ASSOCIATION OF BUSINESS TRIAL LAWYERS

abtl REPORT

Volume XXIV No. 2 *Spring 2002*

The Meaning of An Insurance Carrier's Reservation of Rights — Part 1

In many complex civil cases an insurance carrier agrees to defend one party or the other. Often such a defense is under a reservation of rights. The letter setting forth that reservation generally uses standardized, legal-sounding language. It may even be a form letter sent by a claims representative who may not entirely understand its meaning or effect. And sometimes all the insured or defense counsel understands (or for the moment cares about) is that an insurance carrier is picking up at least a portion of the legal fees. But what does the carrier's reservation of rights really mean?

Robert A. Olson

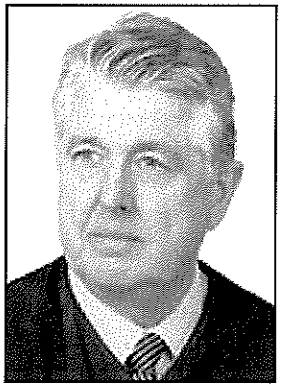
A reservations of rights letter will often identify the various coverage issues that may be present in the litigation (*e.g.*, identifying that potentially the conduct may be willful, or the injury outside of the policy period, or no coverage may be afforded for equitable relief). These coverage issues will vary depending on the nature of the claims at issue and the coverage afforded by the particular insurance policy. The identified coverage issues explain *why* the carrier is reserving its rights; however, they do not explain *what* rights the carrier is reserving. The letter should also specifically set out the *rights* that the carrier is reserving. These are typically fairly standard, falling into a handful of categories. Two of these typical reservations — the right to deny coverage for any ultimate judgment and the right to seek reimbursements for settlements — are discussed in this issue. Two other sometimes reserved rights — the

(Continued on page 9)

INSIDE

Defining Internet Jurisdiction

Through the Internet, world-wide instantaneous communications electronically permeate the political boundaries that traditionally have defined and separated state sovereignties. One court has defined the Internet as "...a worldwide network of computers that enables various individuals and organizations to share information. The Internet allows computer users to access millions of web sites and web pages. A web page is a computer data file that can include names, words, messages, pictures, sounds, and links to other information." *Panavision Intern, L.P. v. Toeppen* (9th Cir. 1998) 141 F.3d 1316, 1318.



Hon. Richard Fruin

Another court has analyzed the spectrum of Internet usage, from passive review of a website, to fully interactive communications, to determine when personal jurisdiction should be exercised over a foreign originator of Internet communications. *Zippo Manufacturing Co. v. Zippo Dot Com, Inc.* (W.D. Penn. 1997) 952 F.Supp. 1119, 1123-24. Four recent California Court of Appeal decisions applying traditional jurisdiction analysis to torts committed over the Internet suggest that careful attention to where the case lands on the Internet usage spectrum and to old-fashioned procedural issues can make a difference to whether California jurisdiction will attach or be rejected.

Jurisdiction Primer

California's long-arm statute authorizes California courts to exercise jurisdiction on any basis not inconsistent with the Constitution of the United States or the Constitution of California. Code Civ. Proc. § 410.10. Personal jurisdiction may be general or specific. For general jurisdiction, the nonresident defendant's contacts with the forum must be "substantial...continuous and systematic." *Vons Companies, Inc. v. Seabest Foods, Inc.* (1996) 14 Cal.4th 434, 445.

Absent general jurisdiction, a nonresident defendant may be subject to specific jurisdiction if she (1) "purposefully availed" herself of forum benefits; (2) the dispute is related to the defendant's contacts with the forum; and (3) the exercise of jurisdiction is reasonable, that is, it comports with "fair play and substantial justice." *Vons Companies, Inc. v. Seabest Foods, Inc.*, 14 Cal.4th at 447-48.

In tort cases, the "purposeful availment" requirement can be measured by the effects of the nonresident defendant's conduct

(Continued on page 2)

Insurance Carrier's Reservation of Rights

Continued from page 1

right to seek reimbursement of defense costs and the right to withdraw from the defense — are discussed in the next issue.

The Right To Deny Coverage For Any Ultimate Judgment. First, carriers generally reserve the right to deny indemnity coverage to the extent a judgment is rendered on a basis that is not covered. This is fairly straightforward if the insured is found liable on a ground that clearly is not covered, *e.g.*, for willful misconduct or intentional fraud (*see* Ins. Code, § 533 [barring coverage in such circumstances].) The carrier, having reserved its right to do so, will not pay that portion of the judgment that on its face is not covered.

But what if the judgment is ambiguous as to whether it is premised on a covered ground (for example, what if there is a general verdict after presentation of claims that might be either covered or not covered)? To address that scenario, a properly drafted reservation of rights letter will also reserve the carrier's right not to be bound by any judgment against the insured. This means that if the judgment is ambiguous, the carrier will be free to litigate with its insured whether the basis for liability, in fact, was a covered or noncovered ground. "'[I]f the insurer adequately reserves its right to assert the noncoverage defense later, it will not be bound by the judgment. If the injured party prevails, that party or the insured will assert his claim against the insurer. [Fn. omitted.] At this time the insurer can raise the noncoverage defense previously reserved.'" (*J. C. Penney Casualty Ins. Co. v. M. K.* (1991) 52 Cal.3d 1009, 1017, quoting *Gray v. Zurich Insurance Co.* (1966) 65 Cal.2d 263, 279.)

Indeed, the carrier's reservation of the right not to be bound by the judgment will allow it to litigate the coverage question in its dispute with the insured even if the judgment against the insured is on an unambiguously covered ground. For example, if the sole claim the plaintiff presents and argues to the jury is one for unintentional negligence, the carrier, having reserved its right to do so, remains free to contend and to litigate with the insured (or with the plaintiff if the insured has assigned any rights against the carrier) whether the insured's conduct, in fact, was willful and not covered. (*J. C. Penney Casualty Ins. Co. v. M. K., supra*, 52 Cal.3d 1009 [even though plaintiff obtained judgment solely for negligence, carrier was free to prove uncovered willful sexual molestation].)

The Right To Seek Reimbursement For Settlements. These rules apply equally to settlements. The carrier generally will reserve the right not only not to be bound by any judgment but also not to be bound by any settlement. But how then is the case to get settled? Most plaintiffs are not willing to wait until the insured defendant and its carrier settle their coverage dispute before being paid.

The scenario often runs something as follows. The carrier is defending, having reserved its rights not to be bound by any judgment or settlement. The plaintiff makes a settlement demand. The insured defendant demands that the carrier settle the case by agreeing to pay the full amount of the settlement demand. At the same time, the insured defendant asserts that the full settlement amount is the carrier's sole responsibility and it will not agree to the settlement if it ultimately is going to be liable for any portion of that settlement.

The California Supreme Court recently addressed just this scenario in *Blue Ridge Ins. Co. v. Jacobsen* (2001) 25 Cal.4th 489. There, a carrier was defending its insureds having reserved its rights to contest coverage. The case involved a dog owned by the insureds that had mauled a young girl. The plaintiff presented a settlement demand within policy limits. It was not disputed that the amount of the settlement demand was reasonable. Unlike some insurance policies (*e.g.*, professional malpractice

(Continued on page 10)

Electronic Briefs: A Peek at the Future?

Like so many things in life, technology is both a blessing and a curse.

The Xerox machine, word processors, e-mail, real time reporting — and the like — while they have made many aspects of life and the practice of law so much easier, they are also burying lawyers and courts alike in ever growing and increasingly unmanageable mountains of paper. Case law, legislation, learned commentary, documentary discovery, depositions and the other tools of the litigator's trade are spontaneously multiplying like the Sorcerer's apprentice's brooms. And if that is not enough, depositions are now not only being reported in "real time" but are also frequently being videotaped. Add to this the ever-increasing complexity of many of the factual and legal issues now being litigated and the serious pressures imposed on an already overworked judiciary by our increasingly litigious society, and the challenge these factors pose to trial lawyers in efficiently and effectively communicating with both trial and appellate judges is monumental.

Robert K. Wrede

How can a lawyer faced with a war-room full of documents; bookshelves chock full of deposition or trial transcripts; volumes and volumes of case law, legislative history, law review articles and learned treatises; frequently numerous conflicting expert reports; discovery responses, myriad motions and other pleadings; trial transcripts and the trial "record;" and all the other accumulated detritus which complex litigation generates effectively and persuasively communicate his or her arguments to an already overburdened court?

One answer, which is rapidly gaining strong support among seasoned lawyers and numerous members of the judiciary, alike, is the electronic brief. An electronic brief is no more nor less than a digitized version of a traditional printed brief and accompanying appendices, PLUS pertinent case law and other legal authority cited in the printed brief AND any audio/video materials which are included in the "record" all of which have been digitally recorded on a CD, which can be loaded in the CD drive of any Windows-based PC or laptop equipped with a CD drive.

Whenever any bit of testimony, case law or other legal authority, documentary evidence, material to be judicially noticed, or any other pertinent material extrinsic to the brief itself is cited, the citation is "hyperlinked" to the item referred to so that, by simply "clicking" on the citation, the cited material is immediately (techies would say "seamlessly") displayed on the reader's computer screen, thus totally dispensing with the need to dig through the voluminous trial records, appendices or other "hard copy" material which generally accompanies printed briefs, motions or other argumentative pleadings. Moreover, audio/video materials are immediately available, also at the click of a mouse. In simple fact, navigating an electronic brief is as simple as surfing the Internet! For those needing a little help in navigating around an electronic brief, an on-screen user's guide is available. However, since the electronic brief screen looks like

(Continued next page)

Electronic Briefs: A Peek at the Future?

Continued from page 9

popular web browsers (only simpler), most users require no training at all.

From the lawyers' standpoint, electronic briefs are powerful tools of communication and persuasion because they allow the reader to immediately refer to testimony, exhibits, authorities, and anything else which makes up the "record" without the need to sift through mountainous hard copies or to trot to the library to paw through (or have clerks trot and paw through) dust law books. All documents, transcripts and even audio/visual materials are IMMEDIATELY accessible to the reader at a click of the mouse, thus eliminating the numerous interruptions that accompany the use of traditional printed briefs and allowing the reader to effectively maintain his or her train of thought and analysis.

From the courts' standpoint the benefits are numerous. Because every citation is hyperlinked, accessing data is instantaneous — no digging through hard to handle appendices, rummaging through boxes full of exhibits, trips to the library, or fumbling to load a tape or video player. Moreover, the entire "case" is totally portable — laptop and CD are easily carried and conveniently used just about anywhere. Perhaps most importantly, the "seamless", instantaneous switch from brief to cited material and back again allows the reader to maintain important trains of thought. Another extremely powerful tool is the ability to search the entire "record" for critical terms or passages, which can then be "cut and pasted" in the reader's word processing program, thus allowing easy preparation of notes and written analysis which the brief is being read. (In fact, full Boolean and proximity searches can be made of all text documents on the CD with results displayed in a hyperlinked list in a separate window.

Not surprisingly, lawyers and courts alike are coming to realize the value of electronic briefs as powerful and highly efficient tools of accurate communication, persuasion, and analysis. The United States Supreme Court, various United States Courts of Appeal and District Courts, and state trial and appellate courts, have entertained and even requested the use of electronic briefs. Not surprisingly, the entire set of filings in the United States Court of Appeals for the District of Columbia in *Microsoft v. United States* utilized CD-ROMs.

Any trepidation about judicial acceptance of this new technology should evaporate upon reading the following expression of judicial approval by Justice Talmadge, of the Supreme Court of Washington about their use in *Alcoa v. Aetna Casualty & Surety*:

> "[The electronic brief] greatly enhanced our ability to handle this case. The savings to the Court in time-motion efforts alone enabled us to retrieve and examine relevant parts of the record with ease, and made the record far more accessible than it would have otherwise been...We note that there is no reason why parties in more routine appeals to this Court should not seriously consider submitting the record and briefs to us in a similar format."

Given the undeniable trend toward using e-technology for document and case management, real-time reporting, OCRing, and the like, much of the work in transforming hard copies into electronic copies is already being done anyway. The move to filing important motions, trial briefs, post-trial briefs, and appellate documents will not take much.

Those interested in further investigating this exciting new technology should contact: RealLegal, the providers of "E-Brief," at www.reallegal.com, or (888) 584-9988, or TrialGraphix, the providers of "iBrief," at www.trialgraphix.com, or (888) 269-9211.

— Robert K. Wrede

Insurance Carrier's Reservation of Rights

Continued from page 9

policies), the policy afforded the carrier the right to settle without the insureds' consent. (*See generally Western Polymer Technology, Inc. v. Reliance Ins. Co.* (1995) 32 Cal.App.4th 14, 23-28 [without consent provision, carrier has right to settle even if insured claims business reputation will be harmed]; *New Hampshire Ins. Co. v. Ridout Roofing Co.* (1998) 68 Cal.App.4th 495 [without consent provision, carrier has right to settle even if doing so adversely affects insured's interest in limiting deductible expenditures].)

The insureds threatened the carrier with a bad faith claim and liability for any judgment in excess of the policy limits if it did not accept the settlement demand. At the same time, the insureds asserted that they refused to consent to the carrier settling unless it waived its reserved right to seek reimbursement from them for any settlement amount. The carrier, after offering the insureds the opportunity to assume the defense at their own expense, accepted the settlement demand anyway and sought reimbursement from the insureds.

The California Supreme Court held that the carrier had neither acted in bad faith nor waived its reserved right to reimbursement in settling over the insureds' objection where (1) it timely and expressly reserved its rights to dispute coverage and seek reimbursement; (2) it expressly notified the insureds of its intent to accept the proposed settlement; and (3) it expressly offered to the insureds that they could assume their own defense if they disagreed with the insurer's intention to accept the proposed settlement. Where a carrier meets these three conditions, it can settle a claim on which it has reserved its right to deny coverage and then seek some or even all of the settlement amount from the insured.

Blue Ridge expressly rejected arguments that the carrier acts as a volunteer and that the carrier has to write the reimbursement right into its policy language. The right to seek reimbursement for moneys advanced to pay uncovered liabilities is inherent in the policy and is preserved simply by expressly reserving it once a claim is tendered.

Blue Ridge also parted company with decisions in some other jurisdictions where the carrier arguably has to waive its reserved rights in order to settle a claim against its insured. (*E.g., Texas Assn. of Counties County Govt. Risk Management Pool v. Matagorda County* (Tex. 2000) 52 S.W.3d 128 [premised on carrier's right, not present in California, to obtain early determination of coverage issue while underlying claim against the insured is still pending]; *Mt. Airy Ins. Co. v. Doe Law Firm* (Ala. 1995) 668 So.2d 534 [contra to *Blue Ridge* as to whether carrier acted as a volunteer, but insured also not offered opportunity to assume defense]; *Medical Malpractice Joint Underwriting Assn. v. Goldberg* (1997) 425 Mass. 46 [680 N.E.2d 1121] [insured not notified of settlement or offered chance to assume the defense].)

There is one other caveat: The insured is free to contest the reasonableness of the settlement that the carrier reached. In the classic bad faith claim, the insured asserts that the carrier should have settled the claim within policy limits or coverage but did not, with the result that the insured is facing a judgment in excess of policy limits or coverage. In that circumstance the insured will claim that liability was reasonably certain and that the settlement amount demanded by the plaintiff was modest in comparison to the damages exposure. By contrast, where the carrier settles and seeks reimbursement from the insured, the insured will be in the position of asserting that liability was unlikely and that the amount the carrier paid was too much.

Blue Ridge greatly affects the dynamics among the insured, the carrier, and defense counsel in cases where the carrier is defending but has reserved its rights. It is now clear that an insured cannot demand that a carrier waive its reserved reimbursement right in order to effect a settlement or claim that the

carrier acts in bad faith by refusing to do so. Insureds — at least financially solvent ones — must walk a fine line.

On the one hand, to get the carrier to contribute to settle the case and to put the carrier at risk to cover any excess-of-limits judgment should a settlement not be effected, the insured will want to argue its potential liability and substantial damages exposure.

On the other hand, to keep the carrier from settling for a large amount that the carrier may then seek to recover from the insured under its reserved rights, the insured will want to downplay its liability and damages exposure. The result is that insureds and the counsel representing them are going to have to attempt to realistically evaluate and represent to the carrier the liability and damages exposure.

Both insureds and carriers are likely to want to settle coverage issues when settling the underlying case. Global settlements are generally more economical than ones that lead to further, follow-on litigation. Thus, it will be in both the insured's and the carrier's interests to resolve coverage issues at the same time the underlying case is settled.

Typically, this will mean that the carrier will waive its reserved reimbursement right in return for a contribution by the insured to the settlement. The result of this is that the evaluation of the ultimate coverage exposure and issues cannot be put off to the end of the case. *Blue Ridge* ensures that it is an integral part of the evaluating a case's settlement potential and posture.

Blue Ridge provides lessons for carriers as well. It provides leverage to carriers in settling cases where a substantial portion of the exposure is for uncovered wrongs or damages. It also, however, provides a checklist of what the carrier should do to preserve its reserved reimbursement rights when the insured refuses to consent to a settlement or conditions such consent on the carrier's waiver of its reserved rights. Assuming that it has timely and clearly reserved its reimbursement right, the carrier should make sure that it (1) informs the insured of the intended settlement, and (2) offers the insured the opportunity to assume the defense at the insured's expense. (*Cf. Novak v. Low, Ball & Lynch* (1999) 77 Cal.App.4th 278 [carrier's appointed counsel violates Civ. Code, § 2860 in assisting carrier in partially settling case without informing insured].)

— Robert A. Olson

Defining Internet Jurisdiction

Continued from page 3

state and thereby minimally invokes its benefits, he may nonetheless be subject to California jurisdiction if the effects are of a kind that the state treats as exceptional and therefore subjects to special regulation. *Jamshid-Negad v. Kessler, supra*, 15 Cal.App. 4th at 1708. With a more skilled discovery plan, one focused on Luhta's ability to carry out his threat against Rambam, the trial court likely would have been required to permit Rambam to proceed with the proposed discovery. The trial court then would have had to evaluate the Luhtas' jurisdiction motion in light of the information the defendants provided in answer to plaintiff's interrogatories.

Internet Message Boards

Trade Disparagement. In *Nam Tai Electronics v. Titzer* (2001) 93 Cal.App.4th 1301, an unidentified person, using various aliases, posted 246 messages on Yahoo!-maintained Internet message boards (sometimes called "chat rooms"), a few of which plaintiff claimed disparaged its reputation and thus reduced the value of its stock. Plaintiff was a consumer electronics products company based in Hong Kong, with its stock traded on NASDAQ National Market System.

Yahoo!, a California corporation, permits only those Internet users who register an alias known as a Yahoo! ID and electronically agree to Yahoo!'s terms of service to post to its message boards. The terms of service include a promise not to post any content that is unlawful, defamatory, libelous or otherwise objectionable. The terms of service further state that the relationship between the registered user and Yahoo! is governed by California law and that in the event of a dispute both parties agree to the exclusive jurisdiction of California courts.

After having filed a complaint for libel, trade libel and violation of Business & Professions Code section 17200 against a Doe defendant, plaintiff served a subpoena duces tecum on Yahoo! to learn the identity of the unknown author, and discovered the author was an AOL subscriber using a fictitious name. Plaintiff then obtained a commission for an out-of-state deposition of the Virginia custodian of records of AOL, and identified the author as Joe Titzer, whom plaintiff served at his residence in Colorado.

On Titzer's motion to quash service, the trial court determined that while California could exercise specific jurisdiction over nonresident Titzer, it would not serve California's interests to do so. To exercise California jurisdiction over Titzer under the circumstances was not "fair play and substantial justice." *Id.* at 1303. "The determinative question," the Court of Appeal said in affirming, "is whether the Web sites themselves [although hosted by a server computer physically located in California] are of particular significance to California or Californians such that the user has reason to know the posting of a message will have significant impact in this state." *Id.* at 1312. The plaintiff failed in asserting jurisdiction because it presented no evidence (1) that Titzer's messages "were directed at Californians or disproportionately likely to be read by residents of this state" or (2) that plaintiff's "relationships with residents of California were of particular importance to its business and likely to be impacted negatively" by the messages Titzer posted. *Id.* at 1312. Although the Yahoo! terms of service were enforceable to require that litigation between Yahoo! and its registered user be conducted in California, they did not govern disputes between registered users and third parties; in the absence of other significant contacts, they did not subject the Yahoo! user to California jurisdiction.

(Titzer's jurisdiction motion was inadvertently put in jeopardy by the trial court's scheduling of a status conference before the hearing date of the jurisdiction challenge. Nam Tai argued that defense counsel's appearance at the status conference, submission of a status conference questionnaire and acceptance of a trial date consented to the court's jurisdiction. The court of appeal held that it did not, noting that Titzer's counsel did not initiate any powers afforded a litigant in a California court. When the trial judge inquired what discovery the defendant contemplated, Titzer's counsel coolly responded: "If in fact we are obligated to defend in California, then I imagine that we are going to be doing some extensive discovery." While holding that "we do not believe appearance at a hearing whose purpose is to inform the court of the status of the case should be deemed a general appearance," the court of appeal nonetheless advised "it would have been better practice to postpone the status conference" when a motion challenging jurisdiction is pending. *Id.* at 308-9.)

Applying the *Zippo* rule of thumb to these four decisions, it appears that passive Internet posting is not enough for California jurisdiction unless the posted message invites conduct in which California has a significant concern; and that occasional interactive Internet communication also is not enough for California jurisdiction *at least* where the use does not differentially impact California or its residents. The cases also show how critical it is for the party asserting jurisdiction to tailor its allegations, discovery and declarations to the particular jurisdictional issues presented by its case.

— Hon. Richard Fruin

Robert A. Olson is a partner at Greines, Martin, Stein & Richland LLP.