

Policyholder's Litigation Costs Are Recoverable in Defending Against Excess Insurer's Declaratory Relief Coverage Action

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On October 1, a New York appellate court held in *RLI Ins. Co. v. Smiedala*¹ that an insured who prevailed in a declaratory relief coverage action brought by its excess insurer could recover its attorney's fees in the litigation, even though the excess insurer's coverage obligations with respect to underlying litigation had not yet been triggered. The opinion, of interest to insureds engaged in coverage disputes, is well supported by prior New York precedent that "'an insurer's responsibility to defend reaches the defense of *any* actions arising out of the occurrence,' and defense expenses are recoverable by the insured, including those incurred in defending against an insurer seeking to avoid coverage for a particular claim."² Under New York law, "an insured who prevails in an action brought by an insurance company seeking a declaratory judgment that it has no duty to defend or indemnify the insured may recover attorney's fees regardless of whether the insurer provided a defense to the insured."³

Under what is known as the "American Rule," which provides that each party in a lawsuit commonly pays its own attorney's fees, a prevailing party's attorney's fees are generally not recoverable unless a statute or contract provides for such recovery. However, many states carve out an exception for policyholders in insurance coverage disputes that permit a policyholder that prevails in a coverage action to recover its attorney's fees and expenses. In New York, the exception applies where the policyholder is placed in a "defensive posture" by a suit brought or counterclaims asserted by the insurer. Some states, such as Arkansas, Kansas, Maryland, Montana, South Carolina, Washington, and West Virginia, apply a broader exception to the American Rule that permits a policyholder to recover its costs when it prevails in a coverage action regardless of whether the insurer or policyholder brought the coverage action and regardless of whether the insurer was acting in "good faith." Other states, such as Minnesota, Wisconsin, and Massachusetts, apply narrower exceptions to the American Rule, permitting recovery of attorney's fees where an insurer with a defense obligation has failed to defend the policyholder in an underlying action under a reservation of rights.

¹ 2010 NY Slip Op. 06836, 2010 WL 3817114 (Oct. 1, 2010).

² *National Grange Mut. Ins. Co. v. T.C. Concrete Constr., Inc.*, 43 A.D.3d 1321, 1322 (N.Y. App. Div. 2007) (quoting *Mighty Midgets v. Centennial Ins. Co.*, 47 N.Y.2d 12, 21 (1979)); see also *Progressive Halcyon Ins. Co. v. Giacometti*, 72 A.D.3d 1503, 899 N.Y.S.2d 783 (2010).

³ *U.S. Underwriters Ins. Co. v. City Club Hotel, LLC*, 3 N.Y.3d 592, 598 (2004).

