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Indiana Supreme Court Sets Up Future Coverage Battles Over Allocation, Defense Costs

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The Indiana Supreme Court recently declined to accept jurisdiction over a major insurance coverage dispute, leaving intact an Indiana Court of Appeals opinion that may now become a landmark decision on a number of insurance coverage issues in Indiana. The Supreme Court's declination of jurisdiction over *Thomson, Inc. v. Ins. Co. of N. America*, 11 N.E.3d 982 (Ind. Ct. App. 2014), on May 15, could have far-reaching effects that are helpful to policyholders in some respects, and potentially contrary to policyholders' interests in others. *First, the good:* The Supreme Court left intact the Court of Appeals' adoption of a policyholder-friendly test for determining whether defense costs are reasonable and necessary, and thus owed by the carrier as part of its duty to defend. The Court of Appeals adopted a "market-tested" analysis for determining the reasonableness of defense costs. Under this analysis, if the policyholder incurred and paid defense costs under circumstances where reimbursement from a carrier was uncertain, those costs are "market-tested," and are presumed to be reasonable. The court also affirmed the trial court's adoption of the policyholder's evidence that the overall amount of defense costs incurred was commensurate with the complexity of the defense and the skill and experience of the defense attorney, rather than the carrier's downwardly-biased, line-by-line approach. The Supreme Court and Court of Appeals also left intact the trial court's ruling that costs incurred in affirmatively pursuing contribution claims against other liable parties are included in the carriers' obligation to pay defense costs. These rulings provide Indiana policyholders with powerful tools to combat common insurer tactics designed to minimize their defense obligations at the expense of the policyholder. The Supreme Court also left intact a number of other Court of Appeals rulings reinforcing policyholder-friendly Indiana law on a variety of coverage issues, including:

- the availability of personal injury coverage for environmental liabilities, in addition to bodily injury/property damage coverage;
- the insurer's inability to deny coverage based on late notice unless it was actually prejudiced;
- and the insurer's inability to deny coverage based on the "known loss" doctrine unless the policyholder had actual knowledge of a liability before the policy was issued.

Now, the bad: The Supreme Court also left intact the Court of Appeals' adoption of pro rata allocation of covered damages in suits alleging latent injuries incurred over a long span of time. Under pro rata allocation, each

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carrier's obligation is limited to only a portion of the entire liability based on the number of years it provided insurance. This exposes the policyholder, in some instances, to the risk of having to pick up a significant chunk of the tab for an otherwise-covered liability. The adoption of pro rata allocation is a drastic departure from longstanding Indiana law holding that each carrier that insured a policyholder during the entire latent injury period is responsible for the entire liability. For a more in-depth explanation of this issue, see my April 10 post entitled "Indiana Supreme Court Hears Oral Argument on Significant Allocation Issue." While this ruling was adverse to policyholders, its full effects will not be known until its outer boundaries are determined in subsequent coverage disputes. In the meantime, policyholders have numerous arguments available to try to limit the scope and reach of the ruling. For example, policyholders still may argue that:

- Pro rata allocation is limited to the standard language appearing in post-1986 liability policies, and does not overturn existing Indiana law governing pre-1986 policies, which still afford coverage, within policy limits, for the entire long-tail liability.

- Even post-1986 liability policies that do not contain the specific language relied upon by the court may still afford coverage for the entire long-tail liability, rather than just a pro rata share.

- Pro rata allocation applies only to the duty to indemnify, and does not apply to the duty to defend. Each carrier still owes a duty to provide a complete defense under Indiana law, even if it owes only a pro rata share of the damages.

- Periods for which coverage is unavailable or excluded (in other words, periods for which the policyholder might be responsible for picking up a pro rata share) should be excluded from the allocation, increasing the carriers' shares.

- The policyholder's obligation to pay a deductible or retention in a triggered policy year should be limited to a pro rata share of that deductible or retention, rather than the full amount, minimizing the policyholder's contribution and increasing the carriers' shares.

In summary, policyholders can expect carriers to exploit *Thomson*'s pro rata allocation ruling by attempting to slash their policy obligations, even where they have acknowledged coverage. Policyholders, however, have numerous arguments available, in the appropriate case, to fight back and limit or avoid *Thomson*'s adverse effects. Additionally, policyholders can affirmatively use *Thomson*'s "market-tested" approach for determining the reasonableness of defense costs to maximize defense cost recoveries from their carriers. Understanding your rights on these issues may help you to get full benefit of your coverage and prevent a carrier from unfairly limiting its obligations at your expense.