Tennessee Reservation of Rights

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What statutes or regulations, if any, govern the drafting of a reservation of rights letter?

Tennessee has not enacted any statutes or regulations governing the drafting of a reservation of rights. However, an extensive amount of case law provides guidance to insurers in preparing correspondence to an insured with respect to issues surrounding coverage, defense and/or indemnity under insurance agreements.

What events necessitate an insurer to issue a reservation of rights letter?

The first event triggering the need for a reservation of rights letter would be when the insured is sued by a third party and seeks a defense to the underlying action. See *State Auto Ins. Co. v. Bishop*, No. M1998-00900-COA-R3-CV, 2000 WL 279940, at *8 (Tenn. Ct. App. Mar. 16, 2000). If the insurer does not reserve its rights through some form of notice and proceeds to conduct a defense for its insured, it will be prohibited from denying coverage. *Id.* at *8 (citing *Allstate Ins. Co. v. Auto Owners Ins. Co.*, No. 03A01-9706-CH-00225, 1998 WL 102075, at *3 (Tenn. Ct. App. Feb. 27, 1998)).

In some situations, the insurer may want to further investigate the facts and circumstances surrounding the claim before making a final determination with respect to coverage, defense and/or indemnity. Tennessee courts have found that position to be acceptable so long as the insurer properly notifies the insured of its position. However, any change in circumstances that causes the insurer to exceed the scope of the original notice or change its position with respect to coverage, defense, or indemnity should be considered an "event" necessitating a supplemental reservation of rights letter. The insurer's failure to do so may result in the waiver of the rights or defenses under the policy. See infra "What are the consequences of not issuing a proper reservation of rights letter?".

As it pertains to excess insurers, the necessity of sending a reservation of rights is not triggered until the underlying coverage is exhausted by the payment of settlements and judgments. See *U.S. Fire Ins. Co. v. Vanderbilt Univ.*, 82 F. Supp. 2d 788, 794 (M.D. Tenn. 2000). However, if an excess insurer is put on notice of a claim it may be prudent to acknowledge the receipt of notice of the tort litigation "under a full reservation of rights position," as the excess insurer did in *Vanderbilt*. See *id.* at 793.

What are the timing requirements for issuing a reservation of rights letter?

Tennessee has no "timing" requirements as it pertains to specific dates or ranges of time that are held to be acceptable. The timing of a reservation of rights is a fact-specific determination. Ultimately, the issue will be whether the language in the insurer's reservation of rights was sufficient to place the insured on actual notice of the controversy so that the insured can take appropriate steps to preserve rights under the policy or to defend against third party claims. Although a reservation of rights should be sent as soon as practicable under the circumstances, a supplemental or amended reservation of rights should be sent to the insured: (a) before the insurer takes any action that might exceed the scope of the original reservation of rights; or, (b) if any additional information comes to light that results in a change in position with respect to coverage, defense, or indemnity.

In *Transamerica Insurance Group v. Beem*, for example, the insurer timely responded to the insured's notice of claim with a non-waiver agreement within *two (2) weeks*, placing the insured on notice of its intent to reserve its rights *during an investigation* of the accident. 652 F.2d 663, 664 (6th Cir. 1981). However, the insurer went beyond the investigation and began defending the insured without providing any additional reservation of rights notice. Accordingly, the court held that the insurer had waived or, alternatively, was estopped from asserting its right to rely on a policy defense or the non-waiver agreement because it went beyond that agreement without providing the insured any information to suggest that it was still relying upon the non-waiver agreement. *Id.* at 665–66.

Similarly, in *Allstate Insurance Co. v. Dixon*, the court held that the insurer exceeded the scope of its reservation of rights when it moved beyond defending the case and paid a settlement of

the underlying claim. No. 01-A-01-9011-CH-00421, 1991 WL 79549 (Tenn. Ct. App. May 17, 1991). The court noted that, had the insurer been acting under a "proper reservation of rights, non-waiver agreement, or a settlement upon an expressed contingency that such rights are reserved," it could have subsequently denied coverage even after paying or settling the underlying action. *Id.* at *5. However, the insurer did not reserve the right to take action beyond defending the claim to pay a settlement and still retain the right to deny coverage. *Id.* The Court of Appeals stated that it "simply cannot extend these agreements beyond their exact terms." *Id.* (citing 45 C.J.S. *Insurance* §746 (1974)).

Overall, the insurer must notify the insured that it intends to reserve its right to deny coverage prior to taking charge of and conducting the defense on behalf of the insured. *Am. Home Assurance Co. v. Ozburn-Hessey Storage Co.*, 817 S.W.2d 672, 674 (Tenn. 1991); see *Fulton Co. v. Mass. Bonding & Ins. Co.*, 197 S.W. 866, 868 (Tenn. 1917); *Hardware Mut. Cas. Co. v. Higgason*, 134 S.W.2d 169, 175 (Tenn. 1939).

Then, the insurer should pay careful attention to the scope of its reservation and the need to notify the insured regarding its intent to reserve the right to deny coverage when moving from investigation to defense and from defense to paying the claim.

As previously mentioned, Tennessee courts have articulated different standards for primary and excess insurers with respect to the timing of a reservation of rights. In *United States Fire Insurance Co. v. Vanderbilt University*, a federal district court held that the excess insurer had preserved its right to assert a failure to notice defense against the insured even though the insured was not aware of its position with respect to the defense until the declaratory judgment action. 82 F. Supp. 2d 788 (M.D. Tenn. 2000).

In *Vanderbilt*, the insured tendered the defense to its primary insurer and requested indemnification for all amounts that it was obligated to pay under the applicable insurance policies. 82 F. Supp. 2d at 790. The excess insurer was likewise put on notice of the lawsuit and responded by accepting the notice "under a full reservation of rights position." *Id.* at 793. The excess insurer's notice was general and did not identify what specific defenses it might rely upon in denying coverage. Several years into the lawsuit the parties reached a settlement agreement, which

was approved by the trial court. *Id.* at 790. A couple of months later, the excess insurer filed a declaratory judgment action seeking a determination of the rights and obligations of the parties. *Id.* at 791.

The insured argued that the excess insurer had waived its right to deny coverage by failing to assert specific defenses in its original reservation. Noting that the duties and obligations of the excess insurer were different from those of the primary insurer, the district court ruled that the excess insurer had no duty to make a specific reservation of rights, even when it was notified of the tort litigation, until the underlying coverage was exhausted by the payment of settlements and judgments. *Id.* at 794 (citing *St. Paul Fire & Marine Ins. Co. v. Children's Hosp. Nat'l Med. Center*, 670 F. Supp. 393 (D.D.C. 1987)).

What information must be included in a reservation of rights letter?

The language utilized by the insurer in its reservation of rights is one of the most outcome-determinative factors when deciding whether an insurer has waived or is estopped from asserting issues regarding coverage, defense, or indemnity. While there is no "magic language," some general rules are as follows:

(a) An insurer must provide actual notice of the reservation in order to preserve its defenses. See *Transamerica Ins. Group v. Beem*, 652 F.2d 663, 665 (6th Cir. 1981);

(b) The reservation of rights or non-waiver notice given by the insurance company "will be held sufficient only if it fairly informs the insured of the insurer's position." *Beem*, 652 F.2d at 666 (quoting 38 A.L.R.2d 1167); see also *Allstate Ins. Co. v. Dixon*, No. 01-A-01-9011CH00421, 1991 WL 79549, at *5 (Tenn. Ct. App. May 17, 1991); *Richards Mfg. Co. v. Great Am. Ins. Co.*, 773 S.W.2d 916, 919 (Tenn. Ct. App. 1988);

(c) Documents prepared by the insurance company, which is in a better position than the insured to understand these matters, will be strictly construed against the company. *Beem*, 652 F.2d at 666 (citing *Interstate Life & Accident Ins. Co. v. Gann*, 268 S.W.2d 336 (Tenn. 1954)); *Pac. Mut. Life Ins. Co. v. Walt*, 227 S.W.2d 434 (Tenn. 1955);

(d) If the time for furnishing proofs of loss has expired, the insurer may deny liability on

grounds that proofs were not furnished within the time allowed. *City of Pigeon Forge, Tennessee v. Midland Ins. Co.*, 788 F.2d 368, 371 (6th Cir. 1986) (citing *Prudential Ins. Co. of Am. v. Falls*, 87 S.W.2d 567, 568 (Tenn. 1935));

(e) The reason given for the insurer's position need not be legally correct. It is the insurer's conclusion regarding the existence or non-existence of certain coverage that must be clearly and fairly communicated to the insured, not its legal reasons therefor. *Richards Mfg. Co.*, 773 S.W.2d at 919;

(f) Although an insurer may assert specific defenses or policy provisions in support of its position regarding coverage, defense or indemnity in a reservation of rights, it will not necessarily waive the right to assert additional defenses or policy provisions in support of its position at a later date so long as the insurer conveys the possibility of that occurrence and takes no steps that would constitute waiver of that right. See *Smith v. Shelby Ins. Co.*, 936 S.W.2d 261, 263 (Tenn. Ct. App. 1996);

(g) The notice should clearly identify through what phases the insurer intends to maintain its right to deny coverage. For instance, the notice should say whether the insurer reserves its right to deny coverage throughout investigation, defense, or payment of the claim. Broad language on this issue will provide more protection for the insurer. Compare *Beem*, 652 F.2d 663 (holding that the scope of the reservation was limited only to the investigation phase) and *Dixon*, 1991 WL 79549, at *5 (holding that the scope of the reservation did not include payment of a settlement), with *Allstate Ins. Co. v. Fitzgerald*, 743 F. Supp. 543 (W.D. Tenn. 1990) (holding that the broad reservation language allowed the insurer to make a small liability payment while still investigating the claim without waiving its right to deny coverage) and *Gen. Agents Ins. Co. of Am. v. Mandrill Corp.*, No. 06-5524, 2007 WL 2050850, at *8 (6th Cir. 2007) (holding that the insurer's non-waiver agreement was sufficiently broad to give notice that it could pay a settlement of the claim without waiving its right to deny coverage); and

(h) The notice should also clearly identify the types of coverage for which it intends to reserve its right to deny. For example, in *Richards Manufacturing Co. v. Great American*

Insurance Co., the insurer's reservation of rights only provided notice of potential non-coverage for punitive or exemplary damages. 773 S.W.2d 916, 916–19 (Tenn. Ct. App. 1988). The reservation did not state any intent to reserve the right to deny coverage for compensatory damages. *Id.* at 919. Thus, the court held that there was a total failure on the part of the insurer to reserve any question regarding compensatory damages until the declaratory judgment action was filed—well after trial and the verdict. *Id.*

What specific statutory or regulatory language must be included in a reservation of rights letter?

There is no specific statutory or regulatory language that must be included in a reservation of rights letter under Tennessee law.

May an insurer reserve the right to seek reimbursement of defense or indemnity payments?

Yes, an insurer may reserve the right to seek reimbursement for defense or indemnity payments made on behalf of the insured. Tennessee federal courts predicting Tennessee law have followed the majority approach on this issue. See, e.g., *Cincinnati Ins. Co. v. Grande Pointe, LLC*, 501 F. Supp. 2d 1145, 1151 (E.D. Tenn. 2007). According to the district court, Tennessee would follow the majority position which "permits an insurer to seek reimbursement for defense costs when it is determined the insurer has no duty to defend or indemnify," even if the policy does not contain an express provision regarding reimbursement if the insurer timely reserves its right to reimbursement in a specific and adequate notice. *Id.* at 1161 (citing *United Nat'l Ins. Co. v. SST Fitness Corp.*, 309 F.3d 914, 916 (6th Cir. 2002) (predicting Ohio law)). In reaching its decision the court stated:

> Courts in other jurisdictions thus consistently have held that an insurer is entitled to reimbursement for defense costs when the insurer did not have a duty to defend any of the asserted claims where the insurer: 1) timely and explicitly reserves its right to recoup the costs; and 2) provides specific and adequate notice of the possibility of reimbursement. The general rule thus appears to be that, if these conditions are met, a reservation of rights is enforceable even absent an express agreement by the insured.

Id. at 1161–62. However, the reservation of rights issued to the insured must "fairly inform the insured of the insurer's position" or the courts may determine that the insurer has waived its right to do so. *Id.* at 1166–67 (citing *Transamerica Ins. Group v. Beem*, 652 F.2d 663, 666 (6th Cir. 1981)).

What are the consequences of not issuing a proper reservation of rights letter?

The consequences for an insurer's failure to issue a proper reservation of rights include, but are not necessarily limited to: (a) estoppel; (b) waiver; and/or, (c) a bad faith claim. Because courts traditionally discuss the theories of waiver and estoppel concurrently (i.e., if one theory is raised the other is as well), this discussion will, likewise, mirror that pattern.

Recall that in *Richards Manufacturing Co. v. Great American Insurance Co.*, the insurer was litigating the issue of indemnity for compensatory damages and punitive damages awarded against the insured in the underlying litigation. Following the general rule, the Court of Appeals held that an insurer could afford a defense while reserving its rights to litigate coverage under the policy, but it must advise the insured of its position. 773 S.W.2d 916, 918 (Tenn. Ct. App. 1988). Prior to trial, the insurer issued a reservation of rights letter advising the insured that it would not provide coverage for any award of punitive or exemplary damages. *Id.* As such, the insurer was not estopped from asserting coverage issues as it pertained to that issue, despite having provided a defense to the insured. *Id.*

However, at all times during the defense of the insured, including through trial, the insurer took the position that it was liable to the insured for any compensatory damages awarded against the insured, up to the policy limits. *Id.* at 919. According to the Court of Appeals, subsequent to the issuance of the policy, the insurer entered into a binding agreement with the insured that it would pay the compensatory damage award and defended the case only with the understanding that it intended to later litigate the matter of punitive damages, if awarded. *Id.* As such, it was estopped from litigating the matter of the compensatory damage award. *Id.*

In *Knox-Tenn Rental Co. v. Home Insurance Co.*, the United States Court of Appeals for the Sixth Circuit held that an insurer was estopped from denying coverage to one of its insured based

on the fraud exclusion in the policy because it had failed to reserve its rights *as to that insured*. 2 F.3d 678, 685 (6th Cir. 1993). The insurer issued a professional liability policy to Jenkins Insurance, Inc. *Id.* at 680. Knox-Tenn Rental ("KTR") filed suit against, inter alia, Jenkins Insurance and Jenkins' employee Mr. Lowe alleging negligence and fraud. *Id.*

The insurer furnished a defense to Jenkins Insurance and Employee Lowe by hiring an attorney to represent them. *Id.* at 680. The insurer sent a reservation of rights letter to Jenkins Insurance and defense counsel, neither of whom provided Mr. Lowe a copy. *Id.* The insurer did not send a reservation of rights letter to Lowe personally, or advise him in any other way that coverage might not be available to him under the policy. *Id.* Litigation concluded years later when the trial court entered a finding that the defendants, including Lowe, had defrauded the plaintiffs. *Id.* at 680. After the verdict, the insurer informed Lowe that it would not pay the judgment, citing the policy's fraud exclusion. *Id.*

In reaching its decision that the insurer could not deny coverage with respect to Lowe, the Sixth Circuit declined to accept that Lowe was aware of the insurer's intentions with respect to its reservation of rights because: (a) there was no evidence suggesting that Lowe was aware of the reservation of rights letter sent to Jenkins Insurance; and, (b) it could not impute the notice received by Jenkins Insurance to Lowe merely because he was employed by the company. *Id.* at 682. The court affirmed that, under Tennessee law, a client is imputed to have notice of facts transmitted to his attorney. *Id.* at 683 (citing *Batchelor v. Heiskell, Donelson, Bearman, Adams, Williams & Kirsch, P.C.*, 828 S.W.2d 388, 394 (Tenn. Ct. App. 1991)). However, it quickly dispelled the insurer's position by noting that, even if the notice provided to Lowe's attorney were attributed to him, the reservation of rights letter only notified Lowe's attorney that the insurer was reserving its rights with respect to its defense of Jenkins Insurance. *Id.*

The Sixth Circuit also discussed the issue of actual prejudice as a result of Home's failure to notify Lowe directly of its reservation of rights. *Knox-Tenn Rental Co.*, 2 F.3d at 684.

> Prejudice to the insured is conclusively presumed where an insurer takes charge of the insured's defense, the insured is cast in judgment and the insured never receives adequate notice from the insurer that it is reserving defenses on the policy until after judgment is entered.

Id.; see also *Ozburn-Hessey*, 817 S.W.2d at 675.

When the insurer provides a reservation notice, even one that cites a different reason for potential non-coverage than later relied upon, the insured may not be able to show prejudice. For example, in *Smith v. Shelby Insurance Co.*, the insurer sent a reservation of rights letter to the insured less than a month after receiving a notice of claim for the insured's property loss, indicating it was reserving its rights under one provision in the insurance agreement. *Smith v. Shelby Ins. Co.*, 936 S.W.2d 261, 262 (Tenn. Ct. App. 1996). A couple of months later, relying on the cited provision, the insurer formally denied coverage. *Id.*

The insured brought a declaratory judgment action seeking a determination with regard to coverage. *Id.* at 262. The insurer answered, but added another defense based on a separate policy provision. *Id.* It was the insured's position that, because neither the reservation of rights letter nor the coverage denial letter mentioned the newly-raised exclusionary provision, it had either waived its rights under that position or was equitably estopped from relying upon that provision. *Id.* at 263.

The Court of Appeals held that it was clear that the insurer had not expressly waived its ability to rely on the additional provision, as the reservation of rights letter contained the following statement:

> No act of any Company representative, while investigating, negotiating settlement of the claim or defending a lawsuit, shall be construed as waiving any Company rights. The Company reserves the right under the policy to deny coverage to your [sic] or anyone claiming coverage under the policy.

Id.

The *Smith* court held that the insured had not demonstrated that it took a prejudicial change in position based on the insurer's letters. *Id.* at 264. Where the insured has made no showing whatsoever of any harm or injury because of the correspondence from the insurer, the defenses of waiver and estoppel are not good. *Id.* (citing *Lewellyn v. State Farm Mut. Auto. Ins. Co.*, 438 S.W.2d 741, 742–43 (Tenn. 1969)); see also *Robinson v. Tenn. Farmers Mut. Ins. Co.*, 857 S.W.2d 559, 563 (Tenn. Ct. App. 1993) (noting that the burden of proof is on the insured to prove that a misrepresentation was made and that the insured reasonably relied upon the

misrepresentation); *Spears v. Commercial Ins. Co. of Newark, N.J.*, 866 S.W.2d 544, 549 (Tenn. Ct. App. 1993) (finding that the party alleging waiver must show how he has been prejudiced by a change of position); *Gitter v. Tenn. Farmers Mut. Ins. Co.*, 450 S.W.2d 780, 783 (Tenn. Ct. App. 1969) (stating that "the crux of the issue on equitable estoppel is whether the complainant relied on these statements and this conduct and thereby changed her position prejudicially.").

On the topic of waiver, *Kentucky National Insurance Co. v. Gardner* states that an insurer's failure to intervene in the litigation does not necessarily create waiver. *Ky. Nat'l Ins. Co. v. Gardner*, 6 S.W.3d 493, 498 (Tenn. Ct. App. 1999). Although it had not done so in this particular case, the Court of Appeals has held that an insurer may waive any contractual provision of an insurance policy by the acts, representations, or knowledge of its agents. *Id.* at 498 (citing *Bill Brown Constr. Co. v. Glens Falls Ins. Co.*, 818 S.W.2d 1, 13 (Tenn. 1991)). The insurer asserted its right to deny coverage on the basis that the insured had violated a policy provision requiring the insured to preserve the insurer's subrogation rights. *Id.* at 493. The insured argued that the insurer had waived its right under said provision by failing to intervene in the case. *Id.* The Court of Appeals disagreed with the insured. *Id.* at 501.

The court outlined Tennessee law on waiver starting with the general rule that a waiver is an intentional relinquishment of a known right. *Id.* at 498 (citing *Baird v. Fidelity-Phenix Fire Ins. Co.*, 162 S.W.2d 384, 389 (Tenn. 1942)). Tennessee courts have repeatedly held that, in order to constitute an abandonment or waiver of a legal right "there must be a clear, unequivocal, and decisive act of the party showing such a purpose, or acts amounting to an estoppel on [its] part." *Id.* at 498 (citing *Ross v. Swan*, 75 Tenn. 463 (1881)); see also *Charleston S.C., Mining & Mfg. Co. v. Am. Agric. Chem. Co.*, 150 S.W. 1143, 1146 (Tenn. 1911); *Springfield Tobacco Redryers Corp. v. City of Springfield*, 293 S.W.2d 189, 198 (Tenn. 1956); *Koontz v. Fleming*, 65 S.W.2d 821, 825 (Tenn. 1933); *Stovall of Chattanooga, Inc. v. Cunningham*, 890 S.W.2d 442, 444 (Tenn. Ct. App. 1994); *Trice v. Hewgley*, 381 S.W.2d 589, 595 (Tenn. 1964); *Webb v. Board of Trustees of Webb School*, 271 S.W.2d 6, 19 (Tenn. 1954).

The law will not presume a waiver, and the party claiming the waiver has the burden of providing it by a preponderance of the evidence. *Gardner*, 6 S.W.3d at 499 (citing *Fleming*, 65

S.W.2d at 825). Waiver may be provided by "express declaration; or by acts and declarations manifesting an intent and purpose not to claim the supposed advantage; or by course of acts and conduct, or by so neglecting and failing to act, as to induce a belief that it was [the party's] intention and purpose to waive." *Id.*; see *Baird v. Fidelity-Phenix Fire Ins. Co.*, 162 S.W.2d 384, 389 (Tenn. 1942). In order to establish waiver by conduct, the proof must show some "absolute action or inaction inconsistent with the claim or right" waived. *Id.* (citing *Fleming*, 65 S.W.2d at 825); see also *Stovall*, 890 S.W.2d at 444; *Webb*, 271 S.W.2d at 19. Specifically, the record must show conduct on the part of the insurer which is so clearly inconsistent with an intention to insist upon a strict compliance with the provision at issue that the conduct constitutes an implied waiver. *Id.* (citing *Crumley v. Travelers Indem. Co.*, 475 S.W.2d 654, 658 (Tenn. 1972)).

Although Tennessee law *allows* an insurer to intervene in a pending lawsuit to protect its subrogation rights, the Court of Appeals denied finding any law in this jurisdiction that *required* it to do so. *Gardner*, 6 S.W.3d at 499. That fact, coupled with the insurer's attempts to stay apprised of the ongoing litigation, is inconsistent with any averment that it waived its right to enforce the policy provisions with respect to its subrogation rights. *Id.*

Moving on to the issue of estoppel, the Court of Appeals held that

> [a]n estoppel… can be maintained only on the ground that, by the fault of one party, another has been induced… to change his position for the worse in such a manner that it would operate as a virtual fraud upon him to allow the party by whom he has been misled to assert the right in controversy.

Gardner, 6 S.W.3d at 500–501 (citing *Baird*, 162 S.W.2d at 388); see also *Burge Ice Mach. Co. v. Strother*, 273 S.W.2d 479, 483 (Tenn. 1954); *Gitter*, 450 S.W.2d at 787; *Shelby Mut. Ins. Co. v. Wilson*, 450 S.W.2d 780, 784 (Tenn. 1969); *Webb*, 271 S.W.2d at 19. In order to establish an estoppel, also known as "implied waiver" or "waiver by estoppel," the party asserting it must show that he prejudicially changed his position in reliance upon the other party's conduct. *Id.* (citing *Gitter*, 450 S.W.2d at 785).

Aside from potentially waiving or being estopped from asserting defenses based on failure to provide a proper reservation of rights, an insurer may also open itself up to a bad faith claim from its insured if it improperly handles a reservation of rights issue. Notably, however, current

Tennessee law does not allow a claim against an insurer for mishandling a reservation issue under the Tennessee Consumer Protection Act (TCPA). *Davidoff v. Progressive Hawaii Ins. Co.*, No. 3:12-00965, 2013 WL 124353, at *1 (M.D. Tenn. Jan. 9, 2013) (noting that a TCPA claim was available prior to the enactment of section 56-8-113 of the Tennessee Code Annotated on April 29, 2011; citing *Myint v. Allstate Ins. Co.*, 970 S.W.2d 920 (Tenn. 1998)).

Section 56-7-105 of the Tennessee Code Annotated is the "exclusive remedy" for an insurer's bad faith refusal to pay on a policy. *Id.* at *2 (citing *Heil Co v. Evanston Ins. Co.*, 690 F.3d 722, 728 (6th Cir. 2012)). The statute referred to as the "exclusive remedy" by the Sixth Circuit states, in pertinent part, that:

> The insurance companies of this state, and foreign insurance companies and other persons or corporations doing an insurance or fidelity bonding business in this state, in all cases when a loss occurs and they refuse to pay the loss within sixty (60) days after a demand has been made by the holder of the policy or fidelity bond on which the loss occurred, *shall be liable to pay the holder of the policy or fidelity bond, in addition to the loss and interest on the bond, a sum not exceeding twenty-five percent (25 percent) on the liability for the loss*; provided, that it is made to appear to the court or jury trying the case that the refusal to pay the loss was not in good faith, and that the failure to pay inflicted additional expense, loss, or injury including attorney fees upon the holder of the policy or fidelity bond; and provided, further, that the additional liability, within the limit prescribed, shall, in the discretion of the court or jury trying the case, be measured by the additional expense, loss, and injury including attorney fees thus entailed.

Tenn. Code Ann. §56-7-105(a) (West 2013) (emphasis added).

Under what circumstances does the issuance of a reservation of rights letter require independent counsel?

Unlike some other jurisdictions, Tennessee law does not require that the insurer provide the insured with independent counsel if it issues a reservation of rights. As discussed under "What information must be included in a reservation of rights letter?" above, the insurer will not be found to have waived its right to later litigate the issue of indemnity if it provides a defense under a clear and unequivocal right to do so.

To whom must the insurer send the reservation of rights letter and to whom must the insurer send a copy?

Knox-Tenn Rental Co. v. Home Ins. Co., cited under "What are the consequences of not issuing a proper reservation of rights letter?" above, addressed to whom the insurer must send a copy of the reservation of rights notice. 2 F.3d 678 (6th Cir. 1993). The United States Court of Appeals for the Sixth Circuit held that the insurer had waived, or was estopped from asserting, its right to deny indemnity coverage for a judgment rendered against an additional insured (Lowe) under the policy of insurance issued to his employer, the named insured (Jenkins Insurance). *Id.* at 685.

There, the insurer: (a) provided a defense to Jenkins Insurance, the named insured and Lowe's employer and to Lowe as an additional insured under the policy; (b) sent a reservation of rights letter to Jenkins Insurance; (c) provided a copy of the reservation of rights letter sent to Jenkins Insurance to defense counsel; (d) continued to provide a defense to both Jenkins Insurance and Lowe until a judgment was rendered; and (e) following the judgment, informed Lowe that it would not pay the judgment, citing to the policy's fraud exclusion. *Id.* at 680. The Sixth Circuit denounced each and every position the insurer asserted and held that the insurer could not deny coverage to Lowe because he was not properly notified of the intent to reserve rights. *Id.* at 685. Accordingly, to be safe, an insurer should notify primary insureds, identified additional insureds, and attorneys representing bothAre there any situations where a disclaimer is required as opposed to a reservation of rights?A reservation of rights is necessary for insurers who do not intend to waive their contractual rights to contest coverage:

Are there any situations where a disclaimer is required as opposed to a reservation of rights?

Tennessee does not have a "disclaimer statute" such as New York. A disclaimer of liability would be part of the reservation of rights letter. As stated in *AMCO Ins. Co. v. Mello*, "A reservation of rights is necessary for insurers who do not intend to waive their contractual rights to contest coverage:

'The general rule supported by the great weight of authority is that if a liability insurer, with the knowledge of a ground of forfeiture or noncoverage under the policy , assumes and conducts the defense of an action brought against the insured, without *disclaiming* liability and giving notice of its reservation of rights, it is thereafter precluded in an action upon the policy from setting up such ground of forfeiture or noncoverage.' *Maryland Cas. Co. v. Gordon*, 371 S.W. 2d 460, 464 (Tenn. Ct. App. 1963) (quoting 29A Am. Jur. Insurance §1465)." 2018 Tenn. App. LEXIS 414.

Are there any other notable cases or issues regarding reservation of rights letters that are important to the law of this state?

There are no other especially notable cases specifically regarding reservation of rights letters other than those discussed or cited above.

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