An Expanding View On Satisfying The Self-Insured Retention

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Recent insurance coverage decisions have reminded insurance companies that, absent incredibly clear language otherwise, inconsequential requirements dictating satisfaction of self-insured retentions (SIRs) will not be enforced. As long as the insurer receives a "credit" equal to the amount of the SIR, courts have been reluctant to enforce requirements as to *who* pays the SIR or even *whether* the SIR gets paid. This makes sense. Insurers are responsible only for the amount in excess of an SIR; thus, it should make no difference *who* pays the SIR or even *whether* the SIR is paid. Either way, the insurer maintains the benefit of the SIR. Many liability policies require that the insured satisfy an SIR before the insurer's duty to defend and indemnify can be triggered. The language of the SIR provisions often requires that "the insured" or "you" satisfy the SIR. Insurers have used this language as an opportunity to argue that no *other* party can satisfy the SIR—the insured must satisfy the SIR out of its "own pockets." Courts are not moved by these seemingly inconsequential distinctions. As a recent example, in a dispute before the Florida Supreme Court, the insurer cited fairly typical policy language to argue that a subcontractor's indemnity payments to the contractor could not satisfy the contractor's SIR. The policy language included:

> We have no duty to defend or indemnify unless and until the amount of the "Retained Limit" is exhausted by payment of settlements, judgments, or "Claim Expense" by you. The "Retained Limit" will only be reduced by payments made by the insured. The payment of the "Retained limits" by the insured is a condition precedent for our obligation to pay any sums either in defense or indemnity.

The lower court agreed with the insurer—finding that these provisions *unambiguously* required satisfaction of the SIR by the insured's own funds. The Florida Supreme Court disagreed and held that the policy "allows the insured to apply indemnification payments received from a third party toward satisfaction of its $1 million self-insured retention." The Court made an important distinction in rejecting the insurer's arguments:

> The language of the instant [] policy states that the retained limit *must be paid by the insured*, but *does not specify where those funds must originate*. Requiring payment to be made from the insured's "own account" is not necessarily the same as requiring that it be paid "by you."

Moreover, Courts have consistently held that, absent clear language to the contrary, the failure of an insolvent or bankrupt insured to fund a SIR will not excuse the insurer's performance under the insurance policy for amounts in excess of the SIR. To the contrary, many insurance policies explicitly state that bankruptcy or insolvency of the insured will *not* relieve the insurer of its obligations under the policy. Otherwise, an insured's insolvency would

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automatically relieve the insurer of its coverage obligations—a result directly contradicting most insurance policies and public policy.

> To illustrate: If an insolvent insured with $5 million in coverage and a $500,000 SIR receives a $3 million judgment, the insurer should not be able to escape its $2.5 million liability merely because the insolvent insured cannot fund the $500,000 SIR. The insurer should receive credit for the $500,000 SIR, yet still cover the $2.5 million.

For example, in the recent case *Phillips v. Noetic Specialty Insurance Company*, 919 F. Supp. 2d 1089 (S.D. Cal. 2013), a California court completely rejected the insurer's argument that payment of the SIR was a condition precedent to coverage. The insurer relied on a SIR provision, stating that the insurer "will pay those sums, in excess of the 'self-insured retention,' that the insured becomes legally obligated to pay," to argue that satisfaction of the SIR was a necessary condition to the insured having a contractual claim and to argue that an SIR is akin to primary insurance coverage, and, thus, coverage is not triggered until the SIR is exhausted. The court disagreed, as this contention directly contradicted the policy provision that "[b]ankruptcy or insolvency of the insured or of the insured's estate will not relieve us of our obligations under this policy." As the court noted, the insurer "had the opportunity to include terms requiring payment of the SIR to serve as a condition precedent to coverage, but failed to do so. As such, the Court will not create such an obligation where it does not already exist." This is a great reminder for policyholders to carefully examine their policy language and consider the relationship between policy provisions. Policyholders should push back against coverage denials based on seemingly inconsequential or irrelevant matters, such as *who* satisfies the SIR or even *whether* the SIR is satisfied. Public policy does not support insurance companies escaping their coverage obligations because of miniscule matters that, in the end, make little to no difference.