

Federal Courts Reject Insurers' Attempts to Recoup Defense Costs Expended Under Reservation of Rights

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Insurance Coverage and Bad Faith Alert
4.4.22

In situations where there is a dispute over a duty to defend, an insurer may provide a defense to its insured, subject to a reservation of rights, to not only deny coverage for a defense, but also to file a declaratory judgment action and recoup defense costs in the event it is determined there is no duty to defend. But are defense costs recoupable? Last week, federal trial courts in Georgia and Pennsylvania answered this question with a resounding "no".

In *Chemical Equipment Labs, Inc. v. Travelers Property Casualty Company of America*, Case No. 19-3441, 2022 U.S. Dist. LEXIS 61298 (E.D.Pa. Mar. 31, 2022), the United States District Court for the Eastern District of Pennsylvania was called to determine whether Travelers Property Casualty Company of America (Travelers) was entitled to reimbursement of defense costs after it was determined that it had no duty to defend its insured in an arbitration for breach of a charter agreement. The Travelers' policies did not contain an express reimbursement provision. The court found that Travelers was not entitled to reimbursement because under Pennsylvania law, "[r]eimbursement of defense costs requires an express provision in the written insurance contract."

Similarly, in *Mt. Hawley Insurance Company v. East Perimeter Pointe Apartments LP*, Case No. 20-cv-3529, 2022 U.S. Dist. LEXIS 61885 (N.D. Ga. Apr. 1, 2022), the United States District Court for the Northern District of Georgia considered whether Mt. Hawley Insurance Company (Mt. Hawley) was entitled to reimbursement of defense costs after it was determined that it had no duty to defend its insured against a lawsuit for negligent management and security. Mt. Hawley's reservation of rights explicitly reserved the right to seek reimbursement of defense costs in the event it was determined that there was no coverage available under its commercial general liability policy; however, the policy did not contain a reimbursement provision.

The *East Perimeter* court acknowledged that the recoupment of defense costs in the absence of an express reimbursement provisions was an unsettled issue in Georgia, as "Georgia courts have not decided the issue and federal courts are split." In *Illinois Union Insurance Company v. NRI Construction, Inc.*, 846 F. Supp. 2d 1366 (N.D. Ga. 2012), the court permitted reimbursement, finding it was justified under an unjust enrichment or implied in fact contract theory. However, in *American Family Insurance Company v. Almassud*, 522 F. Supp. 1263 (N.D. Ga. 2016), the court required an express reimbursement provision in the contract, finding that "if a right to recoupment is a benefit that the insurer deems sufficiently important, it can easily secure that right by including it in the policy agreement."

The *East Perimeter* court ultimately concluded that *Almassud* was more persuasive, on the basis that permitting a right to recoupment absent a policy provision would permit insurers to unilaterally impose post hoc conditions on their contractual obligations.

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