I. REGULATORY LIMITS ON CLAIMS HANDLING

For a complete enumeration of improper claims practices, see 215 ILCS 5/154.6. No private cause of action exists for violating any of these provisions. American Service Ins. Co. v. Passarelli, 323 Ill.App.3d 587, 590 (1st Dist. 2001). However, an insurer that unreasonably and vexatiously denies a claim or delays payment of a claim may be liable for attorneys’ fees and a penalty of 60% of the amount the party is entitled to recover under the policy up to a maximum of $60,000. 215 ILCS 5/155.

A. Timing for Responses and Determinations

The Illinois Insurance Code does not set forth explicit time limitations on the settlement or determination of claims. However, the Code does state that time taken to affirm or deny coverage claims must be “reasonable.” 215 ILCS 5/154.6(i).

B. Standards for Determinations and Settlements

The Illinois Insurance Code provides guidelines for protecting the rights of an insured in the claim process, and specifies eighteen acts of improper claims practices. These include:

- Knowingly misrepresenting relevant facts or policy provisions relating to the coverage at issue.
- Failing to acknowledge communications from the insured.
- Not attempting in good faith to effectuate prompt, fair and equitable settlement of claims where liability is reasonably clear.
- Compelling policyholders to sue to recover amounts due under its policies by offering substantially less than the amounts ultimately recovered.
- Refusing to pay claims without a reasonable investigation.
- Delaying the investigation or payment of a claim by requiring the insured to submit a preliminary claim report and then requiring a subsequent formal proof of loss, resulting in duplication of verification.
• When denying or offering a compromise in a claim, failing to provide a reasonable and accurate explanation of the basis in the policy or law for the denial or compromise.


C. Privacy Protections (In addition to Federal Gramm-Leach-Bliley Act)

Illinois law provides insureds with an individual remedy for an insurer’s violation of the Illinois Insurance Code provision relating to privacy protection. 215 ILCS 5/1021. An individual may apply to the circuit court for equitable relief from such a violation.

An insurer must provide an individual (who has supplied proper identification) with information recorded in the insured’s file. 215 ILCS 5/1009. The Insurance Code only requires that the insurer provide information that is reasonably described by the insured and reasonably locatable by the insurer. The insurer must provide such requested information within thirty (30) days of a written request. The information subject to this provision includes:

1. Personal information pertaining to the individual;

2. The identity of all persons to whom the insurer has disclosed personal information within two (2) years prior to the request;

3. A summary of procedures by which the individual may request correction, amendment or deletion of recorded information;

4. Medical record information and the identity of the medical professional or institution that provided the information.

The rights granted to individuals under the Insurance Code extend to all information collected and maintained about the insured by the insurer. The rights conferred by Section 5/1009, however, do not extend to information of reasonably anticipated claims or to civil or criminal proceedings relating to the insured.

Disclosure of personal and privileged insurance information is generally prohibited in the absence of written authorization from the insured. Section 1014 of the Illinois Insurance Code, 215 ILCS 5/1014, provides a list of limited situations under which the insurer may disclose such information, including:

1. where the disclosure of information would enable the recipient to perform a business function for the disclosing insurance institution, and the recipient agrees not to further disclose the information;

2. where the purpose of the disclosure is to provide the disclosing institution with information in order to determine eligibility for benefits or payment or to prevent criminal activity or fraud;
3. where confidential information is provided to a medical provider to verify coverage or inform the insured of a medical problem of which the insured may not be aware.

An individual claiming a violation of the disclosure limitation may only recover actual damages. 215 ILCS 5/1021. Section 1021 also provides for reimbursement of costs and attorney fees to the prevailing party in any action brought for equitable or monetary relief.

II. PRINCIPLES OF CONTRACT INTERPRETATION

Interpretation and construction of insurance contracts are governed by the same general provisions as those governing other contracts. Hobbs v. Hartford Ins. Co., 214 Ill. 2d 11, 17, 823 N.E.2d 561, 564 (2005); Dempsey v. Nat’l Life & Accident Ins. Co., 404 Ill. 423, 426, 88 N.E.2d 874, 876 (1949). The court’s primary objective is to ascertain and give effect to the parties’ intention as expressed by the policy language. If the terms of an insurance policy are clear and unambiguous, they must be given their plain, ordinary and popular meaning. Central Illinois Light Co. v. Home Ins. Co., 213 Ill.2d 141, 153 (2004); Outboard Marine Ins. Corp. v. Liberty Mutual Ins. Co., 154 Ill.2d 90, 108 (1992). Terms in insurance policies are deemed ambiguous if they are susceptible to more than one reasonable interpretation. Gilien v. State Farm Mut. Auto. Ins. Co.; 215 Ill.2d 381, 393 (2005); Rich v. Principal Life Ins. Co., 226 Ill. 2d 359, 371, 875 N.E.2d 1082, 1090 (2007); Cincinnati Ins. Co. v. Dawes Rigging & Crane Rental, Inc., 321 F.Supp.2d 975, 980 (C.D. Ill. 2004). If policy terms are ambiguous, courts shall consider extrinsic material such as the subject matter of the contract, purpose sought to be accomplished, and circumstances surrounding issuance of the policy. Adman Prods. Co. v. Fed. Ins. Co., 187 Ill. App. 3d 322, 325, 543 N.E.2d 219, 221 (1st Dist. 1989); Seeburg Corp. of Del. v. United Founders Life Ins. Co. of Ill., 82 Ill.App.3d 1034, 1039, 403 N.E.2d 503, 506 (1st Dist. 1980). Any ambiguities will be construed against the insurer and in favor of the insured. Gilien, 215 Ill.2d at 393; Rich v. Principal Life Ins. Co., 226 Ill. 2d 359, 371; Cincinnati Ins. Co., 321 F.Supp.2d at 980. Policy provisions that purport to exclude or limit coverage will be narrowly construed and applied only where the terms are clear, definite and specific. Gilien, 215 Ill.2d at 393.

III. CHOICE OF LAW

Illinois utilizes the “most significant contacts” test in assessing governing law. This test provides that choice of law for insurance policy disputes is determined by the location of the subject matter, the place of delivery of the contract, the domiciles of the insurer and insured, the location of the last act to give rise to a valid contract, the place of performance, or any other place with a rational relationship to the general contract. Lapham-Hickey Steel Corp. v. Protection Mut. Ins. Co., 166 Ill.2d 520, 526-27 (1996); Cincinnati Ins. Co. v. Dawes Rigging & Crane Rental, Inc., 321 F.Supp.2d 975, 980 (C.D. Ill. 2004). Under this choice of law rule, the location of the insured risk is given special emphasis in choosing which law governs insurance policy disputes. Society of Mt. Carmel v. National Ben Franklin Ins. Co. of Ill., 268 Ill.App.3d 655, 664 (1st Dist. 1994); Jupiter Aluminum Corp. v. Home Ins. Co., 225 F.2d 868, 874 (7th Cir. 2000).

IV. DUTIES IMPOSED ON INSURERS
A. Duty to Defend

1. Standard for Determining Duty to Defend

In determining whether an insurer has a duty to defend its insured, the court must look to the allegations in the underlying complaint and the relevant provisions of the insurance policy. American States Insurance Co. v. Koloms, 177 Ill. 2d 473, 479, 687 N.E.2d 72 (1997). A court will look to the four corners of the complaint brought against the insured to determine if a potential for coverage exists. Illinois National Ins. Co. v. Universal Underwriters Ins. Co., 261 Ill. App. 3d 84, 88 (5th Dist. 1994). If the underlying complaint alleges facts within or potentially within the policy coverage, the insurer is obligated to defend its insured even if the allegations are groundless, false or fraudulent. State Farm Fire & Cas. Co. v. Martin, 186 Ill. 2d 367, 378, 710 N.E.2d 1228, 1234 (1999); U.S. Fidelity & Guaranty Co. v. Wilkin Insulation Co., 144 Ill. 2d 64, 73 (1991).

An insurer may not justifiably refuse to defend an action against its insured unless it is clear from the face of the underlying complaint that the allegations fail to state facts which bring the case within, or potentially within, the policy's coverage. Id. When the insurer has a duty to defend, it may not simply refuse to defend. Rather, the insurer has two options: (1) it can defend the suit under a reservation of rights; or (2) seek a declaratory judgment that there is no coverage. Employers Ins. Co. v. Ehlco Liquidating Trust, 186 Ill.2d 127, 150 (1999); State Farm Fire & Cas. Co. v. Martin, 186 Ill. 2d 367, 379, 710 N.E.2d 1228, 1234 (1999); Waste Management, Inc. v. International Surplus Lines Ins. Co., 144 Ill. 2d 178, 207-08 (1991). If the insurer fails to take either option, and is later found to have breached the duty to defend, it will be estopped from later raising policy defenses and is liable for the award against the insured and the costs of the suit. Employers Ins. v. Ehlco, 186 Ill.2d at 150-51; Murphy v. Urso, 88 Ill.2d 444, 451 (1981); Maryland Cas. Co. v. Peppers, 64 Ill.2d 132, 144 (1976).

All doubts concerning the scope of coverage are resolved in favor of the insured. U.S. Fidelity v. Wilkin Installation Co., 144 Ill.2d 64, 74, 578 N.E.2d 926, 930 (1991). An insurer has no duty to defend only where the allegations of the underlying case clearly fail to state facts that bring the case within or potentially within the policy's coverage. Employers Ins. Of Wausau v. Ehlco Liquidating Trust, 186 Ill.2d 127, 153, 708 N.E.2d 1122, 1136 (1999).

While Illinois generally follows the eight corners rule, looking to the four corners of the complaint and the four corners of the policy to determine the duty to defend, an insurer may rely on extrinsic evidence to deny a duty to defend if it brings an action for declaratory judgment. Compare, Employers Ins. of Wausau v. Ehlco Liquidating Trust, 186 Ill.2d 127, 150 (1999) (Insurer estopped from denying coverage where it failed to defend or seek declaratory judgment, and could not rely on insured’s late notice to avoid duty to defend since late notice was not apparent from underlying complaint); Chandler v. Doherty, 299 Ill.App.3d 797 (4th Dist. 1998) (insurer estopped from denying coverage based on fact that car involved in accident was not an insured vehicle, and could not rely on extrinsic evidence to establish that it had no coverage where it failed to file a declaratory judgment action); with Fidelity & Casualty Co. of N.Y. v. Envirodyne Engineers, Inc., 122 Ill.App.3d 301, 305 (1st Dist. 1983) (insurer that filed declaratory action allowed to rely on extrinsic evidence to deny duty to
2. **Issues with Reserving Rights**

A reservation of rights letter must adequately inform the insured of those rights that the insurer intends to protect and must specifically reference the policy defenses that the insurer intends to assert. *Royal Ins. Co. v. Process Design Assoc., Inc.*, 221 Ill.App.3d 966, 973, 582 N.E.2d 1234, 1239 (1st Dist. 1991). This specific reservation of rights allows the insured to make an educated decision whether to retain its own counsel or accept defense counsel from the insurer. Id. at 973-74, 582 N.E.2d at 1239.

An insurer’s duty to defend typically includes the right to control that defense in order to both protect its financial interest in the litigation’s outcome and minimize unwarranted liability claims. *Illinois Masonic Medical Center v. Turegum Ins. Co.*, 168 Ill.App.3d 158, 163, 522 N.E.2d 611, 613 (1st Dist. 1988). This presents no problems where the interests of the insurer and the insured are completely aligned. *American Family Mut. Ins. Co. v. W.H. McNaughton Builders, Inc.*, 363 Ill.App.3d 505, 511, 843 N.E.2d 492, 498 (2nd Dist. 2006). However, where these interests divert, this arrangement may potentially lead to a conflict of interest.

A conflict of interest exists where a comparison of the underlying complaint to the policy terms demonstrates an opportunity for insurer-retained counsel to shift facts in a way that takes the case outside the scope of policy coverage. *W.H. McNaughton Builders*, 363 Ill.App.3d at 511. Although the attorney retained by the insurer to represent the insured has ethical obligations to both parties, in reality the attorney may have closer ties to the insurer and thus a more compelling interest to protect the insurer. Id. Where such a conflict of interest exists, the insurer must decline to defend the insured and, instead of participating in the defense, the insurer must pay for independent counsel for the insured. *Murphy v. Urso*, 88 Ill.2d 444, 451-52, 430 N.E.2d 1079, 1082 (1981); *Maryland Cas. Co. v. Peppers*, 64 Ill.2d 132, 144 (1976).

The federal courts in Illinois have also held that there is a conflict of interest, requiring independent counsel, where there is a “non-trivial probability” of a verdict in excess of the policy limits. *R. C. Wegman Const. Co. v. Admiral Ins. Co.*, 629 F.3d 724, 730 (7th Cir. 2011); *Perma-Pipe, Inc. v. Liberty Surplus Lines Ins. Corp.*, 38 F.Supp.3d 890, 896 (N.D.Ill. 2014). No Illinois state courts have yet adopted this view.

A reservation of rights letter must specifically reference any potential conflict of interest.” *Mobil Oil Corp. v. Maryland Cas. Co.*, 288 Ill.App.3d 743, 754, 561 N.E.2d 552, 560 (1st Dist. 1997) (citing *Royal Ins. Co.*, 221 Ill.App.3d at 973, 582 N.E.2d at 1239). This allows the insured to decide intelligently whether or not to hire independent counsel in order to avoid the conflict. Id. An insurer who defends its insured without disclosing the conflict of interest in its reservation of rights is estopped from subsequently raising coverage defenses. *Doe v. Illinois State Medical Inter-Insurance Exchange*, 234 Ill.App.3d 129, 134, 599 N.E.2d 983, 986 (1st Dist. 1992).

V. **EXTRA CONTRACTUAL CLAIMS AGAINST INSURERS**
A. Bad Faith

1. First-Party Claims

Illinois law does not recognize a first-party claim for bad faith as a separate and independent tort action. Cramer v. Ins. Exchange Agency, 174 Ill.2d 513, 525-26, 675 N.E.2d 897, 904 (1996). Ordinarily, a policyholder may bring a breach of contract action against the insurer to recover the proceeds due under the policy. Section 155 of the Illinois Insurance Code also allows the policyholder to recover reasonable attorney fees and other costs, as well as an additional sum that constitutes a penalty. Id.; 215 ILCS 5/155. A first-party claim for bad faith does not allow the recovery of punitive damages except for the statutory penalty, which is currently limited to $60,000 or 60% of the amount the insurer owes, whichever is less. Id.

2. Third Party Claims

A separate and independent tort action for bad faith does exist, however, where the insurer unreasonably fails to settle a third party suit against its insured that exposes the insured to a judgment in excess of its policy limit. Cramer, 174 Ill.2d at 525, 675 N.E.2d at 903. Unlike first-party bad faith actions, third-party bad faith cases allow the recovery of punitive damages where the insurance company acts particularly egregiously. O’Neill v. Gallant Ins. Co., 329 Ill.App.3d 1166, 1176, 769 N.E.2d 100, 109 (5th Dist. 2002).

An insurer has an obligation to act in good faith toward its insured when exercising its right to settle a liability claim against the insured. Haddick v. Valor Insurance, 198 Ill.2d 409, 763 N.E.2d 299 (2001); Cramer v. Insurance Exchange Agency, 174 Ill.2d 513, 675 N.E.2d 897 (1997). The insurer is not required to place the insured’s interests ahead of its own, but is required to give at least equal weight to the insured’s interests when deciding to settle. The test often applied is whether a reasonable insurer, with no policy limits, would have declined to settle the claim. O’Neill v. Gallant Ins. Co., 329 Ill.App.3d 1166, 1172, 769 N.E.2d 100, 106 (5th Dist. 2002).

To have a duty to settle a claim, there must be a probability of both an adverse verdict and a verdict in excess of the policy limits. Powell v. Am. Serv. Ins. Co., 2014 IL App (1st) 123643, 7 N.E.3d 11, (2014)(must be reasonable probability of both adverse verdict and that verdict will exceed policy limit); Olympia Fields Country Club v. Bankers Indemnity Insurance Co., 325 Ill. App. 649, 670-71, 60 N.E.2d 896 (1945), quoting Hilker v. Western Automobile Insurance Co., 204 Wis. 1, 14, 235 N.W. 413, 414 (1931) (“When damages sought by a third party against the insured do not exceed policy limits, the question of whether the claim be compromised or settled, or the manner in which it shall be defended, is a matter of no concern to the insured.”)(internal quotations omitted).

Illinois courts rely on seven factors in assessing an insurer’s bad faith in failing to settle a claim within policy limits. These include:

(1) the advice of the insurance company’s own adjusters;
(2) a refusal to negotiate;
(3) the advice of defense counsel;
(4) communication with the insured; i.e., keeping the insured fully aware of the claimant’s willingness to settle within the policy limits;
(5) an inadequate investigation and defense;
(6) a substantial prospect of an adverse verdict; and
(7) the potential for damages in excess of the policy limits.

O’Neill, 329 Ill.App.3d at 1172-75, 769 N.E.2d at 106-08.

The duty to settle is not limited to situations in which suit has already been filed against the insured. Rather, the duty to settle arises once a third party claimant has made a demand for settlement within policy limits and, at the time of the demand, there is a reasonable probability of recovery in excess of the policy limits against the insured. Haddick v. Valor Insurance, 198 Ill.2d 409, 419, 763 N.E.2d 299 (2001).


B. Fraud

In order to state a cause of action for common law fraud, the plaintiff must plead the following elements with specificity: (1) a false statement of material fact; (2) the party making the statement knew or believed it to be untrue; (3) the party to whom the statement was made had a right to rely on the statement; (4) the party to whom the statement was made reasonably relied upon the statement; (5) the statement was made for the purpose of inducing the other party to act; and (6) the reliance by the person to whom the statement was made led to the claimant’s injury. Cramer, 174 Ill.2d at 528, 675 N.E.2d at 905.

The Illinois General Assembly has additionally provided a separate remedy for fraud that occurs in trade or commerce. In order to state a cause of action under the Consumer Fraud and Deceptive Business Practices Act, the plaintiff must allege: (1) a deceptive practice or act; (2) intent on the defendant’s part that the plaintiff rely upon the deception; and (3) that the deception occurred in the course of conduct involving trade or commerce. 815 ILCS 505/2.


Consumer Fraud claims are often subject to a motion to dismiss as they may be preempted by Section 155 of the Illinois Insurance Code. See Young v. Allstate Ins. Co., 351 Ill.App.3d 151, 169, 812 N.E.2d 741, 757 (1st Dist. 2004) (Illinois Insurance Code preempts claims made under the Consumer Fraud Act if the allegations made fall within the scope of Section 155).

C. Intentional or Negligent Infliction of Emotional Distress
To state a cause of action for intentional infliction of emotional distress, the plaintiff must allege the following: (1) that the defendant’s conduct was extreme and outrageous; (2) that the defendant either intended his conduct to inflict severe emotional distress or knew there was a high probability that the conduct complained of would cause severe emotional distress; and (3) that the defendant’s conduct caused severe emotional distress. *Graham v. Commonwealth Edison Co.*, 318 Ill.App.3d 736, 745, 742 N.E.2d 858, 866 (1st Dist. 2000).

To successfully sustain an action for intentional infliction of emotional distress, the plaintiff must allege more than mere insults, indignities, threats or annoyances. *Id.* The nature of the conduct must be so extreme as to go beyond all possible bounds of decency and be regarded as intolerable conduct within a civilized community. *Kolegas v. Heftel Broadcasting Corp.*, 154 Ill.2d 1, 21, 607 N.E.2d 201, 211 (1992). Whether conduct is extreme and outrageous is evaluated by using an objective standard, taking into account all of the surrounding facts and circumstances. *Graham*, 318 Ill.App.3d at 745, 742 N.E.2d at 866.

Illinois courts will consider the following factors in determining the outrageousness of a defendant’s conduct: (1) whether the defendant abused a position of authority over the plaintiff or his interests; and (2) whether the plaintiff is more susceptible to emotional distress because of a physical or mental condition. *Kolegas*, 154 Ill.2d at 21, 607 N.E.2d at 211; *McGrath v. Fahey*, 126 Ill.2d 78, 533 N.E.2d 806 (1988) (complaint pled sufficient facts for a claim of intentional infliction of emotional distress where a bank officer threatened a client known to have a heart condition in order to induce him to turn over property to the bank, and the client suffered a heart attack as a result of the threats).


Negligent infliction of emotional distress causes of action differ between direct victims and bystanders. A bystander who is in the “zone of physical danger” and, because of the defendant’s negligence, has a reasonable fear for his or her own safety, has a right of action for illness or physical injury resulting from such emotional distress. *Rickey v. Chi. Transit Auth.*, 98 Ill.2d 546, 555, 457 N.E.2d 1, 5 (1983). Accordingly, a bystander must prove that he or she suffered illness or physical injury. *Id.* A direct victim may only recover damages for negligent infliction of emotional distress if he or she can prove the defendant was negligent. *Corgan v. Muehling*, 143 Ill.2d 296, 306, 574 N.E.2d 602, 602 (1991). As such, a direct victim must establish that the defendant owed the victim a duty, the defendant breached that duty, and an injury was proximately caused by such breach. *Id.* at 574 N.E.2d at 602. Lastly, a direct victim must prove that he or she suffered damages in the form of an immediate severe or extreme emotional response, a severe and extreme long lasting traumatic neurosis, or both. *Id.* at 311, 574 N.E.2d at 608.

D. **State Consumer Protection Laws, Rules and Regulations**

The Illinois Insurance Code prohibits misrepresentation and defamation by insurers. The Insurance Code prohibits the following conduct:
1. any oral or written statement misrepresenting the terms of any policy issued or to be issued by an insurer or any other company, or regarding the benefits or advantages promised or any misleading estimate of the dividends or share of the surplus to be received;

2. any misleading representation or comparison of companies or policies for the purpose of inducing a policyholder to lapse, forfeit, change or surrender his insurance;

3. any verbal or written statement that contains any false or malicious statement calculated to injure any company doing business in this State in its reputation or business;

4. any verbal or written statement that:

   tends to create the impression or imply that the company, its financial condition or status, or the payment of its claims, its policy forms or kinds or plans of insurance are approved, endorsed or guaranteed by the State of Illinois, United States Government or the Director or Department of Insurance or are secured by government bonds, or are secured by a deposit with the Director of Insurance;

   uses or refers to any deposit with the Director or any certificate of deposit issued by the Director or reproduction of any such certificate of deposit.

215 ILCS 5/149.


VI. DISCOVERY ISSUES IN ACTIONS AGAINST INSURERS

A. Discoverability of Claims Files Generally

Claim files are usually discoverable as long as they are deemed relevant. Relevancy is established by reference to the issues, or more generally, a piece of evidence is relevant if it tends to prove or disprove something at trial. Krupp v. Chi. Transit Auth., 8 Ill.2d 37, 132 N.E.2d 532 (1956). Only arguments based upon either attorney-client privilege or the work product doctrine can successfully contest this discovery.

B. Discoverability of Reserves

Courts have recently allowed limited discovery for reserves, particularly when the reserves are set without advice of counsel.
C. **Discoverability of Existence of Reinsurance and Communications With Reinsurers**

Courts have consistently held that insurer’s reinsurance policies are not discoverable. However, the unusual cases in which such discovery is admissible as discoverable involve “lost policy” issues.

D. **Attorney/Client Communications**

Attorney-client privilege precluding admissibility of claims files is established in a corporate setting if the following elements are met: a showing that the communication stemmed from a confidence that it would not be disclosed, that the communication was made to an attorney acting in his or her legal capacity for the clear purpose of securing legal advice, and that the communication remained confidential. *Archer Daniels Midland Co. v. Koppers Co., Inc.*, 138 Ill.App.3d 276, 279, 485 N.E.2d 1301, 1303 (1st Dist. 1985); *Chavez v. Watts*, 161 Ill.App.3d 664 (1st Dist. 1987); See also, *Rapps v. Keldermans*, 257 Ill. App.3d 205 (1st Dist. 1993). The burden on establishing the privilege nature of a communication is on the party claiming such privilege. *Id.*

Illinois appellate courts have split on the question of whether coverage counsel’s advice to the insurer concerning the applicability of coverage is privileged. In *Western States Ins. Co. v. O’Hara*, 357 Ill.App. 3d 509, 828 N.E.2d 842 (4th Dist. 2005), the court held that the common interest doctrine prevented the application of the attorney client privilege to advice concerning the settlement of the underlying claim. However, in *Illinois Emcasco Ins. Co. v. Nationwide Mutual Ins. Co.*, 393 Ill.App. 3d 782, 913 N.E.2d 1102 (1st Dist. 2009), the court ruled that the common interest doctrine did not apply to counsel retained by the insurance company to provide coverage advice, rejecting the standard in *Western States v. O’Hara*. The court noted that its decision is limited to advice concerning coverage, and does not extend to communications from coverage counsel concerning the common interest of the insured and the insurer.

VII. **DEFENSES IN ACTIONS AGAINST INSURERS**

A. **Misrepresentations/Omissions: During Underwriting or During Claim**

Section 154 of the Illinois Insurance Code addresses the effect of misrepresentations and false warranties stated in a policy of insurance, endorsements or riders to the policy, or in a written application for a policy of insurance. 215 ILCS 5/154. Section 154 is generally used as an affirmative defense in a breach of contract action brought by the insured for the denial of coverage under a policy of insurance. An insurer may also seek to rescind the policy based on misrepresentation in the application for coverage.

An insurer has no general duty to investigate the truthfulness of answers given to questions asked on an insurance application and may rely on the truthfulness of these answers when accepting the risk. Brandt v. Time Ins. Co., 302 Ill.App.3d 159, 164, 704 N.E.2d 843, 846 (1st Dist. 1998). The insured has a duty to supply complete answers and accurate information to the insurer. Id.

In order for a misrepresentation or false warranty to defeat or void a claim, or to provide the basis for rescission of a policy of insurance, the insurer has the burden of proving that the misrepresentation was made with the actual intent to deceive; or that the misrepresentation materially affected either the acceptance of the risk or the hazard assumed by the company.


B. Failure to Comply with Conditions

1. Assistance and Cooperation

The basic purpose of a cooperation clause is to protect the insurer’s interests and to prevent collusion between the insured and the injured party. Waste Management, Inc. v. International Surplus Lines Ins. Co., 144 Ill.2d 178, 191, 579 N.E.2d 322, 327 (1991). The cooperation clause “imposes a broad duty of cooperation and is without limitation or qualification. Id. at 192, 579 N.E.2d at 328.

The cooperation clause obligates the insured to disclose all facts within its knowledge and otherwise to aid the insurer in its determination of coverage under the policy. Waste Management, 144 Ill.2d at 204, 579 N.E.2d at 333. “The insurer is entitled, irrespective of whether its duty is to defend or indemnify, to gain as much knowledge and information as may aid it in its investigation, or as may otherwise be significant to [the] insurer in determining its liability under the policy and in protecting against fraudulent claims.” Id.

2. **Late Notice**


A policy condition requiring notice “as soon as practicable” is interpreted to mean “within a reasonable time.” *Livorsi*, 222 Ill.2d at 311, 856 N.E.2d at 343. Whether notice has been given within a reasonable time depends on the facts and circumstances of each case; including, the specific language of the policy’s notice provision, the insured’s sophistication regarding insurance policies, the insured’s awareness that an occurrence as defined under the policy has taken place, the insured’s diligence in ascertaining whether policy coverage is available and whether any delay in notice prejudiced the insurer. *Northbrook Property*, 313 Ill.App.3d at 466, 729 N.E.2d at 922.

Where the reasonableness of notice is at issue “the presence or absence of prejudice to the insurer is one factor to consider when determining whether a policyholder has fulfilled any policy condition requiring reasonable notice.” *Livorsi*, 222 Ill.2d at 317, 856 N.E.2d at 346. However, “once it is determined that the insurer did not receive reasonable notice of an occurrence or a lawsuit, the policyholder may not recover under the policy, regardless of whether the lack of reasonable notice prejudiced the insurer.” *Id.* (emphasis added).

C. **Challenging Stipulated Judgments: Consent and/or No-Action Clause**

No action provisions protect the insurer from overly generous, unnecessary, or collusive settlement by the insured at the expense of the insurer. *Swedish American Hosp. Ass'n of Rockford v. Ill. State Med. Inter-Ins. Exch.*, 395 Ill. App. 3d 80, 97, 916 N.E.2d 80, 95 (2d Dist. 2009). However, Illinois courts have also noted that it is unfair to the insured party to enforce the clause against him or her when the insurer has “erroneously refused to perform the insurance contract.” *De Luxe Motor Stages of Ill., Inc. v. Hartford Accident & Indemnity Co.*, 88 Ill. App. 2d 188, 193, 232 N.E.2d 141 (1st Dist. 1967).

D. **Statute of Limitations**

If a first party policy contains a provision limiting and restricting the period within which the insured can file suit, the running of this period starts on the date proof of loss is filed, in the manner required by the policy, until the date the claim is either denied in whole or in part. 215 ILCS 5/143.1.

VIII. **TRIGGER AND ALLOCATION ISSUES FOR LONG-TAIL CLAIMS**

A. **Trigger of Coverage**
Illinois follows the “continuous trigger” theory - also known as the “triple trigger” theory - to determine which policies are triggered by ongoing exposure to a harmful substance through multiple policy periods. The continuous trigger theory holds that “damage will have ‘occurred’ continuously for a fixed period ‘and every insurer on the risk at any time during the trigger period is jointly and severally liable to the extent of their policy limits.’” Maremont Corp. v. Continental Cas. Co., 326 Ill.App.3d 272, 277, 760 N.E.2d 550, 554 (1st Dist. 2001), quoting United States Gypsum Co. v. Admiral Ins. Co., 268 Ill.App.3d 598, 644, 643 N.E.2d 1226, 1256 (1st Dist. 1994). According to the continuous trigger theory, property damage takes place at or shortly after the time the property is exposed to the injury-causing condition and continues through the property’s exposure to that condition. U.S. Gypsum, 268 Ill.App.3d at 646, 643 N.E.2d at 1257, citing Zurich Ins. Co. v. Raymark Industries, Inc., 118 Ill.2d 23, 514 N.E.2d 150 (1987). Similarly, bodily injury takes place at the initial exposure, when the disease manifests itself and at any interim time when the claimant manifests some sickness. Zurich, 118 Ill.2d 23.

B. Allocation Among Insurers

Illinois follows the “all sums” approach to allocation, in which the insurer promises to pay “all sums” relating to the policyholder’s liability. John Crane v. Admiral Ins. Co., 991 N.E.2d 474 (Ill. App. Ct. 1st Dist. 2013), citing Zurich Insurance Co. v. Raymark Industries, Inc., 118 Ill. 2d 23, 514 N.E.2d 150 (1987). The “all sums” approach allows a policyholder to simply choose the policy or policies which must respond entirely to a loss spanning multiple policy periods. Likely, the selected carrier will pay the entire loss and then seek contribution from the other insurance carriers the policy holder is insured by. Also, if two insurers owe an insured a duty to defend, the insured may choose between the two insurers, and thereby force one insurer to pay the entire loss, up to its limit, provided the insurers are on the same layer of coverage. John Burns Constr. Co. v. Indiana Ins. Co., 189 Ill.2d 570 (2000).

Illinois follows the horizontal exhaustion rule. Thus, all primary coverage, including self-insured retentions, must be exhausted before any excess coverage will be triggered. Kajima Constr. Servs. v. St. Paul Fire & Marine Ins. Co., 227 Ill.2d 102, 114 (2007). The horizontal exhaustion rule applies even where the insured has targeted one carrier over another, so that the coverage provided by a non-targeted primary insurer must be exhausted before any excess coverage will be triggered. Id.

IX. CONTRIBUTION CLAIMS

A. Claim in Equity vs. Statutory

In Doyle v. Rhodes, 101 Ill. 2d 1, 461 N.E.2d 382 (1984), the Illinois Supreme Court established the principle that an action for contribution is a suit for equity. More recently, the court held in a declaratory judgment action that “Contribution as it pertains to insurance law is an equitable principle arising among coinsurers which permits one insurer who has paid the entire loss, or greater than its share of the loss, to be reimbursed from other insurers who are also liable for the same loss.” Home Insurance Co. v. Cincinnati Insurance Co., 213 Ill. 2d 307, 316, 821 N.E.2d 269 (2004). Thus,
Illinois views contribution as an equitable principle, but has also enacted a statue regarding contribution claims, as reviewed below.

B. **Elements**

To state a claim for equitable contribution, an insurer must establish that it has paid the entire loss, or greater than its share of the loss, and that the other is also liable for the loss. Contribution applies to “multiple, concurrent insurance situations and is only available where the concurrent policies insure the same entities, the same interests and the same risks.” *Home Indemnity*, 213 Ill.2d at 316. When two insurers cover separate and distinct risks, there can be no contribution, even if both would be liable for the loss. *Id.* For example, where one insurer provides additional insured coverage to a general contractor for all liability arising out of the work of one subcontractor, and another insurer provides additional insured coverage to the same general contractor but for the work of a separate subcontractor, there is no contribution even if both would be liable to the general contractor for the loss. *Id.*

X. **Duty to Settle**

An insurer’s duty to settle arises when (1) a claim has been made against the insured; (2) there is a reasonable probability of recovery in excess of policy limits; and (3) there is a reasonable probability of a finding of liability against the insured. *Haddick ex rel. Griffith v. Valor Insurance*, 198 Ill.2d 409, 417, 763 N.E.2d 299, 304 (2001). Importantly, the duty to settle does not arise until a third party demands settlement within the policy limits. *Id.* at 417, 763 N.E.2d at 305. An insurer that refuses to settle may be liable for the full amount of the judgment against the policyholder regardless of policy limits. *Cramer*, 174 Ill.2d at 525, 675 N.E.2d at 903.

An insurer has a duty to act in good faith in responding to settlement offers. The basis for the duty to settle is the insurer’s exclusive control over settlement negotiations and defense of litigation. *Haddick*, 198 Ill.2d at 414, 763 N.E.2d at 303. Although the insurance company, in determining whether to accept or reject a settlement offer, may properly give consideration to its own interests, it must, in good faith, give at least equal consideration to the interests of the insured. A failure to do so constitutes bad faith. *Cernocky v. Indemnity Ins. Co. of North America*, 69 Ill.App.2d 196, 207-08, 216 N.E.2d 198, 204-05 (2nd Dist. 1966).