

How to Write Reservation-of-Rights Letters Rightly and How to Respond to Them

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How to Write Reservation-of-Rights Letters Rightly and How to Respond to Them

Robert O. Lamb¹

I. SCOPE OF ARTICLE

In handling liability claims, an insurer must often determine whether to provide a defense to its insured. When a defense is tendered, two more issues arise: (1) whether the insurer should reserve its right to take back its agreement to defend under certain circumstances; and (2) whether the insurer should reserve its right to deny an indemnity claim at a later date. Though these issues are common, there remains considerable confusion about an insurer's duties in these situations.

In hopes of clearing up some of the confusion, this paper is written with four types of lawyers in mind:

- **The most junior lawyer in the insurance-defense firm.** as a practical matter, that lawyer is the one usually asked to draft a reservation-of-rights letter, or to evaluate such a letter already in the claim file. That attorney may have little understanding of the task at hand. This paper tries to serve as a road map.
- **The more senior lawyer in the insurance-defense firm.** Such a lawyer should be offering advice on the drafting or evaluation of a reservation-of-rights letter. This paper hopefully will help.
- **The lawyer for the policyholder.** Just like the lawyer for the insurance company, the policyholder's lawyer may have to evaluate the adequacy of a reservation-of-rights letter received by the policyholder as that lawyer guides the client through an insurance-coverage dispute. This paper tries to provide a yardstick.

¹ The author routinely represents insurers in coverage disputes and litigation. The views expressed are his own and not necessarily those of his firm or his clients. The author gives great thanks to his friends and law partners, Brian Martin and Jamie Carsey of Thompson Coe's Houston office, and Rick Harmon, Jennifer Aufricht, and Jo Allison Stasney of the Dallas office, whose papers form the foundation for this presentation.

- **The appointed-defense counsel.** An insurer’s reservation of rights will present peculiar issues for the defense attorney appointed by the insurer to defend the insured. There is little guidance as to how a defense attorney should resolve these issues. This paper raises questions for the defense counsel’s consideration and suggests some possible approaches to resolving them.

II. WHY RESERVE RIGHTS?

A. To Warn of Possible Uninsured Exposure

Liability insurance policies normally present the carrier with two distinct duties:

- the duty to defend its insureds from claims by third parties; and
- the duty to pay covered claims.

The duty to defend is often described as “broader” than the duty to indemnify, i.e., the duty to pay.² This is for two primary reasons. First, as recently explained by the Texas Supreme Court, the duty to defend is determined solely by the eight-corners rule:

[C]ourts look to the facts alleged within the four corners of the pleadings, measure them against the language within the four corners of the insurance policy, and determine if the facts alleged present a matter that could potentially be covered by the insurance policy.³

“The factual allegations must be considered without regard to their truth or falsity and all doubts regarding the duty to defend are resolved in the insured’s favor.”⁴ Second, if a complaint potentially includes a covered claim,

² *Zurich Am. Ins. Co. v. Nokia, Inc.*, 268 S.W.3d 487, 490 (Tex. 2008).

³ *Ewing Constr. Co., Inc. v. Amerisure Ins. Co.*, 420 S.W.3d 30, 33 (Tex. 2014).

⁴ *Id.* (citing *Zurich v. Nokia*, 268 S.W.3d at 491).

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