

California Statute Limiting Defense Costs Does Not Apply Where Carrier Denies Coverage

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The United States District Court for the Central District of California has held that if a policyholder is able to establish that its insurer breached the duty to defend by denying coverage, the insurer cannot limit the policyholder's recovery for attorneys' fees under California Civil Code section 2860. *Browne George Ross LLP v. Lexington Ins. Co.*, No. 2:10-cv-02148-SVW-PLA (C.D. Cal. May 29, 2012).

The insured attorney was sued by several former clients for legal malpractice and provided timely written notice of the suit to his two professional liability insurance carriers. One carrier denied the claim and refused to provide a defense. The insured hired a law firm to represent him in the underlying legal malpractice action, splitting the defense costs with the carrier that had not denied the claim. The insured incurred over \$1 million in defense costs and ultimately prevailed in the underlying action. He then sued the denying carrier for breach of contract and sought reimbursement for the defense costs not covered by the other carrier.

The defendant carrier moved to dismiss, arguing that the insured was precluded from bringing a claim against the defendant carrier for breach of the duty to defend because the insured had received a defense from another carrier. The defendant carrier contended that the insured's total recovery of attorneys' fees, from all insurers, was limited by Cal. Civ. Code § 2860, which provides that:

When the insured has selected independent counsel to represent him or her . . . [t]he insurer's obligation to pay fees to the independent counsel selected by the insured is limited to the rates which are actually paid by the insurer to attorneys retained by it in the ordinary course of business in the defense of similar actions in the community where the claim arose or is being defended.

The court rejected the carrier's argument. The court held that under California law, if an insured establishes that a carrier breaches its duty to defend, the insured's damages are not limited by Cal. Civ. Code § 2860. According to the court, a carrier must accept tender of an insured's defense, subject to a reservation of rights, in order to take advantage of this statute. The court also held that whether the attorneys' fees already paid for by the other carrier met or exceeded the amount recoverable under Cal. Civ. Code § 2860 was an issue of fact and therefore inappropriate for resolution on a motion to dismiss.