Wisconsin Supreme Court Clarifies Remedy For Breach Of The Duty To Defend

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For years, Wisconsin policyholders and their counsel have maintained that insurers who breach their duty to defend waive (or are estopped from asserting) all their coverage defenses, including their limits of liability. Carriers found to be in breach, they argue, are automatically liable for all defense costs incurred as well as for any judgment or settlement, regardless of whether the policy would have provided coverage and regardless of policy limits. Indeed, there are several appellate decisions that appear to say just that. Radke v. Fireman’s Fund Ins. Co., 217 Wis. 2d 39 (Ct. App. 1998); Professional Office Bldgs., Inc. v. Royal Indemn. Co., 145 Wis. 2d 573 (Ct. App. 1988). Such a rule gives policyholders a powerful tool when negotiating coverage issues with carriers.

Yet several recent decisions from the Wisconsin Supreme Court suggest that waiver of coverage defenses does not automatically spring from a breach of the duty to defend. Indeed, the Court’s decisions in Maxwell v. Hartford Union High Sch. Dist., 2012 WI 58, and Marks v. Houston Cas. Co., 2016 WI 53, suggest that courts are to view a breach of the duty to defend as having much more traditional consequences.

In Maxwell, the Court discussed these consequences. It stated that “[w]hen an insurer breaches a duty to defend its insured, the insurer is on the hook for all damages that result from that breach of its duty.” Maxwell, ¶ 54 (italics added). The Court discussed the types of damages that might ordinarily result from the breach, which may include the amount of the judgment or settlement, costs and attorney fees, and additional costs “that the insured can show naturally resulted from the breach.” Id. This is a much more traditional measure of damages that is in line with ordinary breach of contract cases.

Moreover, the Court was clear that an insurer is not estopped from asserting coverage defenses it would otherwise have under its policies, even when it breaches a duty to defend. The Court directly addressed this issue as follows:

In Newhouse, the court determined that these damages could include damages beyond the policy limits. While these damage awards are sometimes framed as the insurer being “estopped” from denying coverage ... they are the measure of damages actually caused by an insurer’s breach of the contractual duty to defend, not an estoppel based on some otherwise inequitable conduct in the eyes of the insured.

Maxwell ¶ 55 (internal citations omitted).

The Court, thus, concluded: “[t]he scope of coverage in these cases is not expanded by waiver or estoppel. Rather, when an insurer breaches the insurance contract by breaching its duty to defend its insured, the insurer is liable for the damages resulting from the breach of contract.” Id. (italics added).

If there was any question about whether an insurer becomes liable for uncovered damages by failing to defend its insured, the Court addressed that issue too:

Bad faith and breach of the duty to defend are not situations in which an insurer becomes liable for insurance coverage not included in the insurance contract; in these cases insurers are liable for the damages they cause by breach of contract or by tortious breach of duties arising from the contract. While at times these cases have been explained in terms of “estoppel,” the cases do not refer to...
estoppel in the traditional sense and the estoppel referred to does not expand or create coverage.

Id., ¶ 58 (italics added). This aspect of the Maxwell decision was expressly re-iterated in the Marks opinion. Mark, ¶ 64, n. 29.

These decisions potentially transform Wisconsin law on the remedies available against an insurer that breaches a duty to defend. Under these decisions, policyholders may be limited to more traditional damages for breach of contract, and insureds may not have as effective a hammer to use against carriers when negotiating coverage issues when claims arise.

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