White and Williams LLP

ALI Restatement of the Law of Liability Insurance: Lessons Learned After Three Years

By: Sara C. Tilitz
11.2.21

Since the American Law Institute (ALI) voted in May 2018 to approve the final draft of its Restatement of the Law of Liability Insurance (RLLI), many have closely watched to see what impact, if any, the RLLI might have on the insurance coverage landscape. On October 4, 2021, Randy Maniloff of White and Williams, co-author of *General Liability Insurance Coverage – Key Issues in Every State* (5th edition), hosted a webinar titled "ALI Restatement of the Law – Liability Insurance: Lessons Learned After Three Years." The presentation, which was attended by over 500 members of the insurance community, provided an objective, evidence-based examination of the impact of the RLLI in judicial decisions to date and potentially going forward. Mr. Maniloff's in-depth presentation touched on numerous points about the past, present, and future of the RLLI; a few of his key themes are highlighted below.

The Past

At the outset, Mr. Maniloff recounted the battle over the drafting of the RLLI between insurance industry professionals on one side and policyholder representatives on the other. Mr. Maniloff theorized that this contentious history stemmed from the RLLI being the only Restatement that involves an "industry" with millions (if not billions) of dollars possibly at stake. Additionally, insurance coverage has long been a field with established bars – one representing policyholders and another representing insurers. Thus, a mechanism was in place for a battle over the RLLI to ensue. During the drafting process, insurer-side predictions on the effect of the RLLI warned of potentially devastating outcomes, including rate increases, risk of insolvencies, claim paying impairment, and market exits. Thankfully, as we will explore here, seemingly none of those forecasts have or will come to pass.

The Present

In Mr. Maniloff's view, there has been virtually *no impact* of courts' use of the RLLI in decisions and, although opportunities for possible future impact do exist, they will likely be minimal. By Mr. Maniloff's count, only approximately 60 insurance cases out of tens of thousands issued since the RLLI project began have cited to the RLLI. In general, this small subset of decisions cite to the RLLI (1) for a statement of a general, non-controversial principle of coverage law; (2) to point out that the RLLI is consistent with controlling state law; or (3) in a small number of cases where the RLLI had a role in the decision, but it did not hinge solely on the RLLI. This outcome is in stark contrast to fears voiced during the process of drafting the RLLI. Mr. Maniloff credited this result largely to the fact that insurance law is generally well settled. Thus, few opportunities exist for a court to be lacking guidance and have a need to turn to RLLI for assistance.

As to those instances where the RLLI was relied upon for well-established principles or controlling state precedent, Mr. Maniloff highlighted several cases showing the uncontroversial nature of these decisions. For example, in 2015, the Tenth Circuit cited to the then-draft RLLI for the proposition that, where a complaint alleges facts that would, if true, give rise to covered liability, an insurer must defend. *Hanover Am. Ins. Co. v. Balfour*, 594 Fed. Appx. 526, 543 (10th Cir. Jan 16, 2015) (applying Oklahoma law) (citing § 15 of *Principles of Law, Liability Insurance*, Tentative Draft No. 2 (revised) (July 23, 2014)). A Delaware state court cited to the RLLI shortly after approval for the proposition that the burden of proof is on the insurer to prove an exclusion. *Akorn, Inc. v. Fresenius Kabi AG*, No. 2018-0300, 2018 Del. Ch. LEXIS 325 (Del. Ct. Ch. Oct.1, 2018). And most recently, the Vermont Federal District Court cited to the RLLI for the premise that occurrence-based policies generally are subject to a notice-prejudice rule, while a claims-made insurer need not prove prejudice from late notice to deny coverage. *Inn One Home v. Colony Specialty Ins. Co.*, 2021 U.S. Dist. LEXIS 33451, at *20

(D. Vt. Feb. 23, 2021) (citing RLLI § 35(2)).

In those cases where a court cited to the RLLI for a substantive purpose or the RLLI played a role in the outcome of a decision, Mr. Maniloff believes that the holdings would have been identical notwithstanding the RLLI. Citing the draft RLLI in 2017, an Indiana Federal District Court held that reimbursement of defense costs where no defense was owed was improper. In reaching its decision, the court cited RLLI § 21, which states that defense cost reimbursement is inappropriate unless specifically provided for in the policy. *Selective Ins. Co. of America v. Smiley Body Shop, Inc.*, 260 F. Supp. 3d 1023 (S.D. Ind. 2017). But according to Mr. Maniloff, the citation to the RLLI was simply for additional support for an already decided outcome in Indiana and "in no way, shape or form caused the insurance company to lose this case."

In what Mr. Maniloff described as the case where the RLLI "had the chance to be the most significant" authority in the outcome, the Nevada Supreme Court cited to RLLI § 48 for the proposition that a policyholder is entitled to incidental and consequential recovery beyond policy limits when the insurer breaches the insurance contract. *Century Surety Co. v. Andrew*, 432 P.3d 180 (Nev. 2018). In adopting the minority rule, that the insurer's liability can exceed the limits when the insurer did not act in "bad faith," the Nevada high court fell in line with the RLLI, but Mr. Maniloff believes the same result would have been reached regardless of the court's citation to the RLLI.

What's more, in many instances in which the RLLI was cited in decisions, the courts actually *declined* to follow the RLLI in favor of established state precedent. For example, directly in contrast to the outcome in *Smiley Body Shop*, a Delaware state court applying Tennessee law rejected the RLLI's position on reimbursement of defense costs. Instead, relying solely on an eleven-year-old Tennessee federal court decision (the only on-point Tennessee decision in existence), the court found for the insurer and held that reimbursement of defense costs was proper. *Catlin Specialty Ins. Co. v. CBL & Assocs. Props.*, 2018 Del. Super. LEXIS 342 (Del. Super. Ct. Aug. 9, 2018). Similarly, in ruling that coverage defenses are not waived merely because an insurer breaches its duty to defend, a Pennsylvania Federal District Court (applying New York law) rejected the RLLI's view and instead applied a precedential decision from New York's highest court. *Catlin Specialty Ins. Co. v. J.J. White, Inc.*, No. 14-1255 (E.D. Pa. Feb. 27, 2018).

The Future?

Although the RLLI has had limited influence on the insurance coverage law landscape, Mr. Maniloff suggested that courts may yet look to the RLLI in circumstances where (1) there is limited case law; (2) case law exists nationally, but the relevant state law is silent; (3) some relevant case law exists in a jurisdiction, but no clear rule has emerged; (4) a court finds guidance in the RLLI when addressing a nuance; or (5) there is a novel issue to be decided. In particular, Mr. Maniloff identified certain issues where opportunities remain for a court to turn to the RLLI for guidance, including insureds' rights to independent counsel, reimbursement of defense costs, insurer liability for conduct of appointed defense counsel, and the effect of reservations of rights (RORs) on settlement rights and duties.

In closing, Mr. Maniloff warned of possible landmines where the RLLI could impact insurers. These include: (1) circumstances in which insurers should issue follow-up RORs – specifically the RLLI comment that the insurer be aware of developing details of a claim, including those that emerge during discovery; (2) the effectiveness of RORs – the RLLI's adoption of the "fairly informed standard," which provides that an insurer's reservations of rights letter include an explanation of the policy terms and allegations or facts that support all potential grounds for contesting coverage; (3) scope of the right to defend/confidentiality – the insurer has the right to receive from appointed defense counsel everything relevant to the defense of the action but not information that could be used to "benefit" the insurer at the expense of the insured, which may put defense counsel in a difficult position; (4) damages for breach of the duty to defend whereby an insurer's liability for breach of the duty to defend can exceed the policy limits (the *Andrew* case above); and (5) damages for failure to make "reasonable settlement decisions" – if a verdict in excess of a "reasonable settlement" results in punitive damages, those damages may be covered regardless of the lack of coverage for punitive damages otherwise.

Conclusion

Although it is not clear whether the current trend of minimal impact of the RLLI will persist, it is safe to say that the liability insurance community will continue to monitor the situation closely, particularly with respect to the hot-button issues identified by Mr. Maniloff.