suit that followed two years later, QBE sought defense costs for (1) litigation that had already settled or been discontinued, as well as (2) pending litigation for which AIG and Darwin refused to advance defense costs.

Judge Kornreich ruled that coverage for the first category was not ripe for determination. According to the court, when litigation is pending, there is a concern that an insured's inability to procure advanced legal fees will hamper its ability to put forth its best possible defense. By contrast, a decision regarding recoupment of defense costs already incurred will not impact an insured's ability to defend a case that has already ended; such a determination, then, should be made when the court decides whether the underlying claims are covered. The court declined to decide the issue of defense coverage for the terminated lawsuits because the parties had not yet conducted discovery and there were questions of fact as to coverage. Thus, the only issue before the court was whether QBE was entitled to defense costs related to pending litigation.

With respect to AIG, according to the court, there was no duty to defend. Although defense costs

were included in the definition of a “loss” for which the policies provided coverage, the policies expressly stated that AIG “shall have the right, but not the duty to assume the defense against any [c]laim made against [QBE].” Under that language, according to the court, AIG’s obligation to advance defense costs was limited to costs attributable to covered claims. QBE, however, had not established which claims in the pending lawsuits were covered or that the $1.5 million retention applicable to the AIG policies had been exhausted. Unless and until QBE established both, the court said, AIG would not be required to advance any defense costs.

Conversely, the court found that Darwin had a duty to defend based on the language in the Darwin policies which stated that Darwin “shall have the right andduty to defend.” Unlike AIG, Darwin had a duty to advance *all* of QBE’s litigation costs, not just those attributable to covered claims. So long as each lawsuit presented the possibility that any of the claims asserted might be covered, Darwin’s duty to defend was triggered.

In a curious twist, however, the court – without explanation – refused to order Darwin to pay QBE’s *past* expenses from *pending* litigation. If QBE wanted its defense costs advanced for those lawsuits, the court said, it should have sought those costs while the suits were pending; a decision on whether those costs could be recovered by QBE would now have to wait until the merits of coverage were decided.

Regardless of whether the court’s justification for denying defense coverage for past costs is true for terminated lawsuits, it doesn’t explain why QBE was unable to recover costs it already incurred in the underlying lawsuits *still being litigated*.

It’s hard to find a reported opinion discussing the duty to defend that doesn’t repeat the principle that the duty is a broad one, requiring an insurer to provide a defense if any claim brought against its insured is potentially covered under the policy. Why, then, should a policyholder that fails to immediately file suit against its recalcitrant insurer have to conclusively show that the claims aimed against it in the underlying action are covered?

The *QBE* case highlights how seemingly similar policies covering the same risk could have very different defense obligations. Policyholders should read the specific language of their policies closely when tendering claims so they are aware of any potential limits to the defense they are entitled to under the policy. Also, when purchasing or renewing coverage, they should keep in mind that policies under which the insurer must pay defense costs, but has no duty to defend, may provide narrower coverage and impose a heavier burden on policyholders in obtaining defense costs. And finally, companies can’t overlook the possible dangers of waiting too long to hold their insurers accountable for failing to live up to their duty to defend.

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