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NEWSLETTER

Tenth Circuit Predicts That Colorado Law Permits Insurer To Recoup Defense Costs

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Predicting Colorado law, the Tenth Circuit has held that an insurer may, after an adjudication that its policy provides no coverage, recoup defense costs it advanced even if the policy does not explicitly provide for recoupment. *Valley Forge Ins. Co. v. Health Care Mgmt. Partners, Ltd.*, 2010 WL 3211170 (10th Cir. Aug. 16, 2010).

The insurer provided the policyholder with a defense in an underlying medical fraud case but advised the insured that it did not believe the policy provided coverage. It sent a reservation of rights letter stating that it reserved the right to seek reimbursement of the defense costs it advanced in the event that coverage did not exist. The policyholder accepted the defense, did not object to the reservation of rights letter, and was generally aware of the costs of defense throughout the underlying litigation. The insurer subsequently sought and obtained a declaration that its policy did not provide coverage. After affirmance of that judgment on appeal, the district court granted the insurer summary judgment on its claim to recoup its defense costs from the policyholder.

Relying on two Colorado Supreme Court cases that discussed in general terms an insurer's right to recoupment, the Tenth Circuit predicted that the Colorado courts would recognize such a right even if the policy did not specifically include it, so long as the insurer reserved its right to recoup when providing the defense. The court also rejected the policyholder's argument that the insurer's pursuit of a declaratory judgment before the underlying action concluded should cut off any recoupment right. The court noted that the policyholder identified no prejudice it suffered from the declaratory judgment action, so the action was permissible under Colorado law.

The policyholder also argued that the insurer should only be able to recoup reasonable defense costs, as opposed to actual defense costs. The court rejected the policyholder's argument without deciding if Colorado law would impose such a requirement because it found the policyholder did not introduce any evidence that the actual defense costs incurred were unreasonable.