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What's in a Name? Well-Known Insurance Coverage Case Concepts That All Claims Handlers and Insurance Coverage Professionals Should Know

By Christopher P. Ferragamo and Susan Knell Bumbalo

"You have the right to remain silent. Anything you say or do can and will be used against you in a court of law. You have the right to an attorney, if you cannot afford one, one will be provided to you …" Anyone that has ever watched a crime drama or who-done-it movie can no doubt recite these words by heart. An avid fan of "Law & Order" or the quirkier "Brooklyn Nine-Nine" probably also knows that the above phrase is part of a suspect's *Miranda* rights. What the lay people may not know is that these statements uttered by fictional and real life police officers originate from a decision issued by the Supreme Court of the United States in the *Miranda v. Arizona* case in 1966. In that case, the Supreme Court held that the admission of an elicited incriminating statement by an individual not informed of these rights is a violation of the Fifth Amendment and the Sixth Amendment right to counsel. The above quoted statements, as well as the phase "*Miranda* rights," have now made their way into the everyday lexicon of most Americans.

Decisional case law handed down by federal and state courts over the past 40 to 50 years has likewise provided claims handlers and insurance coverage professionals with principles of law, albeit significantly less ubiquitous and well-known as *Miranda*, that have come to be known simply by their case names. This article identifies a number of the more widely-used of these types of insurance coverage concepts, identifies their origins, and provides a brief summary of each. Insurance professionals and attorneys practicing nationwide– or even within a single jurisdiction – should familiarize themselves with these common, insurance coverage principles in order successfully practice and "walk the walk and talk the talk" when these phrases are used in the handling of claims or providing coverage opinions and advice.

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Allocation Concepts

Courts across the country have been addressing the methodologies for allocating loss or damages across multiple triggered policies and policy years for decades. The concepts set forth below are some of the more popular of these concepts known by their case names.

Boston Gas Allocation (Massachusetts) (Pro Rata) - In *Boston Gas Co. v. Century Indemnity Co*., 910 N.E.2d 290 (Mass. 2009), the Massachusetts Supreme Judicial Court held that liability for claims involving environmental damage that occurred over multiple years should be allocated to insurance policies on a pro rata basis. The court held that if it was not possible to determine what specific damage occurred in each policy period, then the total damage should be apportioned among triggered insurance policies on a pro rata, time on the risk basis relative to the total number of years during which the damage occurred. The insured is required to participate in the allocation for uncovered periods, whether or not coverage was available during such time.

Carter Wallace Allocation (New Jersey) (Pro Rata by years and limits) - In *Carter-Wallace, Inc. v. Admiral Ins. Co*., 712 A.2d 1116 (1998), the Supreme Court of New Jersey adopted a method of allocation to determine when an excess insurer must participate in a coverage allocation. In *Carter Wallace*, the New Jersey Supreme Court rejected horizontal exhaustion as a method for allocating losses over a period of years, and rejected vertical exhaustion as an allocation method. Instead, the Court held that allocating loss among policy periods required a calculation of the share of responsibility borne in each year of the triggered coverage period. First, the amount of damages assigned to each triggered policy year must be determined by dividing the coverage available in that year by the total coverage available in all triggered years. The second step in the court's formula is to allocate vertically the costs that are assigned to each policy year. The court stated that it should be the presumptive rule of allocation in continuous trigger cases, "unless exceptional circumstances dictate application of a different standard." *Id*. at 1124. Under *Carter-Wallace* and its progeny, New Jersey Courts must allocate a percentage of liability to the insured for years in which coverage is

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unavailable either because the insured chose not to purchase it or because the insured is unable to produce evidence of coverage. *Owens-Illinois, Inc. v. United Ins. Co.,* 650 A.2d 974 (N.J. 1994). New Jersey Courts have also extended the allocation methodology to defense costs as well as indemnity expenses. *Benjamin Moore Co. v. Aetna Cas. & Surety Co.*, 843 A.2d 1094, 1102 (N.J. 2004).

Keene Allocation (Washington, DC) (All Sums) – Under the *Keene* approach to allocating damages stemming from long-term progressive injuries, the United States Court of Appeals, District of Columbia Circuit adopted joint and several liability in a case involving indemnification for asbestos-related personal injury claims. *Keene Corp. v. Insurance Co. of North America*, 667 F.2d 1034 (D.C. Cir. 1981). The court in *Keene* adopted a continuous trigger for asbestos claims from the date of initial exposure to manifestation of the injury and held that once a particular policy is triggered, the insurer is required to fully indemnify the policyholder for the entire loss up to its policy limits under any of the triggered policies, even though, due to the progressive nature of the injury, part of it may have occurred during another policy period or while the insured was uninsured. *Id*. at 1047. Under this "all sums" or "pick and spike" approach, the insurer can then seek contribution from other liable insurers based on either the "other insurance" provisions in the policies or common law contribution.

Keyspan Gas East Rule (New York) - In a decision issued in 2018 that will likely represent another insurance concept that will be known by case name, the New York State Court of Appeals rejected the unavailability exception to pro rata allocation in *Keyspan Gas East Corp. v. Munich Reinsurance America, Inc*., 31 N.Y.3d 51 (2018). In this case, which involved contamination at manufactured gas plants that operated from the 1880s into the 1900s, Keyspan sought coverage from various insurers, including Century Indemnity, which issued eight excess policies to Keyspan from 1953 to 1969 and whose policies were the only ones at issue in this decision. The issue before the court was whether under pro rata time on the risk allocation, the Century policies provided coverage to Keyspan for years before and after its policy periods when liability insurance for environmental contamination was

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unavailable in the marketplace. The court rejected the adoption of the unavailability exception to allocation, stating that to do so would be "inconsistent with the contract language that provides the foundation for the pro rata approach – namely the 'during the policy period' limitation- and that to allocate risk to insurers for years outside the policy period would be to ignore the very premise underlying pro rata allocation." *Id*. at 61. As a result, insureds are responsible for paying the share of losses that fall within any uninsured years.

Lamb-Weston Rule (Oregon) – Although the *Lamb-Weston* Rule does not really represent an allocation methodology, this legal concept does factor into how insurance policies respond to losses that trigger multiple insurance policies. Under the *Lamb-Weston* rule, *all* competing other insurance provisions are deemed mutually repugnant regardless of the language and defense costs should be split equally among primary insurers. *Lamb-Weston, Inc. v. Oregon Automobile Ins. Co.*, 341 P.2d 110 (Or. 1959).

Demands to Settle Within Policy Limits and Potential Exposure for Excess Verdicts

Most states have well-settled insurance coverage case law addressing the issue of whether, and under what circumstances, an insurer can be held liable for judgments in excess of the policy limits when an insurer has the opportunity to, but fails, to settle a claim at or within the policy limits. Below are some of the more well-known concepts that have made their way into insurance coverage lexicon and are often included in policy limit demands letters from claimants' counsel.

Holt Demand Letter (Georgia) – A *Holt* Demand Letter is a time-limited demand to settle a claim that has the potential to expose insurance carriers to bad faith damages. The concept stems from *Southern General Ins. Co. v. Holt,* 416 S.E.2d 274 (Ga. 1992). In *Holt*, the Supreme Court of Georgia held that where an insurer has full knowledge of an insured's liability and damages exceeding policy limits, the insurer can be subject to bad faith damages if its failure to settle within policy limits subjects the insured to a judgment in excess of those limits. The Court in *Holt* further held that when

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deciding to settle a claim within policy limits, the insurer must give equal consideration to the interests of its insured. The Supreme Court of Georgia recently clarified that an insurer's duty to settle arises only when the injured party presents a valid offer to settle within the insured's policy limits. *First Acceptance Ins. Co. of Georgia, Inc. v. Hughes*, No. 518G0517, 2019 WL 1103831 at * 1 (Ga. Mar. 11, 2019).

Rova Farms Claim (New Jersey) – A *Rova Farms* claim stems from *Rova Farms Resort v. Investors Insurance Company of America,* 323 A.2d 495 (N.J. 1974). In that case, the Supreme Court of New Jersey held that an insurer's bad-faith failure to settle a claim within policy limits can render the carrier liable for the entire judgment, including amounts that are in excess of the policy limits. A *Rova Farms* demand letter is a letter sent by the claimants or the insured to the insurance company to settle the claim within policy limits. The key to evaluating an insurer's potential excess exposure is whether the insurer has exercised good faith business judgment in deciding whether to take a case to trial or not. The *Rova Farms* Court defined a good-faith evaluation as including "consideration of the anticipated range of a verdict, should it be adverse; the strengths and weaknesses of all of the evidence to be presented on either side so far as known; the history of the particular geographic area in cases of similar nature; and the relative appearance, persuasiveness, and likely appeal of the claimant, the insured, and the witnesses at trial."

Shamblin Demand (West Virginia) – This concept stems from *Shamblin v. Nationwide Mutual Insurance Co.,* 396 S.E.2d 766 (W. Va. 1990). In this case, the Supreme Court of Appeals of West Virginia adopted a "a hybrid negligence-strict liability standard" to determine bad faith and held that an insurer "which has the opportunity to settle a claim against its insured within policy limits and fails to do so, may be liable to the insured for the portion of a verdict in excess of that limit." The Court in *Shamblin* specifically held that a *prima facie* finding of bad faith may be made against an insurer if that insurer fails to settle a claim after it has had the opportunity to settle within the policy limits and that such settlement "would release the insured from any and all personal liability." Like a *Stowers* demand, discussed below, a *Shamblin* demand letter is a demand to settle within limits in exchange for a

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full release of the insured from all liability. In assessing whether an insurer is liable to its insured for personal liability in excess of policy limits, courts analyze whether a reasonably prudent insurer would have refused to settle within policy limits under facts and circumstances, bearing in mind always its duty of good faith and fair dealing with insured.

Stowers Demand (Texas) – A *"Stowers"* demand stems from *G.A. Stowers Furniture Co. v. American Indemnity Co.,* 15 S.W.2d 544 (Tex. Comm'n App. 1929). A proper *Stowers* demand has three essential components: (1) the claims must be within the policy's scope of coverage, the settlement demand must be within the policy limits of the policy; and (3) an ordinary, reasonable insurer would accept the terms of the settlement demand when considering the likelihood and degree of the insured's potential exposure to an excess judgment. If the insurance company refuses to pay the policy limits within the time period prescribed in the settlement demand, and the jury verdict is for an amount that exceeds the policy limits, the insurance company is subject to *Stowers* liability and could ultimately have to pay for the entire verdict, including the amount in excess of the policy limits.

Tyger River Doctrine (South Carolina) – *Tyger River Pine Co. v. Maryland Casualty Co*., 170 S.E. 346 (S.C. 1933). In *Tyger River*, the Supreme Court of South Carolina held that an insurer has the duty to settle cases if it deems settling would be the reasonable thing to do. If the insurer fails to settle when reasonable, the *Tyger River* Doctrine provides that the insurer may be liable to both the insurer and the claimant for the amount over the policy that is recovered at trial. According to the *Tyger River* Doctrine, the insurer is bound, under its contract of indemnity, and in good faith, to sacrifice its interests in favor of those of the insured.

Insured's Stipulation to Judgment and Assignment of Rights

Courts across the country have become more and more willing to allow insureds to stipulate to liability and, often times, damages in certain situations. The claimant with the confessed judgment is then permitted to pursue the insurer directly in coverage litigation to enforce the judgments. Below are some of the more well-

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known and widely-used agreements that have been recognized through references to the case in which the concept arose.

Morris and Damron Agreements (Arizona) – These two related legal concepts were among the first to recognize an insured's right to enter into nonrecourse settlements without an insurer's consent.

A *Morris* Agreement stems from *United Servs. Auto. Ass'n v. Morris,* 741 P.2d 246 (Ariz. 1987), and involves a settlement entered into by an insured when an insurer is defending under a reservation of rights. In a "*Morris*" Agreement, the insured stipulates to a judgment, assigns his rights against the insurer to the claimant, and receives in return a covenant from the claimant not to execute against the insured. In permitting such agreements, the Arizona Supreme Court held that an insurer "who performs the duty to defend but reserves the right to deny the duty to pay should not be allowed to control the conditions of payment." *Id.* at 252. Under a *Morris* Agreement, the assignee must establish that the insured acted in bad faith or else the agreement will be a breach of the cooperation clause and the insurer will have no duty to pay the stipulated judgment. *Safeway Ins. Co. Inc. v. Guerrero*, 106 P.3d 1020, 1024 (Ariz. 2005).

A *Damron* Agreement, which stems from *Damron v. Sledge,* 460 P.2d 997 (Ariz. 1969), is similar to a *Morris* Agreement but is entered into in cases in which an insurer has denied coverage rather than providing a defense under a reservation of rights. In permitting such agreements and allowing insureds to stipulate to liability, underlying facts, and damages, the Arizona Supreme Court observed that an insurer that refuses a defense altogether must accept a risk that "an unduly large verdict may result from lack of cross-examination and rebuttal." *Id.* As long as the stipulated judgment is not fraudulent or collusive, an insurer is bound by it "with respect to all matters that were litigated or could have been litigated in that action. *State Farm Mut. Auto. Ins. Co. v. Paynter*, 593 P.2d 948, 950 (Ariz. 1979).

Bashor and Nunn Agreements (Colorado) – A *Bashor* Agreement is a **post-trial** agreement between an insured and a claimant in which the insured agrees

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to: (1) pay a portion of the judgment; (2) pursue the remainder against the insurer through a bad faith claim for breach of the duty to settle; and (3) pay any judgment obtained in the bad faith litigation to the third-party. In exchange, the third-party agrees not to collect on the judgment against the insured. *Northland Ins Co. v. Bashor*, 494 P.2d 1292 (Colo. 1972).

A *Nunn* Agreement is the **pre-trial** version of the *Bashor* Agreement. In a subsequent bad faith case, the claimant must show that the stipulated judgment was "a reasonable reflection of the worth of [the third-party's] injury claims against [the insured]." *Nunn v. Mid-Century Ins. Co.*, 244 P.3d 116 (Colo. 2010). Thus, the particular amount of the stipulated judgment serves as evidence of the value of the claim but not the presumptive value of the actual damages in the bad faith case.

Coblentz Agreement (Florida) - A *Coblentz* agreement is a negotiated consent judgment between an insured and a claimant to settle a lawsuit in which the insurer declined to defend or indemnify. *Coblentz v. American Sur. Co. of New York*, 416 F.2d 1059 (5th Cir. 1969). In exchange for a release from personal liability, the parties establish the insured's liability and assign to the claimant any cause of action the insured has against the insurer. In order to enforce and prevail on the agreement, the assignee must file a lawsuit against the insurer and prove that: (1) the policy covers the damages at issue; (2) the insurer wrongfully refused to defend the insured in the underlying lawsuit; and (3) that the settlement that is the subject to the *Coblentz* Agreement is reasonable and was made in good faith. *U.S. Fire Ins. Co. v. Hayden Bonded Storage Co*., 930 So.2d 686, 690-91 (Fla. 2006); *Chomat v. N. Ins. Co. of NY*, 919 So.2d 535, 537 (Fla. 2006).

Miller-Shugart Agreement (Minnesota) – This legal concept originates from the *Miller v. Shugart*, 316 N.W.2d 729 (Minn. 1982) case and involves situations in which insured's enter into a settlement to avoid liability when an insurer provides a defense under a reservation of rights. A *Miller-Shugart* Agreement is a settlement in which an insured consents to a judgment in favor of the plaintiff on the condition that the plaintiff will satisfy the judgment only out of proceeds from the insured policy of the insured and

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will not seek recovery against the insured personally. Courts have enforced these types of agreements finding that insureds have a right to protect themselves against claims and that insureds have a right to settlement without an insurer's consent when being defended under a reservation of rights.

Truck Insurance (or "537.065") Agreement (Missouri) –Missouri is one of a minority of states that allows an insured to refuse a defense offered under a reservation of rights. In *Truck Ins. Exchange v. Prairie Framing, LLC*, 162 S.W.3d 64 (Mo.App.W.D. 2005), the Court held that if the insured rejects the defense under a reservation of rights, the insurer has three options: (1) defend without a reservation of rights, (2) withdraw from representing the insured in the underlying action, or (3) file a declaratory judgment action to determine the scope of coverage.

The *Truck* case also established that if an insurer unjustifiably fails to defend its insured or if it fails to settle within limits, the insured is free to make a reasonable settlement or compromise without losing the right to recover under the policy and without breaching its duty to cooperate. This concept, often referred to by utilizing the Missouri Statute that codified it, (§537.065 R.S. Mo), has resulted in the execution of "537.065"settlement agreements that stipulate to liability and damages at or below policy limits and, in exchange, the claimant is then permitted to pursue the insurer in coverage litigation.

Other Insurance Coverage Concepts

In addition to the above concepts, below are additional insurance coverage doctrines and principles that arise on a regular basis in states with well-developed insurance coverage case law such.

Buss Rule (California) - In *Buss v. Superior Court*, 939 P.2d 766 (Cal. 1997), the underlying action involved 27 causes of action arising out of various business disputes, only one of which was potentially covered by the liability policies at issue. The insurer accepted the defense of the underlying action but took the

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position that only the defamation cause of action was potentially covered and reserved its right to be reimbursed for defense costs incurred in defending the uncovered claims. After the insurer contributed to the settlement of the underlying action, Buss sued his insurer, claiming that it should have paid for the entire settlement. The insurer filed a cross-complaint, arguing that it had the right to be reimbursed for amounts paid to defend causes of action not covered by its policies. The Supreme Court of California held that an insurer may seek reimbursement of defense costs that can be allocated to the claims that are not potentially covered after the insurer has defended a lawsuit involving mixed claims. *Id*. at 778. In reaching this conclusion, the court stated what is now known as the *Buss* rule: "To defend meaningfully, the insurer must defend immediately. To defend immediately it must defend entirely." *Id*. at 775. The insurer is then entitled to reimbursement for amounts incurred in defending the uncovered claims.

Cumis Counsel (California) – *Cumis* counsel stems from the landmark California decision that established an insured's right to independent counsel paid for by its insurer where a conflict of interest arises when the insurer defends a case under a reservation of rights. *San Diego Navy Fed. Credit Union v. Cumis Ins. Soc'y, Inc*., 208 Cal. Rptr. 494 (Cal. Ct. App. 1984). Citing The State Bar of California's Rules of Professional Conduct, the court held that an insurer is contractually obligated to pay for independent counsel whenever "there are divergent interests of the insured and the insurer brought about by the insurer's reservation of rights based on possible noncoverage under the insurance policy." *Id. at* 506. The California Legislature subsequently enacted California Civil Code § 2860 to codify the concept. The Code provides that a conflict of interest exists when an insurer reserves its rights on a coverage issue and the outcome of that coverage issue can be controlled by defense counsel retained by the insurer. Cal. Civ. Code § 2860(b). If the statute applies, the insured has the right to select independent counsel. The phrase belongs only in California, but it is used in a general sense in other states.

Monstrose (Known Loss) Doctrine (California) – *In Montrose Chemical Corp. v. Admiral Ins. Co*., 913 P.2d 878 (Cal. 1995), the Supreme Court of California

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adopted a continuous trigger for claims for bodily injury and property damage resulting from the insured's disposal of hazardous waste on a continuous basis both before and during Admiral's policy periods. The court held that "[w]here, as here, successive CGL policy periods are implicated, bodily injury and property damage which is continuous or progressively deteriorating throughout several policy periods is potentially covered by all policies in effect during those periods." *Id*. at 904. The court also addressed the loss in progress (known loss) rule because Admiral argued that this rule barred coverage based on the Potentially Responsible Party claim letter Montrose received prior to the inception of the first Admiral policy. The Court held that injury or damage for which an insured may incur liability is not a known loss—and hence uninsurable under basic precepts of insurance law—until liability for the injury or damage has been assessed by a court. After this decision, insurers began to incorporate language in comprehensive general liability policies to exclude coverage for bodily injury or property damage that occurred, in part, before the inception of the policy. This language, frequently called Montrose language, may be found in the insuring agreement or in endorsements and attempts to establish the date that coverage for a continuous injury trigger ends.

Peppers Counsel (Illinois) – This is Illinois' version of *Cumis* counsel in California. *Maryland Cas. Co. v. Peppers*, 355 N.E.2d 24 (Ill. 1976). In *Peppers*, the Court held that an insured has the right to be defended by counsel of its own choice and it has the right to control the defense if a conflict of interest exists between the insurer and its insured, unless, after full disclosure, the insured accepts the insurer's defense or the insurer agrees to defend without a reservation of rights or a waiver of its noncoverage defenses. The insurer must reimburse its insured for the reasonable cost of its independent counsel. In *Peppers*, a conflict existed because in the underlying lawsuit the insured could be held liable on either negligent or intentional act claims and the policy only afforded coverage for the negligence claim.

Peppers Doctrine (Illinois) – This doctrine, which arises from the same *Peppers* case decided by the Illinois Supreme Court referenced above, stands

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for the proposal that it is generally inappropriate for a court considering a declaratory judgment action to decide issues of ultimate fact that could bind the parties to the underlying litigation. The application of the *Peppers* Doctrine often results in the staying of declaratory judgment actions to allow the underlying litigation at issue to proceed in order to avoid the potential collateral estoppel effect that resolution of issues in the declaratory judgment action could have in the underlying action. By way of example, in *Peppers*, the court held that the trial court's ruling that the injury at issue was intentional was one of ultimate fact that could bind the parties to the underlying litigation. *Id*. at 29-30.

Mighty Midgets Rule (New York) – This oddity in New York law stems from a 1979 decision issued by the New York State Court of Appeals in *Mighty Midgets v. Centennial Ins. Co.*, 47 N.Y.2d 12 (1979). The rule stands for the proposition that a prevailing insured in a declaratory judgment action against its insurer for breach of the duty to defend is only entitled to recover its attorney's fees if it is the defendant in the case. In other words, whether an insured can recover its attorney's fees in a declaratory judgment action is dependent upon which side of the "v" it finds itself.

White Waiver (California) – A *White* Waiver is an agreement used by insurance companies to protect against allegations of bad faith arising from settlement negotiations in situations where other protections, such as state and federal evidentiary laws, may not apply. The concept stems from *White v. Western Title Insurance Company*, 710 P.2d 309 (Cal. 1985) where the Supreme Court of California found that an insurer may be liable for bad faith conduct which takes place during litigation between an insured and his/her insurer. Insurers now request that insureds sign White Waiver agreements that provide that settlement discussions are kept private and that the conduct of the insurer in settlement discussions cannot be used to establish bad faith against an insurer.

Wilton/Brillhart Abstention Doctrine – The United States Supreme Court held in *Wilton v. Seven Falls Company*, a diversity action, that a standard of

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> substantial discretion governed a district court's decision to stay a declaratory judgment action on grounds of a parallel state court proceeding. 515 U.S. 277 (1995). This discretion is conferred upon the federal courts by the permissive language of the Declaratory Judgment Act. 28 U.S.C. § 2201(a). In *Wilton,* the Supreme Court reaffirmed *Brillhart v. Excess Insurance Company*, which stated that district courts are "under no compulsion" to entertain claims of declaratory relief, since they possess discretion to exercise their jurisdiction under the Declaratory Judgment Act. 316 U.S. 491 (1942). The *Brillhart* doctrine, applicable to declaratory judgment actions, gives the district court broader discretion to determine "whether and when to entertain an action under the Declaratory Judgment Act, even when the suit otherwise satisfies subject-matter jurisdictional prerequisites. Insured's often raise the *Wilton/Brillhart* doctrine to seek the staying or dismissal of federal declaratory judgment actions when a parallel state court action addressing the same coverage issues is pending.

Although the above-cited cases and legal doctrines are by no means an exhaustive list of all of the insurance coverage principles known colloquially by their case names, they do represent some of the more well-known and widely-used concepts that insurance coverage professionals should familiarize themselves with if they handle claims or provide coverage advice across the country.

This concepts index is not intended to contain legal advice or to be an exhaustive review. If you have any questions about insurance coverage key concepts and terms, please contact Christopher P. Ferragamo or Susan Knell Bumbalo at Jackson & Campbell, P.C.