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An Insured's 'Right' to 'Independent' Counsel

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As a matter of conventional wisdom, if an insurer reserves its right to deny coverage, even while agreeing to defend an insured against a third party's claim, or denies coverage for a loss while accepting the duty to defend the insured, the insured has the right to be represented by defense counsel chosen by the insured and paid by the insurance carrier. The rationale for this result is that a reservation of rights or disclaimer of indemnity creates a conflict of interest between the insured and the insurer. Lawyers familiar with liability insurance issues recognize this principle as axiomatic. (See "Right to Independent Counsel: Effectively Implement an Insurer's Duty to Defend," NYLJ, Sept. 10, 2012.) However, while the principle may be simply stated, its application, not surprisingly, is more complex. When does the "right" arise? Who gets to choose? What does "independent" mean? The right answer to each of these questions is, It depends.

When Does Right Arise?

When does a right to independent counsel arise? In *Prashker v. U.S. Guarantee Co.*, 1 N.Y.2d 584, 154 N.Y.S.2d 910 (1956), the New York Court of Appeals laid down the basic rule. If the grounds of liability asserted against an insured fall partly within and partly outside exclusionary clauses in a liability insurance policy, the insurer faces a conflict of interest. Its duty to the insured demands that it attempt to defeat liability on every ground asserted, while its own self-interest requires only that it defeat liability on grounds that might result in liability that is not excluded from the policy.

In these circumstances, since the insured's interest is paramount, the insured has the right to defense counsel who will not suffer from the conflict, and the carrier remains liable to pay the full cost of defense (subject, of course, to any applicable deductible). This rule has been carried forward. See, e.g., *Hartford Accident & Indemnity Co. v. Village of Hempstead*, 48 N.Y.2d 218, 422 N.Y.S.2d 47 (1979), although, as one lower court commented, "Allowing the insured to select independent or controlling counsel at the insurance company's expense seems to depend on the facts of each case." *Parker v. Agricultural Ins. Co.*, 109 Misc. 2d 678, 684, 440 N.Y.S.2d 964 (Sup. Ct. N.Y. Co. 1981).

The Court of Appeals weighed in again in *Public Service Mutual Ins. Co. v. Goldfarb*, 53 N.Y.2d 392, 442 N.Y.S.2d 422 (1981), often recognized as the leading case on this subject. A dentist was sued for malpractice; the claims included engaging in sexual activity with his patient, triggering a variety of exclusions from coverage. The Court of Appeals held that because the insurer would only be liable to pay some of the claims asserted against the insured and would not be liable for others, the insured was entitled to "defense by an attorney of his own choosing, whose reasonable fee is to be paid by the insurer." 53 N.Y.2d at 401.

In a justifiably famous footnote, the court explained an important—some may say critical—limitation. Paraphrasing *Prashker*, the court decreed that "[i]ndependent counsel is *only necessary* where the defense attorney's duty to the insured would require that he defeat liability on any ground and his duty to the insurer would require that he defeat liability only upon grounds which would render the insurer liable." However, "where multiple claims present no conflict—for example, where the insurance contract provides liability coverage only for personal injuries and the claim against the insured seeks recovery for property damage as well as for personal injuries—no threat of divided loyalty is present and there is no need for the retention of separate counsel." 53 N.Y.2d at 401 (emphasis added).

How can we tell the difference? The deciding factor, the court stated, is whether the question of insurance coverage is "intertwined with the question of the insured's liability." The facts of each case must be examined to ascertain whether the perceived "conflict" is outcome-determinative, i.e., whether the existence or non-existence of coverage depends on the outcome of the liability case. In *Goldfarb* itself, for example, if the dentist were found to have injured the plaintiff unintentionally, his policy would provide coverage; if he intended to harm his patient, there would be no coverage. Counsel's development of the facts prior to and at trial would be crucial to both liability and the availability of coverage. A clear conflict.

Coregis Ins. Co. v. Lewis, Johs, Avallone, Aviles and Kaufman, 2006 WL 2135782 (E.D.N.Y. July 28, 2006), provides a good example of a coverage issue that did not create a conflict of interest between the insurer and the insured concerning the defense of the underlying claim. The underlying liability claim was for legal malpractice in presenting a trial expert whose opinion was based on incorrect data. The lawyers' professional liability policy excluded claims which the insured should have anticipated prior to the beginning of the time period covered by the policy. The coverage issue, therefore, was whether the insured should have anticipated a claim when the fatal weakness of the expert's testimony was revealed—during trial. This issue had no bearing on the lawyers' liability to their clients, and therefore presented no outcome-determinative "conflict" that warranted the selection of "independent" counsel.

Contrasting examples abound. Compare *Ladner v. American Home Assurance Co.*, 201 A.D.2d 302, 607 N.Y.S.2d 296 (1st Dept. 1994) (where a psychologist was accused of professional malpractice for acts including sexual misconduct, and the policy excluded claims for "erotic physical contact," independent counsel was required), *Golotrade Shipping & Chartering v. Travelers Indemnity Co.*, 706 F.Supp. 214, 216 (S.D.N.Y. 1989) (the insurer disclaimed liability "for any malicious, intentional or conspiratorial acts, even if only compensatory damages were awarded"; independent counsel was required), and *Utica Mutual Ins. Co. v. Cherry*, 45 A.D.2d 350, 358 N.Y.S.2d 519 (2d Dept. 1974), aff'd, 38 N.Y.2d 735, 381 N.Y.S.2d 40 (1975) (the plaintiff asserted claims for negligence and intentionally causing death, for which the insured had been convicted of manslaughter;

independent counsel was required); with *New York Marine and General Ins. Co. v. Lafarge North America*, 599 F.3d 102 (2d Cir. 2010) (the coverage issue was whether the policy covered a barge owned by another entity which was not insured by the same carrier; the insured was found to have acted unreasonably in refusing to select counsel from list provided by insurer), *Prudential Property & Casualty Ins. Co. v. Godfrey*, 169 A.D.2d 1035, 1036, 565 N.Y.S.2d 315 (3d Dept. 1991) ("plaintiff's interest in disproving negligent entrustment of the ATV does not conflict with defendants' interest in defeating both the negligence and negligent entrustment claims"), and *Anderson v. Port Authority of New York and New Jersey*, 1985 WL 1893 at *2 (S.D.N.Y. July 11, 1985) ("[N]o actual conflict appears to exist. Counsel for the Port Authority, in filing its answer on behalf of the officers, alleges that the officers were acting within the scope of their employment at the time of the alleged assault and false arrest, and the Port Authority has given no indication that it intends to deny that now or at trial. Thus the Port Authority and the police officers are united in interest with regard to the trial of these claims").

Where the coverage issue is "intertwined" with the insured's liability, a conflict may be present, and the insured may have the right to "independent" counsel. Where the coverage issue relates to fundamental coverage matters—e.g., whether a claim is for property damage or personal injury or whether particular property is covered by the policy or whether the claim was first made during the policy period—there is no outcome-determinative conflict and independent counsel is not required.

Who Gets to Select Counsel?

Most decisions appear to assume that when a true conflict arises between insured and insurer, the insured has the right to select defense counsel. However, as the New York Court of Appeals has recognized, "An insured's right to be accorded legal representation is a contractual right." *International Paper Co. v. Continental Casualty Co.*, 35 N.Y.2d 322, 325, 361 N.Y.S.2d 873 (1974). In *New York State Urban Development Corp. v. VSL Corp.*, 738 F.2d 61 (2d Cir. 1984), the U.S. Court of Appeals for the Second Circuit addressed a right to independent counsel where the policy provided that "claims expenses" would be paid by the carrier and defined "claims expenses" as including "fees charged by an attorney designated by" the insurer and "fees charged by any attorney designated by [the insured] with the written consent" of the carrier. 738 F.2d at 65.

Since the policy provided that the insurer was obligated to pay counsel fees only if it selected or consented to the insured's choice of counsel, the insurer was entitled to participate in the selection of counsel. Compare the decision in *VSL* with *Cuniff v. Westfield*, 829 F.Supp. 55 (E.D.N.Y 1993), where the policy did not contain language that permitted the insurer to have at least a voice in the selection of counsel.

As the court held in *VSL*, the terms of a contract—including an insurance contract—govern unless they are contrary to public policy, and the insurer's participation in the selection of counsel "does not automatically taint the independence of chosen counsel." 738 F.2d at 66. Some carriers (and municipalities that are statutorily responsible for providing a defense to their employees when they are sued) accommodate both the insured's (or defendant's) interests and their own by providing a list of qualified defense counsel and allowing the insured (or defendant) to make the final choice. E.g., *Mothersell v. City of Syracuse*, 952

F.Supp. 112 (N.D.N.Y. 1997); see also *Suffolk County Patrolmen's Benevolent Assoc. v. County of Suffolk*, 751 F.2d 550 (2d Cir. 1985).

Meaning of 'Independent'

What does 'Independent' mean? It is obvious that "independent" means not under the thumb of the insurer, or capable of providing a defense that does not favor the insurer's interest over the interests of the insured. It is less obvious, but perhaps equally valid, to suggest that "independent" also means not favoring the insured's interest over the insurer's. The district court in *VSL* addressed this issue directly: "Northbrook [the insurer] is under a duty to provide only an impartial defense—not to sacrifice its own interests. VSL's defense counsel must not be motivated to slant the defense in any manner relating to whether a claim is or is not in the scope of coverage. Allowing VSL to appoint as 'independent counsel' a firm that bears its loyalty to VSL or any animus to Northbrook would reintroduce, albeit in a converse manner, the very difficulties that necessitate in the first instance the appointment of independent counsel.... The cases' consistent and repeated use of the term 'independent' negates any contrary assertion." *New York State Urban Development Corp. v. VSL Corp.*, 563 F.Supp. 187, 190 n. 1 (S.D.N.Y. 1983), citing Keeton, Liability Insurance and Responsibility for Settlement, 67 Harv. L. Rev. 1136, 1169-70 (1954). We have not found any other New York case that addresses this issue directly, but the VSL court's logic seems unassailable.

In sum, the three questions presented in the first paragraph of this article cannot be answered instinctively. An insured's "right" to select independent counsel at the insurance company's expense depends on the facts of the case, as well as the language of the policy and counsel's independence from both the insurer and the insured.
