Portfolio Media. Inc. | 111 West 19th Street, 5th Floor | New York, NY 10011 | www.law360.com
Phone: +1 646 783 7100 | Fax: +1 646 783 7161 | customerservice@law360.com

Mass. High Court Ruling May Swell Insureds' Litigation Costs

By **Jeff Sistrunk**

Law360, Los Angeles (June 23, 2017, 7:03 PM EDT) -- The Massachusetts high court's ruling Thursday that an insurer's duty to defend doesn't include an obligation to prosecute a client's counterclaims could increase litigation costs for policyholders by forcing them to hire separate attorneys to manage a case's defensive and offensive strategies, attorneys say.

In a 5-2 decision, the Massachusetts Supreme Judicial Court said that the plain language of eyewash and lens cleaner maker VisionAid Inc.'s policy with Mount Vernon Fire Insurance Co. was unavoidable: Mount Vernon had only a duty to "defend" and pay "defense costs." The duty to defend does not, on its own, include a duty to pay for counterclaims, the majority found, and the duty to pay for defense costs is the same thing as the duty to defend.

VisionAid, which had faced a lawsuit from a former employee whom the company in turn accused of embezzling hundreds of thousands of dollars, argued that the counterclaims were so deeply intertwined in its defense that Mount Vernon should have to pay for those as well. According to VisionAid, no reasonable lawyer would decline to bring the counterclaims.

But the majority of the state high court was unswayed, saying the plain language of the policy compelled a decision in Mount Vernon's favor.

"To adopt this interpretation would require us to read in a number of provisions that the parties did not include in the policy," Justice Frank M. Gaziano wrote for the majority.

Attorneys who represent policyholders tell Law360 that the opinion is based on a fundamental misconception about what it means to "defend" a proceeding, asserting that an insured's counterclaims will often be interlocked with its defense strategy. In practice, the ruling means that policyholders may have to pay out-of-pocket for a second lawyer to pursue its counterclaims, rather than having one attorney handle every aspect of a case, attorneys say.

According to Alicia J. Samolis, chair of Partridge Snow & Hahn LLP's labor and employment practice, that type of arrangement can lead to duplicative efforts and, by extension, unnecessary costs for the insured.

"If you start parsing out counts, it is not the case that each attorney will do half; they are both going to virtually be doing it all," Samolis said. "In fact, the insured may actually end up spending more money than if their own attorney did the case alone because the attorneys will be going back and forth on

issues like settlement terms and language in motions. Thus, the insurance policy may not provide any savings for the insured once the insured is told to retain its own counsel for the counterclaim."

However, Crowell & Moring LLP partner Laura Foggan, who represented the American Insurance Association and other insurance industry groups as amici in support of Mount Vernon, said the Massachusetts high court's opinion properly drew a "bright line" limiting an insurer's obligation to defend its policyholder, and she dismissed the notion that having multiple attorneys represent a policyholder is unworkable.

"There is a lot of circumstances where attorneys cooperate in representing a party," Foggan said. "The fact that separate counsel may be necessary here is not something new or unusual. There are choices the policyholder can make about whether it wants to assert the counterclaim. If it chooses to do so, it has the right to do so by retaining its own counsel."

Mount Vernon and VisionAid are tangled up in litigation about the scope of coverage in an underlying lawsuit by a former VisionAid employee. VisionAid said it fired the employee after learning he had embezzled hundreds of thousands of dollars. The employee later filed a lawsuit alleging the company fired him because of his age.

The fired worker offered to settle the case for $400,000, but facing VisionAid’s counterclaims for the alleged embezzlement, he later offered to settle for nothing except VisionAid's agreement to drop the counterclaims, according to court papers.

VisionAid, hoping to recover some of the allegedly embezzled funds, refused, but Mount Vernon declined to cover the embezzlement counterclaims. VisionAid hired its own lawyer and took the fight to federal court, where a judge found in favor of Mount Vernon. The case was appealed to the First Circuit, which asked the Massachusetts Supreme Judicial Court to weigh in on whether an insurer's defense obligations extend to the obligation to prosecute a policyholder's counterclaims.

In Thursday's opinion, the high court found that the plain language of Mount Vernon's policy doesn't support a finding that the insurer must press its policyholder's counterclaims. The majority said VisionAid's position wasn't helped by Massachusetts' "in for one, one for all" rule, which states that an insurer defends an entire lawsuit, even if only some of the claims are covered under the policy.

Furthermore, the majority emphasized that a ruling in VisionAid's favor would have opened the door to tons of peripheral litigation on various issues, including whether counterclaims are adequately intertwined with policyholders' defense efforts.

"Not only is [VisionAid's] proposition found nowhere in the language of the contract, it would result in extensive preliminary litigation to determine what claims are sufficiently intertwined, litigation that would be brought by 'any reasonable attorney,'" Justice Gaziano wrote.

Attorneys who represent insurance carriers say that the majority reached a common-sense conclusion that will avert endless battles between insurers and policyholders on ancillary issues and discourage policyholders from asserting weak counterclaims.

"Courts shouldn't interpret policies in ways that would engender more coverage litigation," said Morrison Mahoney LLP partner Michael F. Aylward, who represented American International Group Inc. and Massachusetts Insurance Federation Inc. as amici in support of Mount Vernon.

For instance, Foggan noted, determining whether a "reasonable" attorney would have pursued a counterclaim is a complex inquiry that would require extensive litigation.

"Goodness knows what that could encompass," Foggan said. "It's such a broad standard."

Indeed, a ruling for VisionAid would have added a layer of uncertainty, making it tough for insurers to appropriately price policies, according to Foggan.

"That wouldn't help the insurance marketplace as far as having a product that can be priced consistently," Foggan said.

Meanwhile, attorneys who counsel policyholders say the dissenting opinion written by Massachusetts Chief Justice Ralph Gants represents a more realistic view of what is entailed in a defense effort.

The chief justice said he would have recognized a limited duty for insurers to prosecute counterclaims, extending to any proceeding where a policyholder's defense is intertwined with compulsory counterclaims, where a reasonable attorney would bring the counterclaims and where the insured agrees that anything recovered by the counterclaim would offset any damages from the main claim.

“In such circumstances, the insurer cannot reasonably fulfill its duty to defend the insured in the proceeding without also prosecuting such counterclaims because it would be impractical and deleterious to an effective defense to fail to do so,” Justice Gants wrote.

Policyholder lawyers agree with Justice Gants' position that permitting an insurer to refuse the cost of prosecuting a compulsory counterclaim is tantamount to not providing a complete defense. Pillsbury Winthrop Shaw Pittman LLPpartner David Klein compared the majority's approach to requiring the policyholder's lawyer to "punch with one fist while keeping the other fist tied behind his back."

"Not all counterclaims are intertwined with the affirmative claims against an insured," Klein said. "But where a transaction or occurrence amounts to a single story with two sides, and each side may have a colorable claim against the other that will affect the value of the damages that might change hands, it makes sense for an insurer to pay for the entire defense. When in a boxing match, you punch, as well as rope-a-dope."

Thus, the opinion creates a situation in which a policyholder may have to rely on insurer-appointed counsel to handle the defense side of a case while paying out-of-pocket to hire a separate attorney to prosecute any counterclaims. According to attorneys, though, effectively managing the boundaries between defensive and offensive elements of a case is often easier said than done.

"The defense attorney, even when appointed by an insurer, still has ethical obligations and professional duties to the policyholder and not the insurer," said Sherilyn Pastor, leader of McCarter & English LLP's insurance coverage group.

"Particularly where claims are factually intertwined, it will be difficult to make the distinction between what needs to be done to appropriately defend a cause of action or press an affirmative defense versus what needs to be done to further a compulsory counterclaim," Pastor added. "The lines are not as clear as the insurers argue, and this ruling will result in confusion and drive up the costs associated with handling an insured’s matter."

Even after the Massachusetts high court's ruling, attorneys say not all insurers will refuse to press policyholders' counterclaims. Pierce Atwood LLP partner Michael J. Daly said that in certain circumstances, an insurer may still decide it is in its best interest to pay for the prosecution of a counterclaim.

"Depending on the relationship between the claim and the counterclaim, it is possible that that can be done without much additional effort or cost while providing a great benefit to the insured and insurer," Daly said. "It could reduce the insured's potential exposure through set-off or provide leverage for a settlement, which helps the insurer as well."

Mount Vernon is represented by James J. Duane III and Scarlett M. Rajbanshi of Peabody & Arnold LLP.

VisionAid is represented by Kenneth R. Berman, Cynthia M. Guizzetti and Heather Repicky of Nutter McLennen & Fish LLP.

The case is Mount Vernon Fire Insurance Co. v. VisionAid Inc. on a certified question from the U.S. Court of Appeals for the First Circuit in the Supreme Judicial Court, case number SJC-12142.

--Additional reporting by Brian Amaral. Editing by Christine Chun and Edrienne Su.
