Strategic Insurance Considerations for Energy Company Policyholders

Large energy corporations are complex organizations engaged in a host of diverse operations. In-house counsel must be prepared to handle a broad variety of legal issues, sometimes in areas where they may have practical experience but not detailed subject matter expertise. This is the first in a series of seven articles discussing how these corporate policyholders go about addressing the sophisticated sorts of insurance problems arising from their corporate activities, and what outside counsel can learn and do to assist them most effectively. This series is based on a paper supporting a panel discussion presented at the 14th Annual Advanced Insurance Law Symposium in San Antonio in June, 2017. The panel included Keith Calcote, Associate General Counsel, Litigation, Motiva Enterprises, Eric S. Eissenstat, Senior Vice-President, General Counsel, Chief Risk Officer and Secretary, Continental Resources Incorporated, Ingram Lee III, Senior Counsel, Anadarko Petroleum Corporation, Ernest Martin, Jr., Haynes and Boone, and Robert M. "Randy" Roach, Jr., Roach & Newton, L.L.P. The panel discussion was moderated by John D. Sullivan of Roach & Newton, L.L.P.

PART 2 OF 7:

PROVIDING PROPER NOTIFICATION OF OCCURRENCE-CLAIM-SUIT-LOSS

Once the claim or loss has been matched up with policies providing potential coverage, counsel should determine how, when and to whom notification must be given. This involves both internal administrative considerations, as well as requirements of policy wording and applicable law. The consequences of faulty notice can be severe in some instances, and can compromise coverage that might otherwise apply.

A. Internal considerations - Who is responsible?

Internal arrangements differ concerning responsibility for the initial handling of potentially insured losses and claims. Typically, early handling including notifications to insurers is handled by the risk Management Department, the Legal Department, or outsourced to the corporation's claims handling facility or insurance broker.

1. Risk Management

In some corporations the Risk Management Department receives and processes any notification or other processing that submits a loss or claim to relevant insurance carriers.

Risk management personnel often have frequent and close relations with the insurers, enjoy ready access to the actual policy wordings issued by insurers, and may even have ready-at-hand lists of notification particulars for each policy or insurer. Sometimes the risk management department is involved with handling standard or repetitive losses or claims that are simply part of operational business, or have responsibility to coordinate with claims handling functions within the company or as contracted for that purpose.

In this model, the Legal Department typically becomes involved only where a particular loss or claim is particularly large, presents complex problems, is disputed by the insurer, or otherwise requires special attention.

But a downside of Risk Management is that, for some corporations, the risk function has an essentially financial focus under the CFO, and personnel may have surprisingly little particular expertise in claims handling or in construing problematic policy wording to favor the corporate policyholder. As a Finance function, risk management often is more interested in contract and governmental requirements to carry certain insurances, and in the cost and tax consequences of coverage arrangements, than in actual collection of insurance proceeds to pay claims. Moreover, internal risk management personnel frequently come to the corporate environment from a background with a broker or other insurance related company, and so may have an affinity for the insurer's perspective that is not always consistent with the corporate policyholder's interests.

2. Legal Department

In other corporations, the Legal Department has initial responsibility for evaluating, handling or coordinating potentially insured losses and claims.

In-house lawyers often are attached formally or informally with specific subsidiaries or operational units within a large corporation, and therefore develop a good sense of the risks, types of losses or claims, related insurance coverage available and policy terms, and contractual arrangements with involved contractors that may provide additional coverage prospects. Sometimes individual in-house lawyers may develop particular expertise with insurance coverage issues, and act as a go-to resource either to handle especially large or complex claims, or to assist other lawyers within the department.

An advantage of in-house counsel is they are less likely to be deterred than risk management by overly friendly relations with insurers, so perhaps are more likely to take an aggressive posture in asserting coverage. A downside is that routine claims handling may be a poor use of comparatively expensive legal personnel. And in-house lawyers rarely develop significant specialized expertise with insurance issues so as to navigate a broad scope of potential insurance coverages and specific policy wordings to grasp what is necessary to protect the corporation's interest.

3. Brokers or out-sourced claims handling

Large corporations usually place most or all of their insurance through mega-brokers who solicit a broad market to obtain the multiple types of coverages necessary to cover a wide variety of assets and risks. And given the typically high deductibles or self-retentions held by such corporations, smaller losses and claims may be outsourced for claims handling administration, perhaps as part of a fronting or retrospectively rated insurance arrangement with an insurer adjusting losses that are paid directly or indirectly by the corporation itself.

In these circumstances, the broker or claims handling facility may also provide services on the front end of any loss or claim, to provide notification to potentially involved insurance companies with whom they have placed coverage or for whom they are handling claims on a lower deductible / self-retention level subject to later potential involvement by insurers at higher layers.

This approach has the benefit that the broker has perhaps the best understanding of the breadth and scope of insurance available to the corporate policyholder, and is most familiar with the requirements of particular insurers / policies for providing notification of losses or claim. But brokers have little incentive to be particularly aggressive or creative in their assertion of coverage, and as a practical matter must retain good relationships with insurers as well as with their corporate customer. And one of the hazards of claims handling under fronting or retro premium claims is that the claims administrator often has little incentive to minimize costs where funding ultimately comes from the corporation itself, under which the corporation may have little say in how the funds are expended.

B. Who should receive notice, and how transmitted?

Notification should be given to any and all insurers who potentially might provide coverage for a particular claim or loss. That is a simple enough principle, but given the wide array of policies and coverages noted above, it is sometimes difficult to determine in practice.

It is virtually always better to err on the side of over-inclusion, than to inadvertently leave out notice to an insurer whose policy later proves to provide potential coverage. Inevitably, the determination of which insurers to notify involves a close review and evaluation of the nature of the loss or claim, and of the terms and scope of various insurance policies that could apply.

Likewise, how and to whom notification must be given is largely driven by policy wording. It is a rare policy that fails to include specifications for notice of a loss, occurrence, claim or suit, typically found in Declarations or Certificate provisions at the front of policy wording. These details may be best known to and accessible by the insurance broker, so even where Risk Management or the Legal Department has initial responsibility for handling, the broker often is called upon to physically implement notification to relevant insurers or their delegated representative.

C. Consequences of faulty notice

At best, faulty notice can create unnecessary issues in obtaining cooperation and coverage from the insurer; at worst, faulty notice may wholly defeat coverage that otherwise would have applied.

In all events, Texas courts normally will not require the insurer to pay pre-tender defense costs, so it is in the policyholder's interest to provide notice before incurring any such expenses. *See Coastal Ref. & Mktg., Inc. v. U.S. Fid. & Guar. Co.*, 218 S.W.3d 279, 294 (Tex.App.-Houston [14th Dist.] 2007, pet. denied)("Because an insurer's duty to defend is triggered by notice, the insurer has no duty to reimburse the insured for defense costs incurred before the insured gave the insurer notice of the lawsuit.") *citing E & L Chipping Co., Inc. v. Hanover Ins. Co.*, 962 S.W.2d 272, 278 (Tex.App.-Beaumont 1998, no pet.).

As a general rule, when the policyholder breaches a condition of the policy prescribing notice, the breach must be considered "material" before the insurer may avoid coverage. Typically, policy wording in an "occurrence" based policy requires notice somewhat flexibly "as soon as practicable" or similarly. Under that sort of policy and wording, the insurer must show that is was tangibly "prejudiced" by faulty notice, to prove materiality and avoid policy obligations. *See PAJ, Inc. v. Hanover Ins. Co.*, 243 S.W.3d 630 (Tex. 2008); *Lennar Corp. v. Markel Am. Ins. Co.*, 413 S.W.3d 750 (Tex. 2013).

However, when a notification provision is part of the bargained-for coverage, as with claims-made policies, notice must be given with strict compliance regardless of any evidenced prejudice to the insurer. *See Matador Petroleum Corp. v. St. Paul Surplus Lines Ins. Co.*, 174 F.3d 653, 658 (5th Cir. 1999)(requiring strict compliance with notification timetable of pollution buy-back endorsement); *Starr Indem. & Liability Co. v. SGS Petroleum Serv. Corp.*, 719 F.3d 700, 704 (5th Cir. 2013)(same); *see also Prodigy Communications Corp. v. Agricultural Excess & Surplus Ins. Co.*, 288 S.W.3d 374 (Tex. 2009)(noting with agreement the general rule that notice under claims-made policies is part of the bargained-for contract, but applying prejudice rule where policyholder complied with "as soon as practical" wording of particular policy); *Fin. Indus. Corp. v. XL Specialty Ins. Co.*, 285 S.W.3d 877 (Tex. 2009)(same observation and result where policyholder effected notice within policy's specified extension of time).

These principles were reviewed and confirmed recently by *Greene v. Farmers Insurance Exchange*, 446 S.W.3d 761 (Tex. 2014). But *Greene* also circumscribed the prejudice rule, holding that a vacancy clause in a homeowners policy was a core aspect of the bargained-for risk, that it did not act as a condition that a policyholder breaches, nor as an exclusion for purposes ot eh anti-technicality statute. And so the policy lapsed by its terms when the property was vacant beyond the specified time, nowithstanding that the insurer was not prejudiced because the particular loss was not caused by or related to the vacancy.

In the third article in this series we will discuss engaging in coverage litigation.