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NEWSLETTER

Insurer May Recover Legal Fees Paid to Defend Claim When Insured Has Recovered the Fees from Another Party

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A Texas appellate court has held that, under Texas law, an insurer may seek reimbursement from an insured for defense costs incurred in an underlying legal malpractice lawsuit that were paid by the insurer and recovered by the insured as part of a counterclaim. *St. Paul Fire & Marine Ins. Co. v. Beirne, Maynard & Parsons, LLP,* No. 01-00-01065-CV, 2002 WL 31771102 (Tex. App. Ct. Dec. 12, 2002).

The insurer issued to a law firm a professional liability insurance policy that required the insurer to pay defense costs for claims covered by the policy. The policy also provided that "[a]ny person protected under this policy may be able to recover all or part of a loss from someone other than us.... If [the insurer makes] a payment under this policy that right of recovery will belong to us." A former client sued the law firm for legal malpractice, and the insurer, reserving all of its rights, paid the defense costs. The law firm successfully counterclaimed for its defense costs, and ultimately recovered all of its expenses, including those paid by the insurer. When the law firm refused to reimburse the insurer from the money recovered, the insurer filed suit.

On appeal, the Texas appellate court reversed the lower court's decision awarding summary judgment to the law firm. The court first rejected the law firm's argument that the insurer was not entitled to any of the defense costs because the award in the underlying action had been only to the law firm and not to the insurer. The court reasoned that the policy language addresses recovery of all or part of a loss from a third party and gave the insurer a right of recovery. The court also rejected the law firm's argument that the term "loss" did not include defense costs, reasoning that total coverage under the policy could be depleted equally for settlements, awards and defense costs and that, as a result, any such payment constituted a "loss."

The court then rejected five affirmative defenses asserted by the law firm. The court first rejected the law firm's argument that the insurer was seeking to attack collaterally the judgment in the underlying suit, reasoning that the insurer merely sought reimbursement from the prior judgment for expenses paid during that suit. The court next held that the law firm did not satisfy any of the requirements for collateral estoppel

because the issue of reimbursement was not litigated in the underlying lawsuit and the insurer and the law firm were not adverse parties in that proceeding. Similarly, the court also held that the law firm did not conclusively satisfy the elements of res judicata. Although the insurer was seeking reimbursement from the law firm for defense costs incurred while defending the law firm in the underlying suit, the insurer's claims did not arise out of the same transaction that was at issue in the underlying action. The court rejected the law firm's argument that the insurer was judicially estopped from taking the position it did, reasoning that the insurer was not a party to the underlying action, and that it therefore could not have made any allegations or admissions in that proceeding that would contradict its position in the subsequent reimbursement action. Finally, the appellate court rejected the law firm's argument that the insurer did not provide timely notice of its reimbursement claim, as required by Texas law. In support of its notice defense, the law firm relied on a case where an insurer had settled a claim on behalf of the insured without providing notice and subsequently denied coverage and sought reimbursement. The appellate court found the case readily distinguishable because the insurer was not seeking to deny coverage, nor was it seeking to recover costs from the law firm's pocket. Instead, it was seeking to recover costs awarded as part of a judgment that included those costs.

For more information, please contact one of WRF's Professional Liability Attorneys at 202.719.7130.