

Approach with reservation



James Cooper,
partner
Clyde & Co

As discussed at Clyde & Co's second annual Clyde & Co financial institutions conference last month, which

was attended by more than 170 market professionals, making a reservation of rights in the right way and at the right time is a key issue in the proper management of relationships between insurer, insured and broker.

This is an area the Association of Insurance and Risk Managers (Air-

mic), together with its insurance partners, has been looking at closely and is close to releasing a model clause that would be legally binding when incorporated into insurance contracts.

However, drawing the right balance between being specific enough, while also ensuring ade-

quate protection against the back-drop of a complex claim, where potentially huge amounts are at stake, is not an easy one for insurers.

Added to this, financial institutions insurers with an international book will often need to navigate the differing principles applying in other jurisdictions, including some where a reservation of rights is not recognised.

For example, while the rules applying to reservation of rights in

the US are similar to the UK, in practice reservations in the US are much more specific, to counter any risk of opening the insurer up to extra-contractual liability claims of misrepresenting the scope of coverage.

Getting it right can be a minefield and the risks of getting it wrong can be commercially and financially painful. The table below acts as a cut-out-and-keep guide to the main principles and practices in a number of key jurisdictions. ■

Table: Reservation of rights (ROR)

Country/state	Is an ROR recognised?	Is an ROR needed to avoid insurers being taken to have waived their rights?	Main principles
UK	Yes, it is recognised in English law.	An ROR may prevent the underwriter losing its right to rely on a defence to a claim under the policy. Defences can easily be lost simply by reason of the underwriter's conduct or lack of it. For example, the underwriter's defences and rights could be lost by: the insurer waiving its rights, affirming a contract which it could have avoided or by being estopped from relying on its rights.	1) The ROR wording must be explicit to be effective in respect of all identifiable defences and, in particular, should cover rights the insurer wishes to preserve; 2) Insurers do not have to reserve rights immediately; reasonable time may be spent investigating. However, delay in communication of the decision to the insured can itself be grounds for waiver by affirmation if the insurer has reason to believe the claim will be met; 3) Even an express ROR could be ineffective if the insurer later represents this will not be enforced.
US	Yes, it is recognised in US law. It is often, though not always, required for an insurer to preserve its rights to invoke a coverage defence. To avoid the possibility of losing the right to assert a coverage defence based on waiver or estoppel it is best practice for an insurer to issue an ROR letter.	Depending on the coverage defences at issue and which state law applies, insurers may be deemed to have waived rights to assert a coverage defence if it does not issue a timely and sufficient ROR letter. An insurer may also be estopped from asserting a coverage defence if it takes action the insured justifiably relies upon to its detriment. Therefore, insurers defending or investigating claims should issue an ROR letter fully informing insureds of their position and right to withdraw from the defence or deny coverage if it is determined the policy does not provide coverage for the claim.	Insurers should send an ROR letter as soon as possible after becoming aware of a potential coverage defence. Some states impose certain time limits. The letter should: 1) Be specific and identify the policy by number and type of coverage, describe allegations and facts of the claim, specify the purpose of the letter is to reserve insurer's rights (expressly using the phrase "reservation of rights"), and refer to/quote specific policy provisions relied upon; 2) Include a "catch all" phrase confirming the insurer reserves all rights and defences under the policy, at law and in equity, including the right to assert additional coverage defences at a later date, and that it does not waive any other defences; 3) Specify whether the insurer will fund or assume control of the defence of underlying litigation, reserve the right to withdraw from the defence at a later date and reserve the right to seek recoupment of costs paid, if permissible; 4) Request the insured's co-operation with investigations and advise of the insurer's right to consent to and participate in settlement negotiations.
Hong Kong	Yes, under common law, an ROR is recognised under Hong Kong law.	By its representations or conduct, an underwriter may be deemed to have waived rights to rely upon the failure of an insured to comply with a policy condition. The underwriter may also, by conduct, be deemed to have affirmed the policy for non disclosure. A waiver, once effected, is irrevocable and final. A ROR may be effective in preventing a finding that underwriters have waived their rights.	Similar to the position in England, any ROR must be clear and unambiguous. It should be made before, or contemporaneous with, any conduct which could be construed as waiving any of underwriters' rights.
France	Yes, it is recognised in French law. An ROR notice is not always determinative, however. It is best practice to make an ROR and it is more likely to be recognised by the courts if it is sufficiently specific.	The Insurance Code requires when an insurer assumes conduct of proceedings against the insured ("direction du procès") a reservation of rights is made. If the insurer proceeds without such reservation, he is deemed to have waived his defences (though there is some debate as to which defences are deemed to have been waived). So, issuing a specific reservation is recommended.	1) Issuing a notice of ROR is good practice. It does not require any particular form of words, but must be unambiguous; 2) An ROR is a legal requirement in cases where the insurer assumes conduct of proceedings against the insured. Failure to do so amounts to a waiver of all defences including exclusions, avoidance/non-disclosures, forfeitures but does not include, defences pertaining to clauses defining the scope of coverage positively, conditions or policy limits.
Canada	Yes, and it is seen as a necessary evil when a non-waiver agreement cannot be negotiated. Whether an ROR entitles an insured to a separate defence counsel is a relatively nascent issue. Generally, insurers have the right to control the defence, where there is a "reasonable apprehension" of a conflict of interest, but that right is not absolute.	Generally, if an insurer does not advise the insured of the areas of the claim that are not covered by the policy at the time when it is first reported, and the insured is prejudiced as a result, the doctrines of "waiver" and estoppel will apply against the insurer and the insurer will be deemed to have waived the breach of the policy and will be estopped from pleading that breach.	1) An insurer should act quickly in deciding its course of action; 2) A ROR should be drafted unambiguously as this may allow the insurer to recover monies paid on settlement; 3) A properly drafted ROR will protect the insurer from an insured's action for the reimbursement of legal fees awarded against it.
Brazil	Yes. Neither an ROR nor a rights "waiver" are expressly provided for in Brazilian law. It is best practice for an insurer to issue an ROR notice when the insurer is unsure about invoking a coverage defence, or is investigating coverage.	Failure to reserve rights under a policy may not amount to a waiver if an investigation of coverage conducted by the insurer is ongoing. The principle of good faith under the Brazilian Federation Constitution allows an insurer to take steps to lessen the extent of its potential loss while investigations are pending and still invoke a coverage defence at a later date. This position is more difficult to maintain, however, if the insurer admits a claim, or liability, and later changes his mind.	Contractual stipulations providing for protection/reservation of rights in Brazilian policies are now common practice.
Russia	An ROR is not recognised in Russian law (in a manner analogous to English law), nor is a rights "waiver" or affirmation of a contract.	The Civil Code of the Russian Federation sets out the basic legal principle "refusal to exercise civil rights that belong to an individual or a legal entity, shall not result in termination of such rights, save for the cases expressly provided by law". So, if an individual/legal entity does not execute its rights, it does not terminate those rights altogether, and legally such rights could be executed at a later date (unless expressly provided for by law).	Not applicable
UAE	An ROR is recognised in UAE law.	A rights "waiver" is not a well-developed concept in UAE law but is expressly referred to in the UAE Civil Code. A "waiver" may operate where there is action inconsistent with a previously adopted position. Provided a general ROR is in place throughout the investigation of the claim, and is repeated over the course of the claim, re/insurers should not be precluded from invoking coverage defences.	1) In the absence of detailed legal provisions and comprehensive reporting of cases there is little guidance on the doctrine of a rights "waiver" and how re/insurers can lose their coverage defences; 2) However, when a coverage dispute comes before the UAE Courts, they may appoint an insurance expert to report on insurance aspects and coverage. In general, the court-appointed expert will be guided by international best practice so proper application of an ROR notice will be of assistance in protecting a re/insurers' position; 3) There is no without-prejudice protection under UAE law so re/insurers need to be careful to avoid taking "without prejudice" or "in the alternative" positions on coverage which could be deemed an admission of policy response.
Australia	An ROR is recognised in Australian law.	There is no legal requirement for an insurer to provide an ROR. However, the doctrines of election and estoppel (interchangeably described in the courts by the term "waiver") may hamper the insurer's defence if it fails to notify the insured of claims that would not otherwise be covered under the policy when a claim was initially reported. Also, an insurer who is liable to pay an insured will be liable to pay interest on the claim from the date from which it was unreasonable for the insurer to have withheld payment.	1) Best market practice suggests it would be prudent for insurers to include an unambiguously drafted ROR notice outlining their position in respect of all particular defences and the rights they wish to sustain; 2) Noting however, insurers would be ill advised to wait should they decide to provide an ROR notice. While mere effluxion of time has not been held to be an affirming action, a delay coupled with any conduct in accordance with the contract could constitute an affirmation.