Loss Control: Strategies for Managing Risk

Authored by ALFA International Attorneys:

William Schneider
MORRISON MAHONEY LLP
Boston, Massachusetts
wschneider@morrisonmahoney.com

James Johannsen
BUTT THORNTON & BAEHR PC
Albuquerque, New Mexico
jhjohansen@btblaw.com
I. INTRODUCTION

Insurance companies and their managing agents operate in an era of complex regulatory oversight and heightened scrutiny. Oftentimes challenges arise not so much from the risks insured, but rather the risks associated with how claims are handled or critical decisions are made. Successful management and minimization of these risks requires the ability to adapt practical solutions for the specific issue at hand. This course will discuss some of the proactive devices and strategies available to insurance companies to control risk. These include loan receipt agreements, policy buy backs, high-low agreements, and interpleader. Each provides flexibility to deal with a broad variety of situations. However, understanding the pros and cons of each will assist in selecting the right method for a particular issue, and avoid pitfalls and traps for the unwary.

II. LOAN RECEIPT AGREEMENTS

A loan receipt is typically a written agreement between an insurer and an insured under which a sum of money is paid to the insured by the insurer as a loan, which in turn is repayable to the insurer only to the extent of any recovery made by the insured. Most often the recovery comes from third-parties on account of a loss by reason of which the loan is initially made.¹ A loan receipt device creates a right of reimbursement directly from the insured, dependent on the insured’s recovery from a third party. It differs from ordinary reimbursement agreements in that it creates a conditional debt.

As a negotiated agreement, the parties may draft its terms to accomplish a variety of lawful objectives. Nonetheless, the use of such agreements is not without risk and judicial scrutiny. The Supreme Court of Indiana observed that “[t]he same ingenuity that

conceived the loan receipt agreement is now being applied to devise innumerable variations."² Hence, the courts are frequently called upon to determine the legal effects of those variant forms and to provide legal parameters for their use.

Courts and legal authorities have commented that a loan-receipt agreement is a device used to achieve an equitable result.³ A loan receipt may be used as a subrogation tool. When this occurs, the insured, in exchange for some payment from the insurer, allows a subsequent action to be brought in the name of the insured even when the insurer has in effect fully indemnified the insured for the loss.⁴ For example, an insured facing a covered third-party environmental liability may agree to let the insurer who pays upfront to prosecute a cost recovery in its name, or pursue the claim directly with an obligation to reimburse the insurer from any sums recovered. While a loan receipt agreement has a proper and legitimate place in the adjustment of losses under insurance policies, its use would be inappropriate to cover up a suit based on subrogation or to obtain the same results as the enforcement of subrogation rights. In addition, courts may not recognize the transaction as a "loan" if the insurer’s right to demand repayment of loan is, in substance, its right to subrogation parading in disguise.

One obvious risk with loan receipt agreements is the contingency of recovery. In its simplest form, the agreement provides that one with potential liability will advance funds in the form of a non-interest loan so that a claim may be prosecuted against another who is also potentially liable. It carries with it the risk that, if unsuccessful, the party

⁴ Blair v. Espeland, 231 Minn. 444, 448, 43 N.W.2d 274, 277 (1950); see also Jostens, Inc. v. Mission Ins. Co., 387 N.W.2d 161, 164 (Minn. 1986) (loan-receipt agreements useful in disposing of insurance disputes when there has been payment); E. Michael Johnson, The Real Party Under Rule 17(a): The Loan Receipt and Insurers’ Subrogation Revisited, 74 Minn. L.Rev. 1107, 1130 (1990).
making the loan may be without recourse. For this reason, the selection and role of counsel may be appropriate to ensure the vigorous prosecution of the claim. The party who receives the “loan” may lack adequate incentives to maximize the effort necessary to ensure recovery.

Securing collateral or a source or recovery for the loan is important if there are questions about whether the person receiving the loan has the ability to pay it back. It is crucial that the party making the loan has the ability to actually recover in the event of a favorable judgment. Exerting resources to secure a judgment against an insolvent defendant or one without insurance coverage is an undesirable outcome. Therefore, proceed with caution to ensure the ability to recover the loaned proceeds.

Suppose an insurer defends its policyholder under a reservation of rights through trial without filing a declaratory judgment action. After the entry of a substantial judgment for the plaintiff, the parties do not agree whether coverage applies. Rather than allow the judgment to linger and accrue interest, or pursue an appeal, the insurer and insured agree the insurer will pay the judgment subject to a right of recoupment from the insured in a subsequent declaratory judgment action. Although this sounds good in theory, the ability of the policyholder to pay the judgment if it loses the coverage dispute is of paramount importance. Before entering such an agreement consider a financial audit or requiring that, as a condition of the agreement, the insured to post security in the form of a bond to ensure payment should the lending party prevail.

Another concern is the collusive effect loan receipt agreements have between the parties to tort litigation. Once a potentially liable party has entered into a loan receipt agreement and has advanced funds to a plaintiff that party will have little, if any, incentive
to participate vigorously in the truth-finding function at trial. In fact, it may be to the settling defendant’s advantage to assist the plaintiff, because to the extent the plaintiff recovers from a non-settling defendant, the settling defendant will be entitled to reimbursement for the money “loaned.” Further, under the typical agreement, the settling defendant will be contractually immune from any further potential liability. Without question, the opportunity for collusion is real. It is for this reason that not all jurisdictions sanction the use of loan receipt agreements, or require disclosure of such agreements to effectuate their terms.

One controversial type of loan receipt agreement is known as the “Mary Carter” agreement after the seminal case of Booth v. Mary Carter Paint Co. In cases with multiple defendants, there are any number of reasons why a plaintiff might be willing to accept less in settlement from one defendant as opposed to another defendant. In return for the funds advanced, the claimant agrees that he or she will not sue or will not seek to enforce a judgment against the lender (or its insured). In some cases, the plaintiff will repay the loan according to some formula based upon the claimant’s recovery against the other party. Such an agreement serves to limit the liability of one against whom a claim might be pressed. It is a type of settlement agreement in which the settling party stays in the case in order to assist its adversary against the non-settling defendant.

In Booth, the court expressly upheld the agreement notwithstanding terms to prevent its disclosure to the other parties. However, the majority of jurisdictions require disclosure of such agreements. Disclosure is required because the jury is entitled to know a witnesses’ interest in the outcome of the case when evaluating their credibility.

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5 182 So. 2d 292 (Fla. Dist. Ct. App. 1966)
However, not all jurisdictions sanction the use of these types of loan receipt agreements or consider secrecy terms fair. If the agreement gives the settling defendant a financial stake in the outcome, it necessarily distorts the adversarial process when the settlement is kept from the jury. The Supreme Court of Nevada, in its consideration of such an agreement, declared a loan receipt agreement void and stated: *We deem agreements whereby insurance carriers agree to pay any consideration to foster litigation in which they are not interested, in order to avoid their own liabilities, contrary to law and public policy.*

Similarly, the Supreme Court of Florida in *Ward v. Ochoa* expressively rejected secrecy provisions approved in *Booth v. Mary Carter Paint Co.*, stating:

> The search for the truth, in order to give justice to the litigations, is the primary duty of the courts. Secret agreements between plaintiffs and one or more of several multiple defendants can tend to mislead judges and juries, and border on collusion. To prevent such deception, we are compelled to hold that such agreements must be produced for examination before trial, when sought to be discovered under appropriate rules of procedure. If the agreement shows that the signing defendant will have his maximum liability reduced by increasing the liability of one or more co-defendants, such agreement should be admitted into evidence at trial upon the request of any other defendant who may stand to lose as a result of such agreement. If defendants not directly affected by such agreement move for severance because of possible prejudice to them, the Court shall exercise its sound discretion in granting or denying such motion.

Courts have set aside jury verdicts and granted new trials where there was an undisclosed agreement between the plaintiff and one of the co-defendants. In *Daniel v. Penrod Drilling Company,* for example, the court stated:

8 284 So.2d 385 (Fla. 1973)
9 393 F.Supp. 1056, 1060 (E.D.La. 1975)
Courts are not merely arenas where games of counsel’s skill are played. Even in football we do not tolerate point shaving. It is perhaps because the trial is adversary that each side is expected to give its best, without secret equivocation. Counsel have no duty to seek ultimate truth in a system where the lawyer’s duty is primarily to represent his client. But even if the lawyer has no duty to disclose the whole truth, he does have a duty not to deceive the trier of fact, an obligation not to hide the real facts behind a facade.

Even when a loan receipt agreement is disclosed, another problem is often exposed. Assuming that an agreement is admissible to show a contractual relationship with reference to the interest of a witness or party to the litigation, any financial considerations that might influence the witness or party may raise concerns. A non-participating co-defendant may yet have a grave decision to make. The agreement may be drafted with admissions and accusations so damning to the non-participating co-defendant that the co-defendant is placed in a dilemma – it must choose to suffer in silence damaging conduct at trial by the co-defendant participating in the agreement, or instead must choose to explain that conduct to the trier of fact by offering into evidence the agreement with its statements calculated to frame the offering party in the worst possible light.

Loan receipt agreements are not simply limited to tort claims. Such agreements have utility in situations where the application of coverage is uncertain. Under a loan receipt agreement, an insurer could make a loan to the insured for defense costs, which the insured agrees to repay from amounts recovered from another insurer. In Cargill, Inc. v. Ace American Ins. Co., the court of appeals held that the lower court had authority to impose a constructive loan receipt agreement that allowed a co-primary insurer with duty to defend the opportunity to obtain equitable apportionment of defense costs among all co-primary insurers. Multiple co-primary insurers had offered to tender a defense in
exchange for a loan receipt agreement, and, thus, principles of good faith and fair dealing imposed an affirmative obligation on the insured to cooperate by entering into a neutral loan receipt agreement that equitably apportioned liability between co-primary insurers. The insured, by declining to execute a neutral loan receipt agreement, was deemed to have acted in bad faith.\textsuperscript{10}

Accordingly, loan receipt agreements may also preserve rights to recover defense costs paid in a situation where more than one insurance company owes a defense, but not all insurers willingly participate. The general rule is that one liability insurer cannot pursue reimbursement from another insurer for defense costs incurred in defending a mutual insured. In jurisdictions which do not recognize equitable estoppel or equitable contribution with regards to the obligations of insurance companies however, an exception to the general rule exists when a loan receipt agreement is in place.\textsuperscript{11}

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<td>• Subrogation tool</td>
<td>• Enforceability</td>
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<td>• Manage exposure</td>
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III. POLICY BUYBACKS AND POLICY RELEASES

Insurance companies looking to extinguish future exposures when contemplating settlement with the policyholder may consider a policy buyback agreement or policy release. The insurer negotiates with its policyholder a settlement of a coverage dispute through a coverage buyback agreement. In this situation, after a potentially non-covered

\textsuperscript{10} 784 N.W.2d 341 (Minn. 2010)
\textsuperscript{11} Home Ins. Co. v. National Union Fire Ins. of Pittsburgh, 658 N.W.2d 522 (Minn. 2003).
loss has taken place, a settlement of the coverage dispute is negotiated whereby the insurance company offers the insured/policyholder upfront cash in exchange for an agreement to annul the policy. As a result of the agreement, the insured essentially becomes self-insured for further losses otherwise within the policy coverage.

The term "buyback" is used in a variety of contexts that may be confusing. The term as it is commonly used in settlement settings refers to a complete policy release or mutual rescission that extinguishes all of the settling policyholder’s rights to the insurance as if it no longer exists. The defining element is the completeness of the transfer of the policyholder’s rights under the insurance contract.

A key aspect of a buyback, in contrast to a cancellation or more limited release, is that the buyback not only applies to any known claims, but also to any past or future obligations or policyholder rights under the policy. Courts reviewing these settlements usually describe and evaluate buyback agreements in terms of “mutual rescission.” Mutual rescission means that both parties of a contract agree to ending it completely with no lingering obligations. In the buyback context, that translates to the insurer and insured terminating the policy completely, with the insured relinquishing all rights and ownership it has to the policy to the insurer. This approach underscores the prospective nature of the settlement, making it clear that the release is not simply of existing claims, but is extinguishing the contract between the parties altogether by a mutual agreement to end the contract.

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12 See Texas Gas Utilities Co. v. Barrett, 460 S.W. 2d 409 (Tex. 1970) ("[P]arties may rescind their contract by mutual agreement and thereby discharge themselves from their respective duties. The mutual release of the rights of the parties is regarded as a sufficient consideration for the agreement.").
If the policy buyback is achieved through a policy rescission, the rescission, if valid, will operate retroactively.\textsuperscript{13} Where the policy buyback is achieved through a mutual policy cancellation, the cancellation of the policy is prospective only. This type of buyback does not extinguish liabilities that have already accrued or rights that had already vested at the time of cancellation.\textsuperscript{14} Parties may also negotiate what is called a “litigation buyout” which involves the settlement of a claim that is the subject of the coverage litigation. Each of these arrangements requires clarity in the settlement terms to be enforceable. What type of agreement to pursue is generally determined on the scope of risk the insurer is looking to extinguish and the unique facts of each claim.

There are exceptions that place significant limits on the availability of policy buyback arrangements. The most common limitation applies where the insured is mandated by law to maintain insurance. In that case, buybacks or any settlements that extinguish the insurance are not an option. An example is compulsory motor vehicle insurance.

Many states have enacted anti-nullification statutes which operate to “freeze liability” on the part of an insurer after an injury or death occurs that triggers a liability policy. The following states have enacted such legislation: Alabama, Arizona, Connecticut, Kentucky, Massachusetts, Missouri, Ohio, Oregon and Washington. These statutes generally provide identical or similar language to the following:

\begin{quote}
No insurance contract insuring against loss or damage through legal liability for the bodily injury or death by accident of any individual, or for damage to the property of any person,
\end{quote}

\textsuperscript{13} See, e.g., \textit{Douglass v. Nationwide Mut. Ins. Co.}, 913 S.W.2d 277, 279 (Ark. 1996) (“[C]ancellation is a prospective remedy and is based upon the insurer’s contract rights or rights under statute, while rescission is an equitable, common law remedy which voids the contract ab initio.”).

shall be retroactively annulled by any agreement between the insurer and the insured after the occurrence of any injury, death or damage for which the insured may be liable, and any attempted annulment shall be void.

In *American Continental Ins. Co. v. Steen*, the Washington Supreme Court analyzed Washington’s annulment statute which contained language nearly identical to that above.\(^{15}\) The Court found that the statutory language voided any agreement between the insured and the insurer to retroactively annul an insurance policy after an occurrence or event for which the insured may become liable. The Court in *Steen* found that the anti-annulment statute did not void agreements that were made before the occurrence of an injury, death or damage for which the insured may be liable. The Court found that the legislative intent expressed in the statute was to insure that cancellation did not adversely impact any person who was injured or damaged by an occurrence before the parties agreed to cancel the policy by agreement.

The court further explained the overarching public policy foundation for prohibiting policy annulment for liability policies after claims had been made. “The purpose of the [anti-annulment statute] is not the protection of either the insured or the insurer. Its purpose is to protect the injured and damaged by preventing insureds and insurers from coming together and canceling or rescinding insurance contracts after a potentially covered injury … has occurred.”\(^{16}\) To be sure, if the insurer and insured could mutually rescind coverage where third-party claims are at issue, unscrupulous insurers would hold the threat over the head of third-party claimants in an attempt to bargain down their claims.

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\(^{15}\) 151 Wash.2d 512, 91 P.3d 864 (2004).
\(^{16}\) *Id.*
However, anti-annulment statutes do not preclude an insurance company and its policyholder from agreeing to a policy annulment governing future claims. A policy buyback for future potential claims remains a viable option provided that the language used in the agreement is specific and unambiguous regarding that intent. The buyback agreement should state that it does not apply to claims that have already occurred prior to the buyback agreement execution date. However, anti-annulment statutes will void any buyback arrangement involving third-party claims that have already occurred.

Considering a buyback agreement that attempts retroactive application is potentially problematic for the insurer. For example, if the insurance company relies upon the agreement and refuses to defend its insured in pending claims, and the court finds that the agreement is void, then the insurer will be responsible for the ultimate result in the undefended tort case and the consequences of its non-defense of its insured. Additionally, questions arise as to whether the insured can assert bad faith against the insurer if it refuses to defend on the basis of the agreement since the agreement is void, leaving the insurance policy in force.

Another thorny issue is if there are any unnamed additional insureds on the policy. Where additional insureds are involved it is unlikely that a mutual rescission of the entire policy can take place without the consent of the unnamed additional insureds.\(^\text{17}\) Additionally, one insurer’s settlement and release with its insured through a policy buyback may not affect its obligation to contribute to the costs of the insured’s defense incurred by another insurer.\(^\text{18}\) This is so because at the time of a loss, each insurer has


a potential obligation to defend and indemnify against claims that might arise. Therefore, although a policy annulment may occur which attempts to retroactively annul the policy, if a claim has already occurred (even though unknown to the parties), the obligation of defense has attached.

Buybacks have become more common because insureds have come to see them as a tool to maximize the value of a policy. In the general liability context, buybacks may occur after the actual term of the policy has expired, so that only long tail risks may remain. The carrier values the buyback based on what may happen in the future as well as on any claims currently identified. The policyholder becomes self-insured. However, the real risk lies with the prospect that the injured parties’ rights under the policy may have already vested.

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<td>• Gets insurer off the risk</td>
<td>• Typically prospective only</td>
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<td>• Mutual agreement</td>
<td>• No effect on other interests</td>
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IV. HI-LOW AGREEMENTS

A high-low agreement is a private contract that, if negotiated before trial, constrains any plaintiff’s recovery to a specified range. Typically, a defendant agrees to pay the plaintiff a minimum recovery in return for the plaintiff’s agreement to accept a maximum amount regardless of the outcome of the trial. “As a tool commonly utilized in litigation, a high/low agreement guarantees a plaintiff a minimal recovery while concomitantly circumscribing a defendant’s potential exposure. Court, counsel, and litigants favor

them.” Such agreements can be in litigants’ mutual interest because they limit the risk of outlier awards while still allowing mutually beneficial speculation through the trial process. This allows the parties to better manage expectations in litigation where the outcome is uncertain with risk to both sides.

One should not enter into high-low agreements without thinking through the terms and potential contingencies. The terms of any high-low agreement should provide that it becomes binding only when both parties communicate final approval, or is terminated when the jury returns a verdict, whichever occurs first. This may be challenging if the parties negotiate during the actual trial. Unfortunately, this is frequently the case since before trial each side will often posture to achieve the most ideal settlement.

High-low agreements are sometimes viewed as a viable settlement alternative. While such agreements tend to discourage full settlements during the discovery process and encourage the parties to proceed to trial, the high-low is attractive and useful to insure against an excess verdict on behalf of the defendant. This may be especially appealing to a defendant facing an exposure in excess of its available insurance coverage, or an insurance company seeking to avoid an excess judgment at trial when it has elected to take the case to trial. On balance, some aversion to such agreements on the part of defendants is grounded in the belief that the agreement takes away a negotiating chip from the defense and gives the plaintiff a guaranteed recovery no matter the outcome at trial. While true, there is benefit to the defendant as well.

As for the plaintiffs, hi-low agreements will guarantee some recovery to protect the plaintiffs in cases with defense verdict potential or an award of low damages. For

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example, medical malpractice cases are expensive to take to trial. Often the plaintiffs are forced to find their experts out of state, driving up the costs of the case. The trial itself is costly. Thus, a high-low agreement is attractive to the plaintiff. If the plaintiff were to lose at trial, there is some comfort in knowing that the expenses will be paid.

High-low agreements may also work in the context of binding arbitration. Transactional costs can be kept low proceeding to a binding arbitration, with a high-low agreement in place. This is most common in a situation where the only issue to be decided is liability.

As with any settlement agreement, a high-low should clearly set forth the material terms to avoid disputes later. For example, the defendant will want to make sure that the plaintiff will satisfy all liens (including but not limited to Medicare, medical, expert witness and attorney) related to this litigation. The defendant also wants the plaintiff to defend, indemnify and hold harmless the defendant and its insurer(s) from any and all liens and claims arising from this litigation and settlement. Such an agreement may also contemplate that no interest, including pre-judgment and/or post-judgment and/or any interest awarded by the jury, shall accrue or be payable on any settlement amounts or amounts awarded and no judgment shall be entered pursuant to the agreement. The parties should stipulate to using the completed verdict form to determine their obligations under the high-low agreement and for no other purpose. If confidentiality is required, it is best to address it upfront when negotiating the agreement rather than later on to avoid disputes over whether it is a material term. Finally, plaintiffs may want specific terms governing the timing and form of payment.
Like most agreements, the high-low stipulation has not escaped judicial scrutiny – especially with regards to when the agreement is made and its effect on rights such as the right to appeal. Common sense suggests that the agreement preserves the right to appeal issues other than the subject of damages. However, absent language preserving such a right that may not happen.

For example, in *Smith v. Settle*, the Virginia Supreme Court construed the viability of a hi-low agreement after the verdict entered.\(^{21}\) In that case, the plaintiff’s vehicle was struck by an ambulance driven by the defendant. Although it was not clear when the agreement was negotiated, defense counsel stated on the record that the parties and the insurer had arrived at a high-low agreement. The low was $350,000, which the plaintiff would get if there was a defense verdict.\(^{22}\)

After deliberation, the jury returned a defense verdict. However, the plaintiff refused the $350,000 tender from the insurer. Instead, the plaintiff moved to set aside the verdict and for a new trial alleging improper jury instructions. The defendant filed a motion to enforce the high-low agreement, even though the jury verdict had been in his favor. The court denied defendant’s motion to enforce, and instead granted the plaintiff’s motion for a new trial. After a jury failed to agree upon the verdicts at the second trial, a third trial was held in which a third jury returned verdicts for Smith. Overruling the plaintiffs’ motion to set aside the verdicts, the court sustained their alternative motions to enforce the high-low agreement and ordered “the defendant insurer” to pay the plaintiffs $350,000, “as agreed by the parties.”

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\(^{21}\) 254 Va. 348 (1997).
\(^{22}\) *Id.* at 350.
The plaintiff in *Smith* appealed that part of the final order enforcing the high-low agreement. He argued that he was no longer bound by the high-low agreement because the plaintiffs repudiated the agreement by refusing the primary carrier's tender of $350,000 after the first verdict. The plaintiffs argued their refusal of the tender was justified under the agreement. The court agreed with Smith.

Recognizing that there is no explicit provision in the agreement requiring the jury to be "properly instructed on the law," plaintiffs assert that it "was an implicit term of the agreement [and] there was no agreement not to seek post-verdict relief in the trial court." In his statement of the terms of the agreement, counsel for the plaintiffs specifically listed a number of terms and conditions relating to a reservation of the plaintiffs' right to seek further recoveries from the defendants' excess liability carrier. However, with regard to the effect of expected verdicts, he said only that counsel on behalf of the parties "have reached an agreement on a high/low with respect to the verdict in the consolidated Settle cases."

Finding nothing in counsel's statement implying that a "properly instructed" jury was part of the agreement or that either party could seek post-verdict relief in the trial court, we will not rewrite the agreement to impose provisions that are neither stated nor implied therein.23

The lesson learned is that it is up to the parties to comply with the high-low agreement, and to ensure the material terms are negotiated and agreed upon. Any refusal to honor the agreement will be treated the same as any other breach contract. If the agreement is written, it will be interpreted the same as any other written contract. Courts will not scrutinize jury verdicts for error or prejudice when a high-low agreement is in place.

We all know litigation is fraught with risk, including the risk of an extreme result. The high-low agreement removes the risk of an extreme result and in its place imposes

23 *Id.* at 351-52.
a range acceptable to both parties. Once a case is submitted to the jury and a verdict is rendered, the court should leave the parties with the benefit and burden of their bargain absent some compelling policy reason to the contrary.

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<td>• Sets parameters for trial</td>
<td>• Continued defense costs</td>
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<td>• Finality to dispute</td>
<td>• Eliminates appellate rights</td>
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V. INTERPLEADER

Interpleader is a well-known common law proceeding in equity which allows a party holding money or other property to which there are competing claims to deposit the property into court, and allow the rival claimants to litigate their claims before the court. This saves the “stakeholder” from the risk of potential multiple liability if it determines for itself who has the better claim, only to later have a court disagree with its decision. The essence of interpleader is to remove a party who has no real stake in the outcome of a struggle for an asset held by the party. It gives all the other claimants to have a forum in which to argue the matter without wasting the time and money of the uninterested party. The utility of this remedy has been successfully adapted in the insurance industry as a means to eliminate disputes of a common asset and insulate an insurer from scrutiny that may arise where there are competing claims to the common stake.

The interpleader procedure has existed for centuries. In modern practice, it is used predominantly by insurance companies confronted with multiple claims to the same proceeds under a variety of insurance policies. Amongst the principal difficulties which interpleader is intended to remedy are those posed for liability insurers and the unfairness which may result to some claimants if certain claims against the insured, alleged
tortfeasor, obtain judgment or negotiate settlement which might appropriate all or disproportionate parts of the insurance proceeds before other claimants are able to establish their claims.\textsuperscript{24} It may also include competing beneficiaries to life insurance benefits, each of whom claims all proceeds, and competing claims to liability or related insurance in which the total amount of claims exceeds the maximum policy limit for the loss.

Interpleader is available in all states. However, in modern times characterized by personal mobility, state proceedings often face the insurmountable obstacle of asserting personal jurisdiction over each of the rival claimants. Since the federal interpleader statute, 28 U.S.C. § 1335, allows for nationwide service, the venue may be set in any district in which any of the claimants resides. Federal interpleader is frequently the only available option for an insurer looking to invoke the doctrine.

There are two separate and somewhat different sources of authority for federal courts to entertain interpleader actions—


The statutory form provides its own, separate basis for jurisdiction, employing a specific form of “diversity” jurisdiction, including an amount in controversy requirement, but both the degree of diversity and the amount in controversy differ from the requirements for pure diversity jurisdiction under 28 U.S.C.A. § 1332. Rule interpleader provides no independent basis for federal jurisdiction, explicitly stating that “Persons having claims against the plaintiff may be joined as defendants and required to interplead

\textsuperscript{24} State Farm Fire & Casualty Co. v. Tashire, 386 U.S. 523 (1967).
when their claims are such that the plaintiff is or may be exposed to double or multiple liability." Fed. R. Civ. P. 22. Further, the federal jurisdiction explicitly granted in statutory interpleader does not prevent the jurisdiction which the federal courts otherwise possess; it does not limit or restrict the general provision for jurisdiction in case of diversity of citizenship or as to the jurisdictional amounts; so a British insurer could sue claimants residing in California where more than the jurisdictional amount was involved.

Jurisdiction to bring a statutory interpleader action rests upon the existence of the requisite jurisdictional amount, diversity of citizenship of the claimants under the policy, and the lack of interest in the proceeds on the part of the insurer. The form of diversity jurisdiction specified for statutory interpleader actions under 28 U.S.C.A. § 1335 differs somewhat from that required for general “diversity jurisdiction” under 28 U.S.C.A. § 1332. The two primary distinctions are the degree of diversity required, and the minimum amount in controversy.

Under the interpleader statute, the “complete diversity” required under 28 U.S.C.A. § 1332 is not required; it is sufficient that there be “minimal diversity” among the claimants, which requirement is met if there are two or more claimants who are citizens of different states, regardless of how many claimants there might also be who are citizens of the same state with other claimants. Under this measure, diversity of citizenship exists notwithstanding the fact that one of the claimants is a citizen of the state in which the stakeholder insurance company is incorporated.

An interpleader proceeding has two stages. The first stage determines if the stakeholder is entitled to an interpleader and if he, she or it should be discharged from liability. The second stage is like an action at law to determine which of the claimants is
entitled to the property. At the second stage, the stakeholder no longer has to spend the
time or money fighting over ownership of the property and the parties have a forum to
fight among themselves in court.

Interpleader statutes may also explicitly authorize courts to enjoin claimants from
prosecuting other litigation concerning the stake or fund, a necessity if interpleader is to
serve a useful, efficient purpose. That authority is missing from rule interpleader, raising
questions about the courts’ authority to enjoin concurrent proceedings when the action
proceeds under the rules. For the liability insurer faced with completing claims for limited
resources, enjoining suits against the policyholder across several jurisdictions will
eliminate the expense of defending suits in multiple jurisdiction.

Interpleader may also serve to insulate, but not necessarily absolve an insurer from
claims of “bad faith” where it bears no blame for the existence of the ownership
controversy and the counterclaims are directly related to the stakeholder’s failure to
resolve the underlying dispute in favor of one of the claimants.

Varied results militate using caution when deciding whether to file an interpleader
action. For example, if a court finds that claimants would not have sued if the insurer had
interpled the available funds, then the insurer’s failure to interplead has been found to be
a proximate cause of the insured’s injury.25 An automobile insurer could be liable for a
bad-faith failure to settle a claim as a result of its failure to interplead where, given facts
of the case, if the insurer had interpled, the automobile accident victim would have
accepted their share of the interpleader funds and would not have sought any additional

funds from the insured, and where other claimants also would not have litigated to judgment against the insured who was essentially judgment-proof.

Where it is clear that the insurer is not entitled to obtain interpleader, it may be subject to statutory penalties for improperly resorting to it. To illustrate, where the daughter of the insured was not a claimant within the meaning of the interpleader act and the insurer had filed a bill of interpleader naming the daughter and the named beneficiary, such delay was vexatious and unreasonable, and the widow would be entitled to recover attorneys’ fees and interest. Filing of interpleader action by an automobile insurer to apportion proceeds among competing claimants cannot absolve the insurer of liability for bad faith; for example, refusing to tender policy limits.

The plaintiff in an interpleader action is entitled to costs, usually including reasonable attorney’s fees, to be paid out of the funds brought into court. However, an insurer will not be allowed costs and fees in interpleader where the interpleader was unnecessary in that the insurer could have determined the rights of the claimants without the necessity of resorting to interpleader. Courts have also declined to award fees where the stakeholder asserts a substantial adversarial position, either by contesting the correctness of the amounts deposited or by setting forth its own claim to the fund.

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<th>PROS</th>
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<td>• Resolves disputes</td>
<td>• Does affect other duties</td>
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<td>• Enjoins suits against fund</td>
<td>• No insulation from bad faith</td>
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VI. CONCLUSION

Deciding how to best manage risk in the claim environment invites novel approaches. The agreements and remedies discussed during this session will provide a sound launch point to achieve better control in the arena of unpredictable outcomes.