

July 31, 2008 Coverage Alert

“Over-Inclusive” Reservation of Rights Letters May Violate the CPA

*By Paul M. Rosner and Misty Edmundson*

United States District Court Judge Benjamin H. Settle<sup>1</sup> refused to dismiss as a matter of law an argument that an “over-inclusive” reservation of rights letter may support a claim for a misrepresentation under the Washington insurance regulations, and, therefore support a claim for violation of the Washington Consumer Protection Act. Judge Settle found that “the question of whether an over-inclusion of policy provisions in a reservation of rights letter is a misrepresentation under the Washington Insurance Regulations is unresolved.”<sup>2</sup>

**Background**

The Owners Association sued the developer, MacLean, who sued AHB, the Sider. AHB tendered to its insurer, Charter Oak, which issued an admittedly over-inclusive reservation of rights letter. AHB settled and assigned rights to MacLean. MacLean sued Charter, which moved for summary judgment, *inter alia*, that the over-inclusiveness of the reservation of rights letter did not constitute a misrepresentation of policy provisions and thus a violation of insurance regulations.

**Does an Over-Inclusive ROR Letter Violate the CPA and Insurance Regulations?**

Under WAC 284-30-330 & 350, an insurer may not “misrepresent... insurance policy provisions” and must “fully disclose all pertinent...provisions of an insurance policy or insurance contract” to its insured. MacLean argued that the over-inclusive reservation of rights letter misrepresented that certain policy provisions might apply, even though there was no current factual basis for their application. The court denied Charter Oak’s motion for summary judgment, concluding that “the question of whether an over-inclusion of policy provisions in a reservation of rights letter is a misrepresentation under the Washington Insurance Regulations is unresolved.”

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<sup>1</sup> *MacLean Townhomes, LLC v. Charter Oak Fire Ins. Co.*, Order Granting in Part and Denying in Part Defendant’s Motion for Partial Summary Judgment (W.D. Wash C06-1093BHS).

<sup>2</sup> The Court also held (1) the insured’s expert’s cost and scope documents in the underlying lawsuit are subject to work-product protection and (2) the issuance of a reservation of rights letter does not release a policyholder from its contractual duty to cooperate with the insured.

## **Conclusion**

Although only a trial court decision, the ruling has the potential for placing insurers in a difficult position. On one hand, insurers traditionally worry about application of principles of waiver or estoppel for failure to identify a policy defense in a reservation of rights letter. On the other hand, Judge Settle's decision now gives rise to potential CPA liability based upon an over-inclusive reservation of rights letter.

At heart, the issue ultimately turns upon a rule of reasonableness. As recognized by Judge Settle, "the determinative question is the reasonableness of the insurer's actions in light of all the facts and circumstances of the case." If there is some basis to believe a policy provision might apply, the reservation of rights letter should quote the provision and explain its potential application. The reservation of rights letter should not quote policy provisions that are not implicated by the facts. Rather, a letter should expressly reserve the right to rely on additional policy provisions that may apply based on the development of additional facts.

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