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Policyholder Rights Under Seige In Illinois

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A bill pending in the Illinois Senate threatens to undermine if not overturn two fundamental rights of policyholders under a policy with the duty to defend: (1) the right to a complete defense of an entire claim insured if any allegation is actually or potentially covered and (2) the right to independent counsel if there is a conflict of interest between the insurance company that pays for the defense and the policyholder being defended. Both of these rights have been established for decades by courts in Illinois and virtually every other state. *See, e.g., Maryland Casualty Co. v. Peppers*, 64 Ill.2d 187, 197-98, 355 N.E. 2d 24 (Ill. 1976). Illinois Senate Bill 1296 threatens to turn these bedrock principles into quicksand. First, the bill vests almost complete discretion in the insurer to determine whether there is a "significant and actual conflict of interest" triggering the right to independent counsel. Second, the bill requires the insurer to send the policyholder a list of three lawyers, and while an amendment to the bill allows the policyholder to choose a lawyer not on the list, the insurer can require any selected lawyer to follow the insurer's guidelines. Those guidelines often require counsel to get specific approval in advance from the insurance company for almost every task or strategic maneuver the lawyer performs. Guidelines of this sort are already controversial because they can compromise a lawyer's professional judgment on behalf of an insured client. Those concerns are exacerbated when the insurer has a conflict of interest. A lawyer required follow the insurer's guidelines may not really be independent at all. Third, the bill provides that the insurance company need not pay for the defense of claims "properly denied" and requires the independent counsel to keep detailed records allocating the fees and expenses accordingly. For example, if one count of a complaint is covered and another is not, the insurer would pay for the defense only of the covered count. This turns on its head the established rule that the insurer must defend the entire case if any allegation is even potentially covered and (in most states) may not recoup from the policyholder the cost of defending a portion of the case that turns out not to be covered. Some policies, such as directors and officers (D&O) liability policies, expressly provide for allocation of defense costs between covered and non-covered claims. That's fine. But most commercial general liability (CGL), automobile, homeowners, and other policies do not. Insurance companies wrote and policyholders purchased those policies knowing that the duty to defend encompasses the entire case, including non-covered claims. The Illinois bill apparently would rewrite untold numbers of existing insurance policies, creating an incalculable windfall for insurance companies. The bill also seemingly would insert an allocation provision into future policies, but only by statutory implication and without disclosure to the policyholder. The Illinois bill is partially and loosely based on the California Independent Counsel Statute, Civil Code section 2860. The California statute, enacted in

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response to *San Diego Navy Federal Credit Union, et al. v. Cumis Ins. Society, Inc.,* 162 Cal.App.3d 358 (1984), sets minimum qualifications of independent counsel, allows the insurer to pay only the normal billing rates it pays to other attorneys in similar matters, and requires independent counsel and the policyholder to keep the insurance company informed about the case. The Illinois bill does all of that and much more. It is the “much more” that concerns us. If enacted into law, the bill may deprive corporate and individual policyholders of some of the most basic and important protections of policies they already purchased and will purchase in the future. The bill can be found here. From that link, you can check the bill’s status, its sponsor and the list of Illinois state senators on the committee responsible for the bill.