

Fifth Circuit Affirms Insurer's Right to Select Defense Counsel

November 2012

The United States Court of Appeals for the Fifth Circuit, applying Texas law, has affirmed a district court decision holding that an insurer's reservation of rights did not create a conflict of interest entitling an insured to select independent counsel to defend an underlying legal malpractice lawsuit. *Coats, Rose, Yale, Ryman & Lee, P.C. v. Navigators Spec. Ins. Co.*, 2012 WL 4858194 (5th Cir. Oct. 15, 2012). Wiley Rein LLP represented the insurer in this case in both the district and appellate courts.

An insured law firm sought coverage under its lawyers professional liability insurance policy for a legal malpractice action. The policy provided that the insurer had the right to appoint defense counsel for claims against the insured. The insurer agreed to provide a defense under a reservation of rights, including the right to deny coverage for the return of fees, which did not come within the policy's definition of "Damages." However, the law firm, asserting that the insurer's selected counsel would have a conflict of interest, hired independent defense counsel. The insurer concluded there was no conflict of interest with its insured and therefore declined to pay the fees of the law firm's chosen counsel.

In subsequent litigation regarding whether the insurer's reservation of rights entitled the law firm to select independent counsel, the district court ruled for the insurer and the appellate court affirmed. Under Texas law, the court stated, only an actual conflict of interest, and not a potential conflict, triggered an insured's right to independent counsel. The law firm had argued that the insurer's reservation with regard to the return of fees created a conflict because it would discourage the insurer from resisting factual findings that would result in a return of fees award. The insurer argued that this did not constitute a conflict of interest because any factual concession would increase the likelihood of compensatory damages. The court agreed with the insurer, explaining that a return of fees award would not be in lieu of compensatory damages, and, moreover, any concession of fact that would lead to a return of fees award would also, by acknowledging wrongdoing, increase the amount of a compensatory damages award. As such, the court held that the insurer's reservation of rights with regard to the return of fees did not create a conflict.

The court also rejected the law firm's argument that a conflict arose when the insurer stated in a reservation of rights letter that it "did not in [its] prior letters and is not now" reserving rights with regard to the policy's dishonesty exclusion. The law firm argued that the insurer's future ability to reserve rights under the exclusion entitled the firm to independent counsel. The court disagreed, holding that the insurer expressly had not

reserved its rights on the dishonesty exclusion, and thus no conflict existed.