

# SC Court Rules in Favor of Insurer, Allowing Them To Recoup Defense Costs

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**The United States District Court for the District of South Carolina** recently held that an insurer was entitled to recover defense costs.

These costs were incurred while defending the insured under a reservation of rights where the professional liability insurance policy did not provide coverage for a malpractice claim.

In the case, the would-be plaintiff hired the insured law firm to file a wrongful death action. The law firm missed the deadline for filing the complaint. As a result, the lawsuit was dismissed with prejudice. The plaintiff then brought a professional malpractice lawsuit against the law firm.

After the dismissal of the wrongful death lawsuit but before the professional malpractice lawsuit against the insured was filed, the insured law firm executed a renewal application for its professional liability insurance. As part of the renewal application process, the firm certified that no lawyer in the firm was aware of any potential malpractice claim against any of the firm's lawyers. The policy also contained a provision that if the insurer provided a defense for an uncovered claim, the insurer was entitled to reimbursement for defense costs.

The law firm's professional liability insurer agreed to defend the insured subject to a reservation of rights and filed a declaratory judgment action to determine its defense duties.

The Court granted summary judgment in favor of the insurer in the declaratory judgment action, finding that the insured had prior knowledge of the potential claim before the inception of the policy. The insurer argued that the insured should have provided notice of a potential claim as soon as the insured became aware of the statute of limitations issue or when the lawsuit was dismissed with prejudice.

The Court agreed, finding that the insured became objectively aware of facts which would "subjectively lead a reasonable attorney" to believe there may be a professional malpractice claim made prior to the inception of the policy and at the time that the insured certified it was unaware of any potential claim when applying for the policy.

Accordingly, the Court found that the prior knowledge exclusion of the policy applied and coverage for the professional malpractice lawsuit was excluded, and the insurer was entitled to summary judgment.

The Court held that because there was no coverage for the malpractice lawsuit, the insurer had no duty to defend or indemnify the insured law firm. Further, the insurer was entitled to reimbursement for the defense costs spent because the insured was being defended subject to a reservation of rights and the policy expressly provided for reimbursement.

The insurer has specifically reserved the right to reimbursement of defense costs. Accordingly, the insurer was entitled to reimbursement of the full amount paid to defend the law firm in the malpractice lawsuit.

**What it means for insurers**

The District Court's decision not only reiterates the importance of reservation of rights letters in South Carolina, but also provides support for an insurer to seek reimbursement for defense costs from an insured where a court has affirmatively held that there is no duty to defend and indemnify the insured, the policy provides for reimbursement of defense costs, and the insurer has reserved the right to reimbursement.

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