

EXHIBIT 1



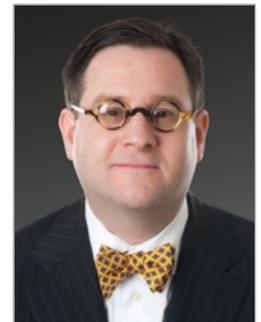
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UPDATE: Why Cosgrove V. National Should Terrify Insurers

By **Randy Maniloff, White and Williams LLP**

Editor's Note: On May 5, 2017, the same date this article first published, the U.S. District Court for the District of Arizona approved a request to vacate and seal its original ruling. This article was based on the court's original ruling. The court order is attached.

Whether defense counsel, retained by an insurer, has breached any duties owed to his or her client-insured, by providing information about the case to the insurer, is often a fact-specific inquiry. What was the nature of the information? How did defense counsel come to learn it? Did it negatively impact the client concerning coverage? These are some of the issues that are likely relevant to answering the question.



Randy Maniloff

The reporting of information, from defense counsel to insurer, was the issue in *Cosgrove v. National Fire & Marine Insurance Co.*, 14-2229 (Apr. 10, 2017). Not surprisingly it's a fact-driven decision. Nonetheless it should terrify insurers, and defense counsel, when it comes to counsel's reporting of information about a case that is being defended under a reservation of rights.

The facts are simple. Karen Cosgrove hired WTM Construction to remodel her home. Cosgrove contended that WTM did a poor job and filed suit against the construction company and its owners, William and Lana Marie Mitzel. WTM was insured under a policy issued by National Fire & Marine. National Fire & Marine hired counsel and undertook the defense of WTM and the Mitzels under a reservation of rights.

One of the policy provisions on which National Fire & Marine reserved its rights was the "Subcontractor Exclusion." This lengthy exclusion basically said that, if the insured uses subcontractors, and the subs do not agree to indemnify and hold harmless the insured, and name the insured as an additional insured on their policy (or something along those lines) then no coverage is owed. We've all seen exclusions to this effect, or perhaps not as draconian, for an insured's failure to obtain these protections from subcontractors.

At the outset of the case, defense counsel wrote to the adjuster stating that he met with William Mitzel and would "gather as much information as possible regarding the plaintiffs' allegations and the extent to which WTM Construction actually performed work at the Cosgrove residence." Shortly thereafter, defense counsel advised the adjuster that he had learned that "[a]ll construction work was done by subcontractors except for the framing" and that "[w]e have been unable to locate any subcontract agreements." Defense counsel thought he learned this information from William Mitzel and a review of the job file. Defense counsel later filed third-party complaints, against seven subcontractors, asserting claims for common law indemnity. He did not assert express indemnity claims because there were no subcontractor agreements.

The underlying action did not settle with the insurer's involvement. The insurer was not willing to pay the settlement demands because it was placing value on its potential coverage defense — the subcontractor exclusion. WTM and Cosgrove entered into a settlement and Morris agreement and WTM assigned to Cosgrove all of WTM's rights under its policy with National Fire & Marine.

Putting aside some issues as to how the settlement negotiations were handled by the insurer, the court addressed Cosgrove's argument that the insurer was estopped from asserting the subcontractor exclusion as a coverage defense.

Cosgrove argued that defense counsel disclosed information that he obtained from William Mitzel — the fact that there were no subcontractor agreements — during the course of the attorney-client relationship and the insurer is relying on that information to deny coverage. The insurer countered that the attorney did not disclose confidential or privileged information, which the subcontractor information was not.

Indeed, the fact that there were no subcontractor agreements does not seem like a state secret buried at Langley. It's a pretty routine fact in a construction dispute — and one that would seem hard to hide. The insurer's argument was along those lines: "[T]he information that [defense counsel] learned about the subcontractors was not confidential information. Rather, defendant contends that all [defense counsel] learned was the identity of who had performed the work on the project and that WTM had no written agreements with its subcontractors. Defendant argues that there is no evidence that suggests that WTM intended to keep this information confidential or that Mr. Mitzel relayed this information to [defense counsel] in confidence. In short, defendant argues that the information about the subcontractors was simply routine information and that this information in a construction defect case is almost always a known fact based on the insured's job file."

But the court didn't see it this way: "[Defense counsel] used the attorney-client relationship with WTM to gather information that he gave to defendant, which defendant then used to the detriment of WTM and now wants to use to deny coverage. At the point [defense counsel] disclosed the subcontractor information to defendant, he knew, or had reason to know, that WTM's policy contained the Subcontractors Exclusion and that defendant may attempt to deny coverage based on this exclusion. Yet despite this knowledge, [defense counsel] communicated to defendant the very information that defendant would need to deny coverage based on the Subcontractors Exclusion. ... [Defense counsel] owed his full loyalty to WTM, but it is clear that this loyalty was 'was diluted by his allegiance' to defendant."

Notably, the court observed that, contrary to the insurer's argument, "there is no requirement that the information in question be independently confidential." The information need only "have been obtained via the attorney-client relationship and that the disclosure of the information be to the detriment of the insured."

Thus, the insurer was estopped from asserting the subcontractor exclusion as a coverage defense. The court indicated that the outcome would have been different if the insurer "had done its own investigation of WTM's claims, rather than relying on the information disclosed by the attorney retained to represent WTM."

Of course, one unpublished federal district court decision does not make a rule. But it is easy to see the dramatic impact on attorney reporting and litigation management, in reservation of rights defended cases, that Cosgrove could have if it took hold. Defense counsel may not want to send any information about the case to the adjuster, for fear that he or she would violate attorney-client privilege, if it had any bearing on an insurer's coverage defense. Not to mention that defense counsel isn't supposed to know what the potential coverage defenses are. While some may be obvious, other may not be. So defense counsel wouldn't know if information being sent to the insurer could be detrimental to the insured. That's all the more reason for defense counsel to err on the side of caution and not send information to the insurer.

Randy Maniloff is an attorney at White and Williams LLP in Philadelphia, where he represents insurers in coverage disputes under a host of policies. He is the co-author of General Liability Insurance Coverage — Key Issues in Every State (3rd edition, National Underwriter) and the publisher of the newsletter and website www.CoverageOpinions.info.

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