UT LAW CLE THE UNIVERSITY OF TEXAS SCHOOL OF LAW

PRESENTED AT

26th Annual Admiralty and Maritime Law Conference
South Texas College of Law

September 29, 2017
Houston, TX

Mediating the Maritime Claim When Insurance Coverage is in Dispute

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Achieving settlement through mediation is challenging enough when a dispute exists simply between a claimant and defendant. And because mediation has become virtually an indispensable stage of litigation–often as a required step in a court-order docket control schedule–most litigators have developed favored mediation strategies based on personal experiences.

Mediation becomes rather more complicated when an insurer rather than the nominal defendant controls the litigation defense, so that the insurer determines whether to settle, when to settle, and how much to pay in settlement on behalf of its insured-defendant. The defendant doesn't always agree with its insurer's assessment.

The complications become even more apparent when the insurer also issues a "reservation of rights" indicating to the insured-defendant that– although the insurer is required and entitled to defend the suit– the insurer may not be liable to pay an eventual settlement or judgment. The significance of these reservations can run a spectrum from boilerplate protection against outcomes nobody realistically anticipates, to full-on conflicts of interest where the insured-defendant is entitled to appoint and direct independent counsel to represent it in the litigation.

The range of mediation strategies can be significantly affected, depending on how deeply the risks and interests of insurer and insured-defendant diverge. In many of these situations, reaching a settlement of the underlying claim also requires resolution of disagreements between the insurer and insured-defendant about the insurance coverage. Indeed, often it is just as important for the underlying claimant to understand and reach resolution of the coverage issues, as a predicate for accurately evaluating and resolving claims asserted in the underlying suit.

I. You might need coverage counsel for mediation if . . .

Involvement of specialized coverage counsel can be helpful in reaching a consolidated settlement with the insurer and underlying claimant. This is particularly true where the insurance program or coverage issues are particularly important or complicated, and where insurance limits are the principal source for settling the underlying claims.

The need for and role of coverage counsel is greatly affected by the initial coverage position taken by the insurer. In the context of third-party liability insurance, those positions fall into some identifiable categories: (i) where the insurer is defending without coverage issues and no reservations; (ii) where the insured-defendant is negotiating with claimant and insurer under a Stowers demand; (iii) where insurer is defending under a reservation of rights; and (iv) where the insured-defendant seeks independent counsel due to conflicts of interest raised by insurer's reservations.

A. When the insurer defends without reservation

Standard third-party liability insurance policies provide that an insurer is obligated and entitled to control the defense and settlement of the suit. The insurer enjoys discretion to conduct negotiations and reach settlement with the claimant within policy limits, regardless whether the insured-defendant agrees. Texas jurisprudence generally supports this contractual empowerment of the insurer, where no conflict of interest otherwise prevents the insurer from acting in place of the insured. *State Farm Mut. Auto. Ins. Co. v. Traver*, 980 S.W.2d 625, Tex 1998). In this ordinary situation, then, the insurer conducts negotiations directly with the claimant whether in mediation or informally, and simply provides notice of any settlement to the insured-defendant, with no intruding coverage issues.

Sometimes the insured-defendant believes the risk of liability or extent of damages is greater than the insurer appreciates, and the insurer should pay more to reach settlement. Or conversely, the insured-defendant may believe it has little or no liability to the claimant, and disagrees with the insurer's willingness to settle with the claimant within the policy limits, because it may be interpreted as an admission of fault, resulting in stigma or unwelcome precedent affecting the insured's public goodwill or operations going forward.

Particularly where the insurer and insured-defendant enjoy a long commercial relationship, the insurer and insured-defendant might work out these differences and agree on a mutually satisfactory strategic approach for negotiating a settlement with the underlying claimant. Disputes over the reasonable amount to pay for settlement are especially susceptible to resolution if the defense lawyer is known to and trusted by both insurer and insured-defendant, and the lawyer's professional judgment supports a particular assessment of liability and damage.

Separate coverage counsel is seldom necessary and may even be an obstacle to resolving such disagreements. And these sorts of disagreements rarely affect mediation, most pointedly because the insurer ultimately is entitled to drive that process and make those decisions notwithstanding an insured-defendant's protestation. So long as the claim and settlement is within policy limits and the insurer accepts coverage, there is seldom a separate insurance aspect that needs to be addressed in mediation of the underlying matter.

B. When there is (or may be) a Stowers demand

But regardless of contractual entitlement, whenever the insurer exercises its right to defend litigation and control settlement, the insurer must exercise that right non-negligently. Where the insurer violates this rule by failing to take the opportunity to secure a reasonable settlement, the insurer can become liable for a judgment even exceeding the policy limits.

This is the so-called "Stowers" doctrine, based on the common sense rule that an insurer should

Title search: Mediating the Maritime Claim When Insurance Coverage is in Dispute

First appeared as part of the conference materials for the
26th Annual Admiralty and Maritime Law Conference session
"Mediating the Maritime Claim When Insurance Coverage is in Dispute"