6 INSURERS' DUTY TO DEFEND, RESERVATIONS OF RIGHTS, AND THE DUTY TO APPOINT INDEPENDENT COUNSEL

The Alaska Supreme Court has held that liability insurers have separate duties to defend and to indemnify their insureds. The duty to defend is broader than the duty to indemnify.[54] The duty to defend arises "if the complaint on its face alleges facts which, standing alone, give rise to a possible finding of liability covered by the policy."[55] If the complaint does not contain such allegations, there is a duty to defend where "the true facts are within, or potentially within, the policy coverage and are known or reasonably ascertainable to the insurer."[56]

In fact, in a case in which the Alaska Supreme Court assumed that the trial court's instructions to the jury were valid (because the insurer did not argue that the instructions misstated the law), the court accepted the principle that an insurance company investigating a claim has an affirmative duty to diligently search for evidence supporting coverage for the claim. The jury instruction in question told the jury that, if the insurer merely seeks to discover evidence that defeats the claim, it holds its interests above the interests of its insured.[57]

In cases where the insurer asserts either policy or coverage defenses, and defends its insured under a reservation of rights, the Alaska Supreme Court has held that there are various conflicts of interest between the insurer and the insured. For example, where the insurer knows it can later assert non-coverage, it may only go through the motions of defending, or it may defend in such a way as to increase the likelihood of a verdict on an uninsured claim versus a covered claim. These conflicts require the insurer to surrender its right to control the defense whenever the insured refuses to accept the insurer's reservation of rights.[58] Consequently, when the insurer wishes to reserve its rights, and doing so creates a conflict of interest, then the insurer must allow the appointment of independent counsel to defend the insured. The independent counsel is selected by the insured.

Guidelines regarding the duty to appoint independent counsel were codified by the Alaska legislature in 1995 at AS 21.89.100. AS 21.89.100(b) provides that

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[54] *Sauer v. Home Indem. Co.*, 841 P.2d 176 (Alaska 1992).

[55] *Afcan v. Mutual Fire, Marine & Inland Ins. Co.*, 595 P.2d 638, 645 (Alaska 1979).

[56] *National Indem. Co. v. Flesher*, 469 P.2d 360, 366 (Alaska 1970); *see also Fejes v. Alaska Ins. Co.*, 984 P.2d 519, 522 (Alaska 1999).

[57] *Great Divide Ins. Co. v. Carpenter*, 79 P.3d 599 (Alaska 2003).

[58] *CHI of Alaska v. Employers Reins. Corp.*, 844 P.2d 1113 (Alaska 1993).

reservations of rights regarding policy limits, punitive damages, or the fact that the insurer denies coverage for some of the claims in the action do not create conflicts of interest. Notwithstanding subsection (b), if the insurer reserves its rights on an issue for which coverage is denied, the insurer shall provide independent counsel to the insured.

Where the reservation creates a conflict of interest, insurers may require that independent counsel have at least four years' experience in civil litigation, including defense experience in the general subject area at issue. The insurer may also require independent counsel to have malpractice insurance. The insurer's obligation to pay the independent counsel's fee is limited to the rate paid by the insurer to defense attorneys in similar actions in the community where the action is being defended.

In cases where independent counsel must be appointed, independent counsel and the insured are obligated to consult with the insurer regarding the civil action and must disclose to the insurer all information relevant to the civil action, except information that is privileged and relevant to disputed coverage. Both independent counsel and the counsel representing the insurer shall be allowed to participate in all aspects of the civil action. The insured may waive the right to select independent counsel by signing a statement as prescribed in the statute.[59]

In cases involving intra family torts (e.g., child suing parent for injuries caused by parent's negligence) the Alaska Supreme Court has held that the parent's liability insurer is the real party in interest and that the insurer's interest in the action should be disclosed to the jury in order to allow the jury to fully and fairly evaluate the case and the testimony and to prevent undue confusion or prejudice.[60] Because of the court's concern that, in a lawsuit among family members, there is a danger of fraud and collusion (such that the defendant-insureds might stand to gain monetarily from an adverse verdict funded by the insurer) the court held that negligent tortfeasors must be prevented from sharing in any award resulting from their conduct. This is true whether the negligent person would have benefited directly, as a specified beneficiary under the wrongful death statute, or indirectly through intestate succession. However, this rule does not result in a reduction of the damage award by the pro rata share otherwise payable to the negligent party. Instead, ineligible beneficiaries are deemed to have renounced their right to recovery.

Appendices:

AS 21.89.100

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[59] *See* AS 21.89.100(f).

[60] *Myers v. Robertson*, 891 P.2d 199 (Alaska 1995).

Sec. 21.89.100. Appointment of independent counsel; conflicts of interest; settlement. (a) If an insurer has a duty to defend an insured under a policy of insurance and a conflict of interest arises that imposes a duty on the insurer to provide independent counsel to the insured, the insurer shall provide independent counsel to the insured unless the insured in writing waives the right to independent counsel. An insurance policy may contain a provision that provides a method of selecting independent counsel if the provision complies with this section.

(b) For purposes of this section, the following do not constitute a conflict of interest:

(1) a claim of punitive damages;

(2) a claim of damages in excess of the policy limits;

(3) claims or facts in a civil action for which the insurer denies coverage.

(c) Notwithstanding (b) of this section, if the insurer reserves the insurer's rights on an issue for which coverage is denied, the insurer shall provide independent counsel to the insured as provided under (a) of this section.

(d) If the insured selects independent counsel at the insurer's expense, the insurer may require that the independent counsel have at least four years of experience in civil litigation, including defense experience in the general subject area at issue in the civil action, and malpractice insurance. Unless otherwise provided in the insurance policy, the obligation of the insurer to pay the fee charged by the independent counsel is limited to the rate that is actually paid by the insurer to an attorney in the ordinary course of business in the defense of a similar civil action in the community in which the claim arose or is being defended. In providing independent counsel, the insurer is not responsible for the fees and costs of defending an allegation for which coverage is properly denied and shall be responsible only for the fees and costs to defend those allegations for which the insurer either reserves its position as to coverage or accepts coverage. The independent counsel shall keep detailed records allocating fees and costs accordingly. A dispute between the insurer and insured regarding attorney fees that is not resolved by the insurance policy or this section shall be resolved by arbitration under AS 09.43.

(e) If the insured selects independent counsel at the insurer's expense, the independent counsel and the insured shall consult with the insurer on all matters relating to the civil action and shall disclose to the insurer in a timely manner all information relevant to the civil action, except information that is privileged and relevant to disputed coverage. A claim of privilege is subject to review in the appropriate court. Information disclosed by the independent counsel or the insured does not waive another party's right to assert privilege.

(f) An insured may waive the right to select independent counsel by signing a statement that reads substantially as follows:

I have been advised of my right to select independent counsel to represent me in this lawsuit and of my right under state law to have all reasonable expenses of an independent counsel paid by my insurer. I have also been advised that the Alaska Supreme Court has ruled that when an insurer defends an insured under a reservation of rights provision in an insurance policy, there are various conflicts of interest that arise between an insurer and an insured. I have considered this matter fully and at this time I am waiving my right to select independent counsel. I have authorized my insurer to select a defense counsel to represent me in this lawsuit.

(g) If an insured selects independent counsel under this section, both the counsel representing the insurer and independent counsel representing the insured shall be allowed to participate in all aspects of the civil action. Counsel for the insurer and insured shall cooperate fully in exchanging information that is consistent with ethical and legal obligations to the insured. Nothing in this section relieves the insured of the duty to cooperate fully with the insurer as required by the terms of the insurance policy.

(h) When an insured is represented by independent counsel, the insurer may settle directly with the plaintiff if the settlement includes all claims based upon the allegations for which the insurer previously reserved its position as to coverage or accepted coverage, regardless of whether the settlement extinguishes all claims against the insured. (§ 107 ch 62 SLA 1995; am §§ 34, 35 ch 26 SLA 1997)

Cross references. — For a statement of legislative intent relating to the provisions of ch. 26, SLA 1997, see § 1, ch. 26, SLA 1997 in the 1997 Temporary and Special Acts. For severability of the provisions of ch. 26, SLA 1997, see § 56, ch. 26, SLA 1997 in the 1997 Temporary and Special Acts.

Effect of amendments. — The 1997 amendment, effective August 7, 1997, added the third and fourth sentences in subsection (d) and added subsection (h).

Editor's notes. — Section 55, ch. 26, SLA 1997 provides that the provisions of ch. 26, SLA 1997 apply "to all causes of action accruing on or after August 7, 1997."