A Deeper Dive into Nautilus: Differentiating Insurer Efforts to Recover Defense Costs and Assessing Recoupment in the Wake of the ALI Restatement

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A DEEPER DIVE INTO NAUTILUS: DIFFERENTIATING INSURER EFFORTS TO RECOVER DEFENSE COSTS AND ASSESSING RECOUPMENT IN THE WAKE OF THE ALI RESTATEMENT

Jeffrey W. Stempel*

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I. INTRODUCTION: THE RECOUPMENT CONTROVERSY

Promulgation of the American Law Institute’s Restatement of the Law, Liability Insurance (RLLI)¹ was marked by more pronounced controversy than that usually attending Restatements.² Among the provisions attracting criticism from insurers was RLLI § 21, which states: “Unless otherwise stated in the insurance policy or otherwise agreed to by the insured, an insurer may not obtain recoupment of defense costs from the insured, even when it is subsequently determined that the insurer did not have a duty to defend or pay defense costs.”³

Because the typical general liability insurance policy does not provide for insurer recoupment of defense expenditures in connection with claims eventually deemed outside potential coverage,⁴ this provision effectively means that insurers using standard forms are precluded from seeking reimbursement of defense costs under the RLLI approach.⁵ Insurers of course are free to include such language in the policies that they draft but have consistently declined to do so despite being well aware of the issue.

Although the black letter of § 21 leaves some room for argument, the Comments and Reporters’ Note to the Section make clear that an insurer

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1. AMERICAN LAW INSTITUTES, RESTATEMENT OF THE LAW, LIABILITY INSURANCE (2019) [hereinafter RLLI].
2. See Jeffrey W. Stempel, Hard Battles over Soft Law: The Troubling Implications of Insurance Industry Attacks on the American Law Institute Restatement of the Law of Liability Insurance, 69 CLEV. ST. L. REV. 605 (2021) (chronicling RLLI project and insurer opposition to particular provisions regarded as unduly pro-policyholder). Notwithstanding the controversy surrounding portions of the RLLI, it should be emphasized that many portions of the fifty-section RLLI were uncontroversial and that the Institute rejected most insurer motions to alter contested versions of the document, approving the final RLLI by an overwhelming majority vote. Equally important is that support for the final version of the RLLI was enhanced or solidified by the revisions made in response to insurer concerns.
3. RLLI, supra note 1, § 21 (emphasis omitted).
4. See, e.g., Insurance Services Office (ISO), Commercial General Liability Coverage Form CG 00 01 04 13 (2012). In addition to promising to defend “suits,” the standard CGL policy promises to provide “supplementary payments,” including “all” defense costs in actions the insurer chooses to defend, a typically overlooked provision discussed infra notes 105-06 and accompanying text.
5. Pursuant to RLLI § 21, an insurer with a duty to defend may not be reimbursed for defense costs related to claims not potentially covered unless the policy has express language to that effect or an express agreement exists in that regard. This is the RLLI’s attempt to deal with what is frequently referred to as the “Buss” issue, so named after a famous California Supreme Court case. See Buss v. Superior Ct., 939 P.2d 766 (Cal. 1997). Since that decision, several significant courts (most prominently Pennsylvania and Illinois—General Agents Insurance Co. of America v. Midwest Sporting Goods Co., 828 N.E.2d 1092, 1102–03 (Ill 2005), and American & Foreign Insurance Co. v. Jerry’s Sport Center, Inc., 2 A.3d 526, 546 (Pa. 2010)—have rejected Buss and denied recoupment, at least for standard language CGL policies. See also RANDY MANILOFF ET AL., GENERAL LIABILITY INSURANCE COVERAGE: KEY ISSUES IN EVERY STATE ch. 7 (5th ed. 2020) [hereinafter Key Issues]. Chapter 7 of Key Issues provides a discussion of the history and development of the issue as well as a state-by-state scorecard. Insurers have opposed RLLI § 21 and argued in favor of the Buss approach.
cannot create a right of recoupment that is not in the policy simply by agreeing to defend pursuant to a reservation of rights that includes a purported right to seek recoupment as does case law rejecting recoupment. In reaction to the draft form of § 21, insurers cried foul and attacked the RLLI provision. These attacks were consistent with the arguments advanced by insurers for “recoupment” (the commonly used shorthand reference for an insurer obtaining repayment from the policyholder for the insurer’s cost of providing a defense of claim ultimately found not to trigger the duty to defend a claim or action) for decades, which have been met with considerable but mixed success. The majority of courts considering

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6. RLLI, cmt. a, provides:

[B]ecause [§ 21] is merely a default, if it turns out that the recoupment rule would be relatively easy to administer or that the costs justify the expense, insurers can incorporate an express right to recoupment in their policies. Second, situating the right to recoupment in the insurance policy carries significant advantages; it puts the legal basis of the insurer’s entitlement beyond dispute, and it specifies the contours of that entitlement in advance of a dispute, making it easier to evaluate for all parties concerned. Third, a default rule of no recoupment places the burden of contracting around the rule on the party best able to do so.

Against this background, an insurer’s choice not to insert a recoupment provision in the policy acquires contractual significance. At a minimum, it suggests that the hardship created by the lack of a right of recoupment is not so substantial as might appear in retrospect, when an insurer has defended a specific legal action that it was not obligated to defend. Moreover, recognizing that the insurer is making the choice not to insert a recoupment provision in the policy brings the default rule followed in this Section within the principle disfavoring the use of unjust enrichment when the parties are in a position to address the issues by contract. See Restatement Third, Restitution and Unjust Enrichment § 2, Comment c. The issue of the right to recoup the costs of defending a noncovered legal action is a known uncertainty that the insurer can address in the liability insurance contract, as is frequently the case in Directors’ and Officers’ Liability Insurance policies. In addition, a default no-recoupment rule better informs insurance regulators of the coverage that the insurer intends to provide under the policy form, facilitating informed administrative review of insurers’ intent to seek recoupment, and, once the form permitting recoupment is approved, better informs insurance purchasers of the more limited defense coverage provided by the policy.


8. See Hard Battles, supra note 2, at 658–62 (noting insurer-affiliated comments submitted to ALI during the RLLI process criticizing draft RLLI provisions, including what became § 21).

the issue have sided with insurers, ordering recoupment if the insurer’s reservation of rights (ROR) letter makes sufficiently clear that it may pursue recoupment if it is successful in obtaining a declaratory judgment finding no duty to defend.10

But the insurer win rate is one of slim margin. Courts are roughly divided on the issue,11 and it appears that prior to the RLLI the decisional trend had shifted in favor of policyholders.12 Although insurers had prevailed in

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10. As previously noted, the typical general liability policy, in which defense costs do not erode policy limits available to pay settlements and judgments, does not provide for insurer recoupment of defense expenditures. The prevailing law regarding the duty to defend holds that if an insurer defends an action without comment, the insurer has waived any defenses to coverage that would otherwise have been available and has not right to seek reimbursement. Consequently, an insurer wishing to pursue recoupment must at a minimum reserve this right in sufficiently clear language in its response to a policyholder request for a defense.

To a significant extent, what divides courts on the question of recoupment is their differing views as to whether the policyholder’s acceptance of a defense under these conditions forms a new agreement binding the policyholder to provide reimbursement if no duty to defend is found. Courts favoring recoupment effectively treat this sort of reservation of rights (ROR) letter as a binding commitment, while courts rejecting recoupment take the position that the insurer cannot amend the policy through such an ROR letter even where the policyholder arguably “consents” by accepting the defense.

On the contract law aspects of this issue, the anti-recoupment courts are clearly on more solid ground. In Anglo-American contract law, a “deal is a deal” absent select extenuating circumstances. Although waiver, estoppel, and acquiescence may result in de facto amendment to a deal, the prevailing view is that revision of the contract must satisfy the criteria for a “novation,” which requires that the revised contract be accompanied by new consideration. See Fanuchi & Limi Farms v. United Agric. Prods., 414 F.3d 1075 (9th Cir. 2005) (applying California law); Joseph M. Perillo, Contracts § 21.8 at 758–59 (7th ed. 2014). Additional consideration is absent when an insurer merely makes a unilateral reservation of rights, no matter how clear the ROR letter. The policyholder is not receiving anything that was not already promised in the policy.

11. See Key Issues, supra note 5, at 306 (fifty-state survey reveals that “both sides can claim many victories”).

12. See id.; RLLI, supra note 1, Reporter’s Note a., supra note 1 (reflecting recent decisions rejecting recoupment). Certainly, the pre-RLLI trend among state supreme courts has opposed recoupment (in the absence of language in the policy itself). See RLLI, cmt. a. (noting that § 21 “adopts the position embraced by . . . several recent state-court decisions, while recognizing that a slightly greater number of state courts have espoused contrary views”). However, “[a] majority of federal courts making Erie predictions also have adopted positions contrary to the rule stated” in § 21. Id.

Apart from the recoupment issue alone, widening gaps between federal and state court assessments of insurance controversies appears significant and growing. For example, in the recent avalanche of coverage litigation surrounding business interruption claims related to COVID-19, insurers have prevailed at nearly a ninety-five percent rate in federal courts but “only” a two-thirds rate in state courts. See University of Pennsylvania Covid Litigation Coverage Tracker, https://cclt.law.upenn.edu (visited Sept. 20, 2021). Where the federal-state gap in insurance outcomes is pronounced and consistent, it reflects rather imperfect application of Erie Railroad Co. v. Tompkins, 304 U.S. 64 (1938), which requires application of state substantive law where federal subject matter jurisdiction is premised solely on diversity. See John L. Watkins, Erie Denied: How Federal Courts Decide Insurance Coverage Cases Differently and What
cases in the late twentieth century,\(^4\) so had policyholders.\(^5\) The California Supreme Court's 1997 decision in *Buss v. Superior Court*,\(^6\) although not the inaugural decision on the issue, gave the question renewed prominence and was trumpeted by insurers as a definitive holding ushering in an era of recoupment.\(^7\) But California's influence was not as extensive as insurers hoped, with several state supreme courts (and some federal courts making *Erie* predictions) rejecting *Buss* in strong anti-recoupment opinions.\(^8\) And while California reiterated its support for *Buss*, it did so under the much more compelling circumstances involving a lawsuit where no duty to defend was ultimately found for even a single claim in the underlying action.\(^9\)

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\(^{11}\) See *Scottsdale Ins. Co. v. MV Transp.*,\(^{12}\) 115 P.3d 460 (Cal. 2005). *Scottsdale* is a more compelling case for recoupment than *Buss* in that *Scottsdale* held that the insurer had no duty to defend even a single claim in the underlying lawsuit against the policyholder. In *Buss*, the...
Thus, as the RLLI was taking shape between 2011 and 2019, recoupment enjoyed a narrow majority of judicial support but was losing ground as the RLLI authors adopted and maintained allegiance to what would become § 21’s bar to recoupment absence specific agreement in the policy (more on that in a minute). Although strongly opposed by insurers, § 21 continued to enjoy the support of the RLLI reporters and the bulk of project’s advisers, as well as the Institute as a whole on final passage. In the aftermath of § 21 (which was in draft form as early as 2016), courts began to decide recoupment disputes with specific reference to the RLLI, with varying extent of analysis and commentary.

A. Acceptance and Rejection of RLLI § 21

The first decision making reference to § 21 was Selective Insurance Co. of America v. Smiley Body Shop, Inc., but the court did not rely extensively

policyholder faced a barrage of claims, most of which did not trigger a duty to defend, but the lawsuit alleged one claim (defamation) for which there was clearly a potential for coverage pursuant to the commercial general liability (CGL) policy at issue. Consequently, in Buss, there was a foundation for defending the “suit” against the policyholder in light of the longstanding, widely accepted maxim that the duty to defend is “indivisible,” while, in Scottsdale, the CGL insurer could argue that, because there was no duty to defend even a single claim, there was never any duty to defend the “suit” as promised in the policy.

19. During the promulgation process of the RLLI, commentary and motions sought revision of § 21 and its predecessors. But these and other efforts at floor amendment of the RLLI failed, usually by lopsided voice votes. The final RLLI was approved at the 2018 ALI Annual Meeting by voice vote. See Stempel, supra note 2, at 662–63.

The RLLI production process leading up to the vote included nearly a dozen meetings of the Reporters and the Advisors, a group of forty that was evenly divided between insurer-side counsel, policyholder counsel, judges, and professors. See Stempel, supra note 2, at 628 n.80 (listing Advisors); see also id. at 629 n.81 (discussing RLLI Members Consultative Group and noting prominent members) and 627–30 for further discussion of the RLLI process and Advisors, including a list. See also Jeffrey W. Stempel, From Quiet to Confrontational to (Potentially) Quiescent: The Path of the ALI Liability Insurance Restatement, The BRIEF, Fall 2020, at 10 (reviewing ALI Restatement process and RLLI history).

While there were objectors to § 21 among the Advisors (almost exclusively among the insurer representatives), my recollection as an Advisor attending all of the working sessions was that the battle was not particularly pitched. Everyone appeared to recognize that after a big win in Buss, insurers had been losing more than winning on the issue in state supreme courts. It was outside the ALI process that insurers and counsel were more adamant in their opposition to § 21.

As to the division of Advisor opinion, it cleaved along client lines, but I again emphasize that this was not something where the ten insurer executives or counsel made much protest. Nor do I recall any judges going to the ramparts in favor of recoupment. Policyholder lawyers predictably approved of § 21 and opposed recoupment. And so do almost all law professors whose opinions on the issue are known to me. A very prominent exception is Professor Robert Jerry, who was an Advisor. See Jerry, supra note 14 (generally approving recoupment and the California Supreme Court’s Buss decision). Another RLLI Advisor and insurance scholar outside the academy, Douglas Richmond, is less categorically supportive of recoupment, concluding that “insurers have a right to restitution depending on the facts of the particular case.” See Douglas R. Richmond, Reimbursing Insurers’ Defense Costs: Restitution and Mixed Actions, 35 SAN DIEGO L. REV. 457, 459 (1998); id. at 472–80 (tracing history of recoupment prior to Buss). 20. 2017 U.S. Dist. LEXIS 81007 (S.D. Ind. May 26, 2017).
on § 21. Rather, the opinion reads as though the court had independently made its decision to prohibit recoupment and was merely citing the RLLI as a confirming authority. That decision still counts as judicial approval of § 21, of course, but does not necessarily reflect significant influence of the RLLI.

Since Smiley Body Shop, courts have diverged on the issue. Some have cited RLLI § 21 favorably in denying recoupment.24 Others have rejected § 21, at least in part.22 The culminating case in this debate (for the moment) is Nautilus Insurance Co. v. Access Medical, LLC,23 which provides the most extensive post-RLLI analysis of the issue and a narrow victory for insurers, with strong majority and dissenting opinions on both sides of the question. Although one cannot deny that Nautilus is a win for insurers, it is something short of the extensive pushback of the RLLI sought by insurers, who have invested significant resources in seeking endorsement of recoupment through the courts.

In particular, as discussed below, Nautilus involved a situation in which a federal trial court, affirmed by an appellate court, found no duty to defend any portion of the action against the policyholder. This fact was key to the 4–3 Nautilus majority’s conclusion that reimbursement was warranted, which stressed its view that the insurer never had the duty to defend any portion of the underlying claim. If faced with a situation in which the action against the policyholder involved at least one claim subject to insurer defense obligation (so-called “mixed” actions), the Nevada Supreme Court might well reach quite a different result.

As discussed below, the RLLI position has largely prevailed in mixed actions. In cases where courts find no duty to defend even a single claim in the underlying “suit,” insurers have tended to achieve recoupment success in what might be termed the “post-Buss” era. In addition, Nautilus in context is a good deal more complicated than the narrow answer to the Ninth Circuit’s certified question might initially suggest. And although the Nautilus majority opinion is reasonable, closer examination demonstrates the superiority of the RLLI approach reflected in the dissent.


II. DIFFERENTIATING RECOUPMENT SCENARIOS

Too often overlooked in the recoupment debate are distinctions between different recoupment situations before the court. Situations in which insurers seek to recoup defense expenditures fall along a continuum, one in which the case for recoupment can range from reasonably strong (but often still not persuasive for the reasons set forth in RLLI § 21 and the Nautilus dissent) to woefully weak.

A. Policy Provisions on Recoupment

The best, perhaps unquestionable, case for recoupment is when the insurance policy expressly gives the insurer a right to recoupment, provided that enforcement of this aspect of the policy is not barred by consumer protection statutes or contract doctrines such as unconscionability or public policy concerns. Although general liability policies typically lack a recoupment provision, these have been standard fair in Directors and Officers liability policies for some time, making it overwhelmingly likely that such provisions will be enforced by courts in commercial settings. Less clear is whether regulators or courts would tolerate recoupment provisions in personal umbrella policies, automobile policies, or the liability portion of a homeowners policy.

The insurance industry’s consistent reluctance to address the recoupment issue in policy language suggests that insurers regard an explicit recoupment provision as a drain on sales and anticipate a negative market reaction if such clauses should become common for consumer or general

24. See RLLI, supra note 1, § 21, cmt. a (recoupment provisions are “frequently the case” in Directors’ and Officers’ Liability Insurance policies).

25. There should be some room for non-enforcement of even clearly drafted recoupment provisions that are inconsistent with substantive policyholder rights or basic insurance principles. For example, one hopes that a court would not enforce without modification a recoupment provision that tacked on to the recoupment bill a double-digit interest rate. In addition, where recoupment is permitted, the details of proving amounts owed hold potential for unfairness. A court should not, for example, permit a recouping insurer to recover more than actual payments to counsel, including any negotiated reductions in billing, or to obtain bonus or success fees based on the results of defense. If recoupment is permitted in a mixed action, the insurers should bear a significant burden (perhaps even being held to a “clear-and-convincing” evidence standard) to separate defense costs attributable to covered and uncovered claims.

26. Although law in general and contract law in particular aspire to provide a consistent set of rules applied to all regardless of status, one can readily see the potential for unfairness if a recoupment provision (no matter how clearly drafted) lies submerged in the fine print of a policy that consumers receive weeks after purchase and almost certainly never read. Although commercial policyholders are also not leading candidates for flyspecking the text of their policies, at least these entities have a business reason for the effort as well as more realistic access to expert professional and legal services to aid the inquiry. In both commercial and consumer settings, if recoupment provisions eventually appear in policy text, they perhaps are better evaluated as part of a product, rather a classically negotiated agreement. See generally Jeffrey W. Stempel, The Insurance Policy as Thing, 44 Tort & Ins. L.J. 813 (2009).
liability policies. Whatever the rationale, insurer refusal to address the issue in policy text strongly suggests that courts should be very reluctant to introduce a de facto revision of the insurance policy on behalf of insurers who control the drafting, marketing, sales, and underwriting processes.

In short, if insurers really think recoupment was required by economic or equity considerations, they should be required to say so through policy language, rather than reserving rights and litigating with their policyholders. As the RLLI observes:

It is sometimes said that, in choosing the most desirable default rule in a contractual setting, the task of the court is to identify the rule that the majority of parties in that contractual setting would agree to, if transaction costs were minimal and the parties had the time and inclination to reach a bargain. With that framing of the question, there are several reasons why the default rule followed in [§ 21] is the more sensible of the two in this context. First, because this rule is merely a default, if it turns out that the recoupment rule would be relatively easy to administer or that the costs justify the expense, insurers can incorporate an express right to recoupment in their policies. Second, situating the right to recoupment in the insurance policy carries significant advantages; it puts the legal basis of the insurer’s entitlement beyond dispute, and it specifies the contours of that entitlement in advance of a dispute, making it easier to evaluate for all parties concerned. Third, a default rule of no recoupment places the burden of contracting around the rule on the party best able to do so.

Against this background, an insurer’s choice not to insert a recoupment provision in the policy acquires contractual significance. At a minimum, it suggests that the hardship created by the lack of a right of recoupment is not as substantial as might appear in retrospect, when an insurer has defended a specific legal action that it was not obligated to defend. Moreover, recognizing that the insurer is making the choice not to insert a recoupment provision in the policy brings the default rule followed in this Section within the principle disfavoring the use of unjust enrichment when the parties are in a position to address the issues by contract. See Restatement Third, Restitution and Unjust Enrichment § 2, Comment c. The

27. See also Jerry, supra note 14, at 26 n.45 (suggesting that insurer reluctance to include recoupment language in policies may be result of simple inertia in that revisions of widely used standard forms are expensive undertakings for which deferral may be the preferred option and concern that if an insurer includes a recoupment provision regarded as ambiguous, application of the contra proferentem principles of construing ambiguity against the contract drafter could trap insurers into defending claims not potentially covered).

Although these concerns may be valid, they are not in my view particularly weighty excuses for the insurance industry’s problematic behavior. There is little justification for litigating recoupment in the courts based on implication when the industry could simply add recoupment language to its policies, a move that—notwithstanding concerns over contra proferentem—could be done efficiently and effectively. When insurers want to be clear in policy drafting to avoid adverse rulings, they have the rhetorical skill, as reflected in policy provisions such as those rather clearly excluding coverage for asbestos, CERCLA, or nuclear incident claims.
issue of the right to recoup the costs of defending a noncovered legal action is a known uncertainty that the insurer can address in the liability insurance contract, as is frequently the case in Directors’ and Officers’ Liability Insurance policies. In addition, a default no-recoupment rule better informs insurance regulators of the coverage that the insurer intends to provide under the policy form, facilitating informed administrative review of insurers’ intent to seek recoupment, and, once the form permitting recoupment is approved, better informs insurance purchasers of the more limited defense coverage provided by the policy.28

B. A Finding of No Duty to Defend Any Claims Against the Policyholder

*Nautilus* involved what might be termed the “best” case for insurers seeking recoupment in the absence of a policy provision specifying such a right. The district court and an apparently unanimous panel of Ninth Circuit judges found that no defense was owed regarding any aspect of the claim against the policyholder.29 In this situation, insurers can, with the proverbial straight face, make a reasonable argument that paying for a defense ultimately found not to be owed is inequitable and that equity should permit recoupment of reasonable defense expenditures.

The *Nautilus* majority was clearly influenced by not only the seeming unfairness of an insurer advancing costs later deemed not owed but also by the accompanying between-a-rock-and-a-hard-place dilemma of a nondefending insurer facing extra-contractual liability if its calculation was wrong and later being held in breach of its defense obligations.30 A similar attitude is reflected in the California Supreme Court’s 2005 *Scottsdale Insurance Co. v. MV Transportation* decision.31

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28. RLLI, *supra* note 1, ¶ 21, cmt. a (emphasis added).


Although the district court noted that “*Nautilus never raised a claim for reimbursement or damages in its complaint*” and that “[a]ll it asked for was a declaration that it has no *further* duty to defend the insureds,” 2017 U.S. Dist. LEXIS 75923 at *7–10 (emphasis in original; footnote to case record omitted), the Ninth Circuit panel found this statement not to bar recoupment in the wake of the Nevada Supreme Court decision. See *Nautilus Ins. Co. v. Access Med.*, LLC, 2021 U.S. App. LEXIS 23541 (9th Cir. Aug. 9, 2021) at *3–5.

30. See *infra* 49–75 and accompanying text (discussing *Nautilus* majority and dissenting opinions).

31. 115 P.3d 460, 468 (Cal. 2005).
C. An Action Against the Policyholder Presenting a Mix of Covered and Uncovered Claims

Many if not most recoupment disputes involve a situation considerably less sympathetic for the insurer than presented in *Nautilus* or *MV Transportation*. In these situations, the policyholder faces multiple underlying claims, where one or more of those claims clearly meets the potential for coverage standard and triggers a duty to defend. Insurers in this situation concede as they must that a defense is owed, but argue that it is owed only as to covered claim(s) and not the remainder.

So-called “mixed” lawsuits combining covered and uncovered claims can present varying degrees of sympathy for insurers and policyholders. For example, *Buss* was a good vehicle for insurers seeking to establish a right to recoupment in that only one of twenty-seven claims against the one-time owner of the Los Angeles Lakers involved a potentially covered claim.32 Other cases that involve an even division of covered and uncovered claims are less sympathetic for insurers while cases in which the majority of claims are subject to defense seem unripe for recoupment because the burden is on the insurer to allocate defense expenses among covered and uncovered claims, which can be difficult to separate.

But even *Buss*, in which a potentially covered claim “tail” wags the “dog” of the litigation as a whole, presented a weak case for recoupment, at least based on a reading of the clear language of the standard form general liability policy. As the dissent in *Buss* and many cases rejecting *Buss* have noted, the typical general liability policy (and the policy at issue in *Buss*) promises that the insurer will defend “suits.”33 Nothing in the policy language limits the duty to defend to only potentially covered “claims” asserted within such “suits.” Applying the textualist mode of construction usually favored by insurers, there is no question that policy language logically precludes recoupment. In addition, as discussed below, the typical “supplementary payments” provisions of a general liability policy promise payment of defense costs without restrictive recoupment language.

Beyond this insurance policy text issue, insurers seeking recoupment in mixed situations on equitable grounds have no good answer for the rejoinder that insurers have known about the recoupment issue for at least thirty

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32. *Buss* involved twenty-seven claims against the policyholder, only one of which was potentially covered by the policy. The insurer funded defense of the case, with policyholder using independent counsel, incurring more than $1 million in defense expenditures. See 939 P.2d 766–70 (Cal. 1997). The case also involved a defendant—Jerry Buss, the late owner of the Los Angeles Lakers and Southern California real estate tycoon—with substantial means. The *Buss* majority’s decision was something quite far afield from sticking a small business with a large legal bill after the fact.

33. See 939 P.3d at 784 (Kennard, J., dissenting); R.L.I. *supra* note 1, § 21, Reporter’s Note a (listing cases rejecting recoupment in part because insurance policy at issue promised to defend “suits” against policyholder and not merely potentially covered individual claims).
years and have failed to amend the policy language providing for a duty to defend “suits.” Under these circumstances, policy text, logic, and fairness auger against permitting recoupment, as do the public policy and insurance operations arguments raised by policyholders and courts rejecting *Buss*.

D. A More Sophisticated Scorecard

When categorizing insurer and policyholder wins and losses in recoupment disputes, the nature of the dispute must be considered. Where insurers have won, it has been primarily in cases where courts found no duty to defend even a single claim against the policyholder. By contrast, in mixed cases, recoupment has largely—with the exception of *Buss* and California cases bound by *Buss*—been rejected when the case involves at least one potentially covered claim triggering defense obligations. Since the RLLI took its position against recoupment, it appears that no judicial decision has permitted insurer reimbursement for non-covered claims in mixed cases unless the jurisdiction already had *Buss*-like precedent in place.

The distinction between mixed cases and cases where there is ultimately held to be no duty to defend whatsoever appears to be as underappreciated as it is important. As reflected in the Reporters’ Note to § 21:

Many published opinions addressing recoupment of defense costs have not addressed a potentially important distinction between a circumstance in which an insurer is held not to have had a duty to defend and a circumstance in which the insurer defended an action that included both potentially covered and not even potentially covered counts (a “mixed” case). The argument for recoupment in a mixed case is weaker, because, in a mixed case, the insurer is legally obligated to defend the entire action. Thus, the insurer does not incur any costs that it had the legal right to avoid. This explains why an unjust-enrichment claim should not lie in such a circumstance, as well as why there would be no consideration to support a separate agreement, made at the time of claim, to provide the insurer a right of recoupment. By contrast, when the insurer never had the legal duty to defend in the first place, the insurer incurred costs without any legal obligation to do so. Accordingly, jurisdictions that have allowed recoupment in mixed cases, where the ground for recoupment is weaker, almost certainly also would allow recoupment in non-mixed cases. . . . Conversely, jurisdictions that have disallowed recoupment in mixed cases still might allow recoupment in a non-mixed case, because in the latter action the insurer did not have the legal obligation to defend at all. Thus, judicial decisions disallowing recoupment in mixed cases provide only partial support for the rule stated in this Section.34

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34. RLLI, *supra* note 1, § 21, Reporters’ Note a (citations omitted). Although the Comments to § 21 address the distinction between mixed actions and those with a finding of no duty to defend any claim, my strong recollection is that the distinction was not discussed at length in RLLI drafting sessions with Advisors or in debate before the full ALI, something I now view as surprising in retrospect.
Consequently, when insurers talk about Nautilus or another prominent post-RLLI case rejecting RLLI § 21, it should be appreciated that these decisions emerged from “best case” scenarios for the insurer. Absent a complete absence of potentially covered claims in a matter, recoupment in mixed cases has primarily been on a losing streak for most of the two decades since Buss, particularly in state supreme courts. With luck and logic, promulgation of RLLI § 21 will seal the matter and end recoupment in mixed cases.

E. Recoupment Barred by Insurer Action or Inaction

At the far end of the continuum are scenarios least favorable to insurers because the insurer failed to make a timely reservation of rights raising the recoupment issue or (at the dead end of the continuum), engaged in other conduct amounting to waiver of insurer rights or equitable estoppel precluding recoupment (such as making assurances to the policyholder that recoupment would not be pursued, inducing reasonable reliance by the policyholder), or committed other misconduct that necessitates forfeiture of whatever recoupment rights the insurer might have otherwise enjoyed.

Recoupment decisions reveal few instances of insurer misconduct or misrepresentation regarding recoupment, but there are undoubtedly cases in which an insurer fails to make an adequate reservation of rights. In these instances, insurers may very well forgo arguing for recoupment knowing that this failure makes it unlikely that a court will permit recoupment.

III. THE CLOUDED WATERS AND CONFLICTING ANALYSES OF NAUTILUS

Nautilus originated with a business dispute that prompted a claim of mismanagement and an allegation that one of the insureds had misappropriated funds, improperly interfered with business relationships, and was not


36. It is probably no accident that the Case No. 11 CE CG 04395, Superior Court of California for the County of Fresno majority invoked the California Supreme Court’s Scottsdale v. MV Transportation decision more than its Buss decision. In addition to closer factual similarity, using Scottsdale as the paradigmatic recoupment situation created a more sympathetic picture for the prevailing insurer. But see Nautilus Insurance Co. v. Access Medical, LLC, 482 P.3d 683, 692 (Nev. 2021) (Cadish, J., dissenting, joined by Parraguirre and Silver, JJ.) (noting that the insurer had delayed inordinately in pursuing a judicial determination of the duty to defend the issue underlying the recoupment dispute).

37. Because so much insurance coverage litigation is in federal court, there are sometimes long waits for definitive insurance decisions by state supreme courts. For example, it took significant time for other state supreme courts to address the recoupment issue and accept or reject the California Supreme Court’s analysis in Buss: 2000 (Wyoming); 2005 (Illinois); 2005 (Montana); 2010 (Pennsylvania); 2013 (Washington). See KEY ISSUES, supra note 5, ch. 7.
authorized to distribute particular medical products. The insurer did not consider these allegations sufficient to constitute defamation that might have triggered personal injury coverage, but agreed to defend pending the outcome of its declaratory judgment action, upon which it prevailed in federal trial court.

The underlying claims in question were made in an action titled *Switzer v. Flournoy Management, LLC.* Labeled a “cross-complaint,” the pleading is more in the nature of an initial complaint against a variety of former business colleagues and their counsel by Mr. Switzer, who in essence describes being squeezed out of commercial activity, defrauded, deprived of funds owed, and generally mistreated by the insureds. In response to Switzer’s action, the defendant insureds requested a defense from Nautilus, which Nautilus eventually agreed to provide under a reservation of rights to seek recoupment, all while contending that that no defense was owed. Nautilus then commenced a declaratory judgment action in federal court.

While this cross-complaint is not a model of clarity, it certainly states claims against Access Medical, the named insured of a Nautilus Commercial Lines generally liability policy, and other insureds seeking coverage pursuant to the Nautilus policy. Although the cross-complaint in the main alleged unfair competition, breach of contract, and other business misconduct that normally falls outside the scope of general liability insurance, the Switzer cross-complaint also alleged seven counts of “Conversion,”—a tort—as


39. See Nautilus Ins. Co. v. Access Med., LLC, (E.D. Cal. Oct. 10, 2014). The action was subsequently transferred to the District of Nevada, which issued the rulings prompting the Ninth Circuit to certify the recoupment question to the Nevada Supreme Court. Weighing in at sixty pages of lengthy paragraphs and boilerplate-style allegations, the Switzer cross-complaint does not state a separate count of defamation or commercial disparagement, which is odd in that such a contention does not seem far removed from the allegations that are present in the document. One is left wondering whether claimant and counsel made a conscious decision to plead allegations that would not give the defendants the benefit of insurance coverage and a defense by panel counsel.

40. See Cross-Complaint of Ted Switzer for Legal and Equitable Relief on Individual Claims on His Behalf and Derivative Claims on Behalf of Nominal Defendant Flournoy Management, LLC at 29, Switzer v. Flournoy Mgmt. (No. 11 CE CG 04385 JH) (Cal. Super. Ct, County of Fresno) (“Fifth Cause of Action Conversion—Direct claim by Mr. Switzer against Mr. Wood, Access and Roes 11–25 and 36–50) (emphasis and capitalization omitted) and ¶¶ 71–75) and Cross-Complaint at 30 (“Sixth Cause of Action Conversion—Direct claim by Mr. Switzer against Mr. Wood, Access and Roes 11–25 and 36–50) (boldface and capitalization removed) and ¶¶ 76–80; Cross-Complaint at 31 Cross-Complaint at 30 (“Seventh Cause of Action Conversion—Direct claim by Mr. Switzer against Mr. Wood, Access [Medical] and Roes 11–25 and 36–50) (emphasis and capitalization omitted) and ¶¶ 81–85); Cross-Complaint at 32 (“Eighth Cause of Action Conversion—Direct claim by Mr. Switzer against Mr. Wood, Access [Medical] and Roes 11–25 and 36–50) (emphasis and capitalization omitted) and ¶¶ 86–90; Cross-Complaint at 34 (“Ninth Cause of Action Conversion—Direct claim by Mr. Switzer against Mr. Wood, Access [Medical] and Roes 11–25 and 36–50) (emphasis and capitalization omitted) and ¶¶ 91–95); see also Cross-Complaint at 55 (27th
well as "Negligence." To the extent that the allegations of these claims are
pure financial disputes outside coverage, the tort labels do not supersede
them to create potential for coverage. But the allegations can be read as
alleging theft and confiscation that go beyond mere argument over respec-
tive contract rights, although these assertions also tend to suggest inten-
tionally inflicted injury outside the scope of the policy.

The various courts' analyses and the insureds' effort to obtain a defense
focused not so much on the cross-complaint allegations, which rather
clearly did not allege defamation per se (but arguably alleged facts amount-
ing to defamation, a potentially covered claim), as upon an email in which
one of the defendants stated that Switzer was "banned" from distributing
certain spinal implant medical products. As the trial court summarized:

Nautilus Insurance Company seeks a declaration that it does not owe a duty to
defend or indemnify its insureds, defendants Access Medical, LLC, Flournoy
Management, LLC, and one of the companies' managing members Robert
Clark Wood, II. Access, Flournoy, and Wood are defendants in a California
state-court tort and contract action brought by Wood's former business part-
tner, non-party Ted Switzer.43

... After their relationship soured, Wood's former business partner, Ted Swit-
zter, filed a "Complaint for Enforcement of Limited Liability Company Mem-
ber Information and Inspection Rights" in the Superior Court of California,
County of Fresno, against Wood and Flournoy—the company that Wood and
Switzer had formed to market and sell medical implants. In the course of
that suit, Switzer filed the cross-complaint that is at issue in this case. In the
cross-complaint, Switzer names Wood, Access [Medical], Flournoy, and vari-
ous third parties as defendants and asserts 31 claims either on behalf of Swit-
zter individually or derivatively on behalf of nominal-defendant Flournoy. In
the cross-complaint, Switzer alleges that Wood misappropriated funds from

cause of Action, ¶¶ 181-85, also alleging Conversion); Cross-Complaint at 56 (28th Cause
of Action, ¶¶ 186-90, also alleging Conversion).
41. See Switzer Cross-Complaint, supra note 40, at 47 (21st Cause of Action), ¶¶ 146-56;
Switzer Cross-Complaint at 48 (22nd Cause of Action), ¶¶ 157-61).
42. See, e.g., Cross-Complaint of Ted Switzer in Switzer v. Flournoy Management, LLC,
Case No. 11 CE CG 04395 JH at 30 (Sixth Cause of Action: Conversion—Direct claim by
Mr. Switzer against Mr. Wood, Access and ROES 11-25 and 36-50) (emphasis and capitaliza-
tion omitted) (stating that insureds "fraudulently induced" Switzer to permit sale of goods
"worth $64,900.00" and then improperly retained the funds).
This and other "conversion" claims made by Switzer effectively alleged a fraudulent
swindle that deprived Switzer of property as well as contract rights. It certainly could have
been better pled if the goal was to trigger duty to defend and coverage. And resolution of
the potential for coverage in such situations would probably go against the policyholder. But
the Cross-Complaint's conversion claims nonetheless present an arguably colorable case for
coverage in that, at least in theory, Switzer's proceeds could have been wrongfully detained
without intent to injure on the part of the insureds.
Flournoy’s bank account, that he did not receive the distributions that he should have received from Flournoy, and that Wood and Access improperly interfered with his current and prospective business relationships.44

Defendants contend that Switzer’s four interference-with-prospective-economic-advantage claims, combined with an allegedly defamatory e-mail sent by a representative of Access, trigger Nautilus’s duty. In relevant part, Switzer alleges that defendants engaged in “wrongful acts” that caused “various vendors to stop using Mr. Switzer’s businesses and [to] use Access instead,” which resulted in “the complete loss of business . . . and injury to the personal and business reputation of Mr. Switzer and Flournoy.” Switzer further alleges that Wood acted maliciously and “with the intent to injure [Switzer’s] profession, business and emotional well-being and with a conscious disregard of [Switzer’s] rights.” The complaint does not contain claims for slander, libel, or defamation or allege that defendants made any false statements about Switzer or his businesses.45

. . . On July 25, 2011, Jacquie Weide, a representative of Access [Medical] and Flournoy, sent an e-mail to Cottage Hospital in California (one of the companies whose relationship with Switzer the defendants are alleged to have disrupted) to sell Aphatec spinal implants. Weide’s e-mail indicates that she believes that two of the hospital’s doctors were using Aphatec’s implants but that their former distributor is now banned from selling them, and she offers to provide a quote on the products. The e-mail does not name the banned distributor, and Switzer does not reference the e-mail in his cross-complaint.46

. . . Under California law, a disparagement claim “requires a plaintiff to show a false or misleading statement that (1) specifically refers to the plaintiff’s product or business and (2) clearly derogates that product or business. Each requirement must be satisfied by express mention or by clear implication” [citing Hartford Cas. Ins. Co. v. Swift Distribution, 326 P.3d 253, 256 (Cal. 2014)]. Libel and slander are both forms of defamation, and each requires proof of a false and unprivileged communication that injures the plaintiff’s reputation [citing Shiveley v. Bozanich, 80 P.3d 676, 682–83 (Cal. 2003)].47

Switzer’s cross-complaint—even when read in conjunction with the June 25, 2011—e-mail does not give rise to a potential claim for slander, libel, or disparagement (or include allegations of these offenses), and therefore does not

44. Id. at *2.
45. Id. at *8–9. While strictly true, the trial court’s statement is perhaps overly categorical in dismissing the prospect of allegations of defamation. As noted above, the cross-complaint is a lengthy document that at times appears to be throwing in the metaphorical kitchen sink yet does not clearly set out a defamation claim, which may be intended as a means of putting more litigation pressure on defendants should they be denied a defense by the insurer. But one cannot discount the possibility of simple oversight by Switzer counsel. A more charitable reading of the cross-complaint than given by the trial court could reasonably find that Switzer’s allegations amount to commercial disparagement and defamation.
46. Id. at *9–10.
47. Id. at *13 (footnotes omitted with key citations indicated in brackets in text).
trigger Nautilus’s duty to defend under the “personal and advertising injury” provision of the policy. Each of these torts requires a false statement, among other elements. Even assuming that the June 25, 2011, e-mail mentions Switzer by clear implication (he is not expressly named) defendants do not argue—let alone offer any facts to show—that the email contains a false statement, i.e. that Switzer was not, at that time, banned from distributing Aphatec spinal implants as the e-mail states. Additionally, nowhere in Switzer’s cross-complaint does he allege that defendants made any false statement about him in an effort to tortiously interfere with his business relationships, and the cross-complaint does not mention or incorporate the June 25, 2011, e-mail. Accordingly, Nautilus is entitled to a declaration that it owes no duty to defend defendants against Switzer’s cross-complaint.48


The trial court’s opinion appears to fuse portions of “Twombly” pleading requirements set forth in the prominent U.S. Supreme Court cases of Bell Atlantic Corp. v. Twombly, 550 U.S. 544 (2007) and Aschcroft v. Iqbal, 556 U.S. 662 (2009), which increased the pleading burdens on claimants, in that it seems to require that, as a precondition to obtaining a defense, the insured be pleading sufficient facts to reach the “plausibility” threshold required by those cases. But this implicit assessment, although affirmed by the Ninth Circuit without dissent, seems wrong. The duty to defend in Nevada, as in most states, is determined by the face of the complaint, with extrinsic evidence available for consideration if it tends to establish coverage but not if it tends to negate coverage. See Century Surety Co. v. Andrew, 432 P.3d 180 (Nev. 2018).

The Nautilus policy, like most standard form CGL policies, states that there is coverage for “[o]ral or written publication, in any manner, of material that slanders or libels a person or organization or disparages a person’s or organization’s goods, products or services.” There is no requirement that the disparaging comment satisfy a given state’s elements for recovery on a defamation claim or that the alleged disparagement survived a Rule 12(b)(6) motion to dismiss.

The Switzer cross-complaint rather clearly alleges something pretty disparaging—being improperly negatively labeled (a/k/a defamed) by the insureds even if the cross-complaint does not provide much if anything by way of proof. The Nautilus policy does not require that the allegations be proven at the pleading stage and does not require that the claim against the policyholder have merit. Further, a word like “banned” has an extraordinarily negative connotation and implies wrongdoing that prompted the “ban.”

Even if it was correct that Switzer was no longer an authorized dealer, labeling him as “banned” is quite different than merely noting his loss of agent status. Under these circumstances, one can make a good case that both the trial court and the Ninth Circuit took an excessively restrictive view of the cross-complaint’s allegations, even though the trial court was willing to consider the email that was not part of the pleading.

In effect, the federal courts converted the “face of the complaint” standard for determining the duty to defend to one in which the pleading must not only allege a potentially covered claim but that the claim have sufficient support to survive both Rule 12 and Rule 56 motions. Worse yet, the policyholder seeking a defense is implicitly tasked with making this showing—effectively forcing the policyholder to argue that the claim against it has merit. An insurer’s imposition of such a requirement upon its policyholder constitutes a breach of the covenant of good faith and fair dealing and should not be indirectly imposed by federal courts.
The Ninth Circuit affirmed the finding of no duty to defend\textsuperscript{49} and certified to the Nevada Supreme Court the following question:

Is an insurer entitled to reimbursement of costs already expended in defense of its insured where a determination has been made that the insurer owed no duty to defend and the insurer expressly reserved its right to seek reimbursement in writing after defense has been tendered but where the insurance policy contains no reservation of rights?\textsuperscript{50}

As previously noted, the Nevada Supreme Court in a 4–3 decision answered the question “yes.” The majority\textsuperscript{51} concluded that if the matter lacked any potentially covered claims and there was no duty to defend, the insurer had conferred a benefit to the policyholder to which it was not entitled and that had been accepted by the policyholder, thus supporting a restitution analysis for reimbursement.\textsuperscript{52}

[When a court holds that there was never a duty to defend, it is holding that the claims were never even potentially covered by the policy. Therefore, when the insurer reserved its right to seek reimbursement, it was not extracting an amendment to a contract that would otherwise govern its defense. No contract governed its defense. In these circumstances, there is no reason it cannot reserve a right it has, not pursuant to the contract, but pursuant to the law of restitution.\textsuperscript{53}]

The \textit{Nautilus} majority also applied a public policy analysis reasoning that a contrary rule would put insurers in an untenable position in that they face significant pressure to defend under doubtful circumstances in order to avoid excess liability of the policyholder and allegations of bad faith and unfair claims handling. The majority further found that taking this approach did not improperly undermine or deviate from the terms of the insurance policy contract, which was subject to overarching principles of contract law.\textsuperscript{54}

The \textit{Nautilus} majority expressly agreed with and followed California law, not only \textit{Buss v. Superior Court} but in particular \textit{Scottsdale v. MV Transportation Co.},\textsuperscript{55} noting the RLLI but only for its acknowledgment that § 21 rep-


\textsuperscript{51} Nautilus Ins. Co., 482 P.3d at 685 (Stiglich, J., joined by Hardesty, C.J., Pickering and Herndon, JJ.).

\textsuperscript{52} See id. at 688–90 (citing Restatement (Third) of Restitution & Unjust Enrichment § 35 (2011) [hereinafter R3RUE]).

\textsuperscript{53} See id. at 690.

\textsuperscript{54} See id. at 690–91.

\textsuperscript{55} See id. at 691 (citing, in particular, Scottsdale v. MV Transport, 115 P.3d 460 (Cal. 2005)).
resented a minority view in caselaw. By contrast, the Restatement (Third) of Restitution & Unjust Enrichment (R3RUE) was favorably cited and relied upon. The dissent, however, embraced RLLI § 21 and its rationale while viewing R3RUE § 35 as inapplicable because of the existence of an “express, written contract”—the insurance policy—which made no provision for recoupment. Consequently, under Nevada law, it argued that the restitution theory of the majority was therefore foreclosed. The dissent also faulted the insurer for failing to make timely pursuit of a declaratory judgment, waiting more than nine months after the duty to defend dispute surfaced before commencing the action.

The dissent took particular issue with the majority’s willingness to permit the insurer to attempt to condition defense on agreement to a recoupment action, taking the view that a unilateral reservation of rights cannot create contract rights for the insurer. Regarding RLLI § 21, the dissent noted, as had the § 21 Comments and Reporters’ Note, that although a majority of decisions permitted recoupment, the modern trend has been to the contrary. Without doubt, Nautilus was a significant if narrow (4–3) victory for insurers. One widely read insurance newsletter described it as the “Biggest ALI Restatement Case to Date” and the “first decision to use the RLLI in the process of making new law” in the jurisdiction at issue. But some restraint in celebration by insurers is required. Nautilus, unlike Buss, involved a situation where courts held that the claims the insurer defended all had no potential for coverage. As noted above, it appears there is no judicial decision rejecting RLLI § 21 that has involved a mixture of potentially covered and uncovered claims as in Buss. Further, Nautilus was a

56. See id. at 689.
57. See id.
58. See id. at 692 (citing cases).
59. Id. at 692 n.1 (citing R3RUE, supra note 52, § 35 comment a (restitution apt only where it is impossible to obtain a legal determination prior to date claimed performance due).
60. See id. at 692 (Cadish, J., dissenting, joined by Parraguirre & Silver, JJ).
61. Id. at 694–95 (quoting Am. & Foreign Ins. Co. v. Jerry’s Sport Ctr., Inc., 2 A.3d 526, 539 (Pa. 2010) and citing other cases rejecting recoupment).
62. But, as also noted by Coverage Opinions, the Nautilus court was not using the RLLI to alter existing law but rather to provide supplementary guidance. The R3RUE arguably played a larger role in the decision than did the RLLI.
63. See supra notes 25–36. In a similar vein is Catlin Specialty Insurance Co. v. CBL & Associates Properties, Inc., 2018 Del. Super. LEXIS 342, 2018 WL 3805868 (Aug. 9, 2018), in which the insurer also defended a matter in which no claims qualified for duty to defend and then sought recoupment.
64. The situation in Buss v. Superior Court, 939 P.2d 766 (Cal. 1997), was extreme in that only one of twenty-seven counts of a complaint involved a potentially covered claim, which undoubtedly influenced the court in finding recoupment apt. But there was that one potentially covered claim and, as opponents of Buss and recoupment have noted, the standard
close decision. Both the majority and dissenting opinions in *Nautilus* provide helpful analysis that can be deployed in arguing the issue, but, on balance, the dissent, like RLLI § 21, is more persuasive.

Unfortunately, courts facing recoupment claims may be inclined to look only at the final score in *Nautilus* rather than its rationale, an approach that undoubtedly gives succor to insurer opponents of § 21 and prompts a closer examination of *Nautilus*. Although the majority opinion makes a spirited defense of recoupment, its analysis ultimately errs.

The majority gave “no weight” to policyholder “arguments concerning the scope of the insurer’s duty to defend in first instance” because the federal court had already found no potential for coverage stemming from the “Switzer has been banned” email, placing the case in the category of situations most favorable for insurers. This starting point removed from the state supreme court decision whatever nagging feeling might persist that the federal courts may have been unduly ungenerous in assessing the potential for coverage of claims against the insureds. The general liability policy states that the insurer will defend “suits” involving potentially covered claims, an argument that has proven persuasive to courts rejecting recoupment in such situations, as detailed in Key Issues, supra note 5.

65. See *Nautilus Ins. Co.*, 482 P.3d at 688.

66. As previously noted, the cross-claim directed at the Access Medical insureds was chock full of allegations of wrongdoing. While most nest comfortably in the category of business or contract disputes that do not allege bodily injury, property damage, or personal injury that might trigger general liability coverage (such as trespass or defamation), there remain the conversion and negligence claims of the cross-complaint as well as the “Switzer has been banned” email that the district court considered, even though it was outside the four corners of the cross-complaint. But Switzer was not expressly named in the email, leading the trial court with appellate approval to find it insufficient under California law as set forth in *Hartford Casualty Insurance Co. v. Swift Distribution*, 326 P.3d 253, 261 (Cal. 2014), which stated:

[i]n evaluating whether a claim of disparagement has been alleged, courts have required that the defendant’s false or misleading statement have a degree of specificity that distinguishes direct criticism of a competitor’s product or business from other statements extolling the virtues or superiority of the defendant’s product or business. As explained below, disparagement involves two distinct but related specificity requirements. A false or misleading statement (1) must specifically refer to the plaintiff’s product or business, and (2) must clearly derogate that product or business. Each requirement must be satisfied by express mention or by clear implication.

As explained supra notes 45–50, a closer look suggests that the judges deciding the issue may have been excessively restrictive in applying *Hartford v. Swift Distribution*. Under the context set forth in the cross-complaint and noted by the trial court, it seems rather clear that the sender of the email is referring to Switzer, or at least that this is a reasonable inference unless dispelled. Further, as he was labeled as a “banned” distributor, there is an element of both personal defamation as well as commercial disparagement. Under these circumstances, in spite of the apparent unanimity of the federal bench on the matter, one could readily image a finding of a potential for coverage for at least a portion of the underlying claims.
But favorable is not ironclad in that the majority makes more of the insurer’s victory than it should for purposes of recoupment. The majority states:

Because this case is a certified question, not an appeal, we are not concerned with whether we would have reached the same conclusion. We accept the judgment of the federal courts that there was never even “arguable or possible coverage.” We are concerned here only with the consequences of that judgment. . . . [T]his court is not tasked with construing the policy. The federal courts have already done that. . . .”67

The never even “arguable or possible coverage” language is taken from United National v. Frontier Insurance Co.68 This segment of the Nautilus majority overlooks that, although this is the standard (and insurers may note, a generous one for policyholders often obligating insurers to defend), an ultimate finding of no defense duty does not erase the potential for coverage that preceded the decision so long as the claimed potential for coverage was not clearly unreasonable. Absent a Rule 11 violation or its equivalent, the policyholder’s colorable claim of potential coverage remains viable until rejected by the court.69 Until a court resolves the uncertainty regarding potential for coverage (provided the policyholder’s arguments are not meritless), the potential for coverage remains until extinguished. For that reason, courts have found that the duty to defend remains in effect until a judicial determination to the contrary.70 It is misleading for the majority to characterize the situation as one in which “Nautilus never owed a duty to defend.”71 To the extent a potential for coverage existed at the outset, Nautilus had that duty until it prevailed in its declaratory judgment action.

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67. See Nautilus Ins. Co., 482 P.3d at 688 (citation omitted).
68. 99 P.3d at 1158 (Nev. 2004).
69. Although no court appears to have expressly adopted a Rule 11-like standard on potential for coverage, such a yardstick would have much to recommend it. Absent an extraordinarily clear case of no prospect for construction of a claim that brings the matter within coverage, one cannot say with certainty that a court will reject the policyholder’s argument. Under these circumstances, the proper approach may be to consider non-frivolous arguments for coverage as creating a potential for coverage unless and until rejected.

Insurers can, with some force, complain that this standard effectively imposes a short-term duty to defend in cases that they are likely to win once a declaratory judgment is eventually entered, but this burden is not much greater than what insurers already face when deciding whether to forgo defense of a matter and risk losing coverage defenses, the protection of policy limits, or bad faith liability. Burdensome though it may be, courts have consistently found that this is part of the “bitter” that insurers must endure with the “sweet” of being paid premiums that can be invested for years or even decades before payment may or may not be required pursuant to the aleatory nature of an insurance policy.

70. See, e.g., Buss v. Superior Court, 939 P.2d 766, 775 (Cal. 1997).
71. Nautilus Ins. Co., 482 P.3d at 688 (footnote omitted).
The majority expanded this oversight into real error by concluding that, because the insurer ultimately prevailed on the duty to defend issue, “the contract between the parties does not apply to the instant dispute and the existence of that contract does not foreclose an unjust enrichment claim.” As the dissent correctly noted:

An express written contract exists between Nautilus and its insureds . . . Nautilus and Access Medical had a lengthy, detailed contract drafted by Nautilus that covered the entire insurer-insured relationship and set out the parties’ rights and obligations. The contract did not contain any provision allowing for the recoupment of costs expended if a court later determined that Nautilus never had a duty to defend Access Medical. Furthermore, the contract contained an integration clause, making it clear that the contract constituted the parties’ entire agreement governing their insurer-insured relationship. . . . [T]he majority’s holding that there was no contract governing the subject matter of the underlying dispute between Nautilus and Access Medical is belied by the record. Plainly, [defense of the Switzer claim subject to reservation of rights] was not an extra-contractual undertaking by Nautilus, but rather a defense undertaken based on the very existence of the parties’ contract.

The fact that a contract does not provide for a particular remedy—here, reimbursement of defense costs—does not mean that the contract is inapplicable and thus extra-contractual remedies are available; to the contrary, it represents a considered choice, presumably by Nautilus as the contract drafter, not to provide for this remedy. . . . The fact that the duty to defend was found not to exist in this circumstance does not equate to dissolution of the entire contractual relationship or allow us to disregard it. 72

72. Id.; see also id. at 690 (“[W]hen a court holds that there never was a duty to defend, it is holding that the claims were never even potentially covered by the policy. Therefore, when the insurer reserved its right to seek reimbursement, it was not extracting an amendment to a contract that would otherwise govern its defense. No contract governed its defense.”) (emphasis in original).

The failure of logic in this portion of the majority’s analysis is stunning. I defer to the dissent’s diplomatic refutation of this bizarre assertion. Of course, there was a contract—the insurance policy. The insurer that elects to defend pursuant to a reservation of rights is of course defending pursuant to a contractual obligation. The insurance policy is the sole source from which an insurer’s obligation to provide a defense may originate. Insurers do not voluntarily pay lawyers for defendants who are not insured under a policy issued by an insurer. The Nautilus majority’s labored defense of this perspective is similarly unconvincing. See Nautilus Ins. Co., 482 P.3d at 690-91.

73. Id. at 693 (citations omitted; emphasis in original); see also id. at 693 n.3 (“The insurance contract governs the parties’ entire relationship, including the duty to defend, and the fact that this recoupment remedy is not provided means it is not available, not that there is no applicable contract. The conclusion by the federal court that there is no duty to defend, which we must accept, does not lead to the conclusion that there is no contract.”). The dissent also noted delaying conduct by Nautilus that made its claim for recoupment as a matter of equity and fairness seem more than a little strained. Potentially more important, the dissent also observed that this delay made the “urgency” rationale of R3RUE § 35 inapplicable, suggesting that the insurer had sufficient time to obtain a ruling on the duty to defend rather than waiting until years later to seek recoupment. See id. at 693 n.1.
The majority's position that the contract-does-not-apply-because-the-insurer-prevailed-on-the-duty-to-defend-issue undermines both contract law and logic. To illustrate, consider a long-term lease that requires the lessee to "maintain the property in its original condition." During the course of the lease, the water level of a creek bounding the property rises, submerging a sand beach swimming hole on the leased property side of the creek. As the lease nears its end, the eager lessor sues the lessee demanding that the lessee reduce the water level and restore the small swimming area—and probably loses the lawsuit. Maintaining the property probably does not require Army Corps of Engineers style efforts to reverse climate change and other natural phenomena. Baseline stewardship of the property probably suffices. Regardless of the outcome of the dispute, would any reasonable lawyer (or layperson) seriously argue that a decision against the lessor meant the contract was inapplicable? On the contrary, it appears the decision is based on the court applying the contract.

Unlike the majority, the Nautilus dissent noted and appreciated that insurance policies are typically contracts of adhesion, that insurers owe certain fiduciary-like obligations to policyholders, and that a triggered duty to defend "continues through the litigation or until the 'potential for indemnification ceases.'" The insurers eventual victory on the duty to defend issue does not erase the contract-based duty that was seemingly activated at the outset of the Switzer claim.

The at-issue insurance contract does not contain any provision that entitles Nautilus to reimbursement if it incorrectly chooses to defend a suit for which it did not owe a duty to defend. Nautilus drafted this complicated insurance contract, and it certainly could have included a provision that provides for recoupment of costs spent if a court later determines that it never had a duty to defend its insureds. Because Nautilus drafted the insurance contract and because insurance contracts are contracts of adhesion, we must construe the insurance contract's silence on recoupment against Nautilus. Furthermore, the plain language of the contract provides that both Nautilus and the insured must approve any amendments to the contract. Therefore, Nautilus may not use a reservation of rights letter to unilaterally create new rights for itself at the expense of the insured.

74. Id. at 694 (citation omitted); see also id. at 694 n.4 ("[T]he majority's reliance on generally applicable basic contract principles without addressing the special relationship between an insurer and its insureds is contrary to Nevada precedent.") (citation omitted); id. (noting insurers' "vastly superior bargaining power" and "special element of reliance" policyholders place upon insurer); Ins. Co of the West v. Gibson Tile Co., 134 P.3d 698, 702 (Nev. 2006).

75. Nautilus Ins. Co., 482 P.3d at 694 (citations omitted; emphasis in original); see also id. at 694 n.6 (citing the Black's Law Dictionary (11th ed. 2019) definition of ROR letter as notice of insurer intent "not to waive contractual rights to context coverage" or apply an exclusion).
Having taken the wrong fork in the “is the matter subject to contract” road, the majority is now trapped on a byway that leads to its intellectual dead end of permitting recoupment under circumstances where the underlying duty to defend ruling is subject to question and the insurer arguably did not preserve a right to seek recoupment (notwithstanding the Ninth Circuit panel’s spirited support of allowing the insurer to raise the issue years after commencement of the action and initial dispute over defense duties). More important, the majority’s bizarre finding of no applicable contract permits it to apply R3RUE even though the ALI in 2019 resoundingly rejected its application in cases of this type through its overwhelming adoption of RLLI § 21.

Once in the silo of R3RUE, the majority analysis appears reasonable, at least on a superficial level. “When the insurer furnishes a defense, it is clear that the insurer has conferred a benefit to the policyholder, and that the policyholder appreciates it. The issue is whether equity requires the policyholder to pay.” The majority then goes on to find equity favoring the insurer on the ground that, without the prospect of recoupment (even though the insurer did not care enough to write this into the policy), the insurer is unduly disadvantaged (i.e., facing an inequitable situation) because of the risks that it faces if it refuses to defend and loses the accompanying declaratory judgment action.

[I]t can be inefficient and inequitable to require [contracting parties in dispute] to require those parties to obtain a declaratory judgment before proceeding . . . . That is especially true in the insurance context. An insurer that refuses to defend a claim and then loses the coverage dispute may be subject to significant liability, which can vastly exceed the policy limits. This creates a significant disincentive for the insurer to deny a defense outright when there is any possibility—even a relatively remote one—that the claim may turn out to be covered. . . . These situations arise frequently enough that scholars have devised solutions [set forth in the R3RUE].

76. As a civil procedure teacher who, like most in the field, finds the U.S. Supreme Court’s strictures on pleading problematic, one can only hope that federal judges facing delays or pleading imperfections will be as charitable to consumers, employees, injured drivers, and victims of fraud or discrimination as the Ninth Circuit was to an insurer in Nautilus. See, e.g., A. Benjamin Spencer, Pleading and Access to Justice: A Response to Twombly Apologists, 60 UCLA L. REV. 1710 (2013); Brooke D. Coleman, What If?: A Study of Seminal Cases as If Decided Under a Twombly/Iqbal Regime, 90 OR. L. REV. 1147 (2012); A. Benjamin Spencer, Iqbal and the Slide Toward Restrictive Procedure, 14 LEWIS & CLARK L. REV. 185 (2010).

77. Any inconsistency between RLLI § 21 and R3RUE § 35 did not result from inadvertence or oversight. To the contrary, insurers opposing RLLI § 21 argued that it was inconsistent with Restatement Restatement § 33 and that the RLLI should yield to the R3RUE on this issue. The drafters of the RLLI, who were of course much more focused on insurance than were the drafters of the R3RUE, rejected this view as did the ALI as a whole. Under these circumstances, it is more than a little odd that the Nautilus majority embraced R3RUE § 35 to the exclusion of RLLI § 21.

We are persuaded by the [Restitution] Restatement’s reasoning. When time is precious, it makes sense for the parties to decide quickly what to do, and to litigate later who must pay. Because an insurer risks unbounded liability if it loses the coverage dispute after refusing to defend a suit, it is generally “reasonable [for the insurer] to accede to the demand rather than to insist on an immediate test of the disputed obligation.”

But in hewing to the path of the now superseded (at least functionally per promulgation of the RLLI) R3RUE, the Nautilus majority overlooks the persuasive reasons why the ALI took a different tack when most focused more intently on insurance. The RLLI expressly addressed its relationship to the R3RUE, stating:

The [R3RUE] expresses a general view with respect to recoupment that differs from the special case of the default rule followed in [the RLLI] as a matter of insurance law. As explained in Comment a to this Section, insurers sometimes may feel compelled to provide a defense of a legal action in circumstances where, it turns out after resolution of the coverage dispute, the insurer bore no duty to render such performance. Insurers sometimes defend in these

79. Id. at 688–89 (emphasis in original); see also id. at 690 (noting that the Nevada Supreme Court has “forcefully encouraged insurers to offer to defend doubtful claims” and that “it is only fair to permits those insurers to recover costs that they never agreed to bear”) (citing Century Surety v. Andrew, 432 P.3d 180, 184 n. 4 (Nev. 2018).

In contrast to Nautilus, Andrew was a significant victory for policyholders (as well as a case making use of the RLLI analysis of the issue) in that it held that an insurer in breach of its duty to defend no longer had financial responsibility capped at its policy limits for the result of the underlying litigation, in that case one of catastrophic brain injury resulting in an eighteen million dollar judgment against the insurer based on a policy that, had the insurer provided a defense, would have limited the insurer’s liability to its one million dollar policy limits.

But Andrew hardly a strained gift to policyholders. It follows from the application of ordinary contract principles of consequential damages and was a case in which an insurer could have easily avoided excess liability by simply defending. Instead, the insurer took and lost a multi-million-dollar gamble that it could use information beyond the face of the complaint to avoid even the potential for coverage. Andrew hardly justifies a pro-insurer recoupment rule.

80. The issue of recoupment in the context of insurer defense of claims against a policyholder appears not to have received particularly significant attention during the ALI’s promulgation of the R3RUE. The discussion of recoupment by defending insurers is only a small part of the entire R3RUE.

Further, a mere glance at those involved in creation of the R3RUE and the RLLI reveals that the former Restatement was largely the product of commercial lawyers and scholars with relatively little involvement with insurance, while the latter was steeped in insurance expertise. See infra notes 93–96 (listing R3RUE Advisors and examining R3RUE Members Consultative Group and finding no significant insurance expertise among the former and largely insurer side representatives among the latter).

Without denigration of those involved in the R3RUE, I find it puzzling that the Nautilus majority would turn to this non-insurance document but would largely ignore a more recent, on-point insurance document. In the full disclosure department, I was (as is evident for anyone searching materials in the public domain) an Advisor on the RLLI project but was not significantly or especially involved in § 21 as a promoter, researcher, or drafter. I think I have no subconscious “dog” in this “fight,” other than irritation that the Nautilus majority more or less ignores the careful analysis of an ALI insurance project in deference to an earlier non-insurance product of the ALI.
circumstances, when the insurer believes in good faith (and in fact correctly) that the underlying action is not covered, in view of the risk of enhanced liability that could attend an adverse decision on coverage. See [RLLI] § 27 (a breach of duty to make reasonable settlement decisions exposes the insurer to liability to indemnify without regard to policy limits); § 48 (a breach of duty to defend exposes insurer to liability for all foreseeable loss caused by the breach, without regard to policy limits); § 50 (a breach determined to be in bad faith may expose insurer to additional liability). The R3RUE general rule permits an obligor acting in good faith with regard to a legally uncertain obligation to render the performance demanded under a unilateral reservation of the right to seek restitution. See R3RUE § 35.

This Restatement does not question the R3RUE’s analysis of a general pattern of unjust enrichment outside of the liability insurance context, but there are substantial reasons to conclude that recognition of such a claim by a liability insurer is inappropriate because of special considerations of insurance law. Because the R3RUE treats recoupment of liability insurance defense costs as an instance to which the general view of restitution should apply, without taking full account of these special considerations of insurance law, this Restatement [the RLLI] departs from the defense cost reimbursement position taken in Comment e to R3RUE § 35, which would permit reimbursement. This Restatement does so because, in addition to those reasons for the rule stated in Comment a to this Section, an insurer that chooses to defend under a reservation of rights receives substantial benefits from exercising that choice, beyond avoiding the risk of enhanced liability that could accompany a breach of the duty to defend that causes an excess verdict, or a breach found to be in bad faith. These benefits include maintaining control over the cost, quality, and direction of the defense, obtaining access to privileged defense-related materials, and participating in settlement discussions. All of these benefit the insurer in the event that the legal action is later determined to be within the scope of coverage.

Most restitution claims between insurers and policyholders arise in contexts unrelated to coverage disputes; they more typically involve problems of mistake or subrogation. See Restatement Third, Restitution and Unjust Enrichment §§ 6, 24. The rule stated in this Section has no bearing on the insurer’s entitlement to restitution in these fundamentally different liability insurance settings. See, e.g., § 20, Comment e (following R3RUE § 24 in the context of overlapping defense obligations) and § 28, Comment a (following R3RUE § 24 in the context of equitable subrogation). Moreover, the special insurance-law rule followed by this Restatement can be reconciled with the general R3RUE § 35 rule by recognizing that the premise underlying the general R3RUE § 35 rule (that the party is rendering an extra-contractual performance) and the conclusion that follows from that premise (that the other party is unjustly enriched) do not apply in the context addressed in this Section, in which insurance law is understood to include a no-recoupment default rule. In that case, the insurance policy incorporates the default rule unless the policy states to the contrary. Thus, when an insurer defends under a reservation of
In addition to failing to appreciate this persuasive RLLI analysis, the Nautilus majority glosses over the fact that the insurer, which drafted the insurance policy in question, did not provide for recoupment and instead sought it after the fact when the policyholder was in no position to obtain coverage from another carrier or to register its objection prior to premium payment. The vulnerable policyholder is at least as sympathetic as the insurer worried that failure to defend a close case might result in extra-contractual liability. Nonetheless, the majority gives short shrift to this practical reality of power differential and leverage to find that recoupment was apt where the insurer "clearly reserved its right to do so in writing," without any discussion of whether such a reservation improperly operates as an amendment of the insurance policy, one that is not supported by additional consideration, congruence with policyholder expectations, or any opportunity for fair choice by the policyholder. Both the RLLI and the Nautilus dissent refute this perspective.

Engaging with the majority on the battle turf of insurance structure and function and public policy concerns when addressing insurance disputes, the Nautilus dissent again has the better of the argument.

First, reimbursing an insurer for costs it expended defending a claim that is not potentially covered by the terms of the insurance contract "is inconsistent with the broad duty to defend." The majority's position will narrow this broad duty to defend by making it contingent upon a subsequent judicial determination rather than whether there is potential for liability. Here, Nautilus had some doubt as to whether the insureds' claim was covered. Otherwise, it would have simply declined to defend the insureds without worrying about the risk of breaching the insurance contract. While this may be a difficult decision, "it is a decision the insurer must make" in the first instance. After all, "[i]nsurers are in the business of making this decision." Once the insurer chooses to defend, it is bound by that decision until it obtains a declaratory judgment terminating the duty to defend. I recognize it has now been determined by the federal court that Nautilus never had a duty to defend here, but the retroactive imposition of a recoupment obligation on the insureds would limit the benefit it contracted for pursuant to the duty to defend.

Second, when an insurer chooses to defend a claim that the insurance contract may not cover, it "voluntarily under [takes] the defense for its own interest,"

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81. RLLI, supra note 1, § 21, cmt. b (emphasis added).
82. Nautilus Ins. Co., 482 P.3d at 689.
even though it may have made the payments "under some rudimentary form of protestation." Specifically, "the insurer avoids breaching its duty to defend and incurring the potentially greater expense of defending itself from a claim of breach." Therefore, the insurer is not defending for the benefit of the insured, thus justifying reimbursement; instead, it is doing so to protect itself from potentially greater liability if it is found to have breached its duty to defend. Having weighed those risks and determined the balance favored defending, it should not be able to then reallocate those costs to the insured once it gets a favorable court declaration.

Third, "concerns of equity and fairness weigh against reimbursement, because an insurer benefits unfairly if it can hedge on its defense obligations by reserving its right to reimbursement while potentially controlling the defense and avoiding a bad faith claim." Here, insureds were precluded by the terms of the insurance policy from having any control over the defense of their claim. Under the majority's position, an insurer may defend under a reservation of rights, amass a substantial legal bill, obtain a declaratory judgment absolving the duty to defend, and then seek to recoup the costs of the defense from the insured. Such a rule does not comport with our long-standing recognition of the inherent power disparity between insurers and insureds.

RLLI § 21's Comments and its Reporter's Note—important sources given short shrift by the Nautilus majority—buttress the dissent's assessment. Although it is hard to improve on this (or any) portion of the dissent's analysis, there is another aspect of the majority's deployment of R3RUE and elevation of this older, less on-point Restatement over the RLLI specifically directed toward insurance. On closer examination, the text of R3RUE § 35 and the principle it embodies provides less support to insurers that appreciated by either the Nautilus majority or the R3RUE itself. Section 35 states:

(1) If one party to a contract demands from the other a performance that is not in fact due by the terms of their agreement, under circumstances making it reasonable to accede to the demand rather than to insist on an immediate test of the disputed obligation, the party on whom the demand is made may render such performance under protest or with reservation of rights, preserving a claim in restitution to recover the value of the benefit conferred in excess of the recipient's contractual entitlement.

(2) The claim described in subsection (1) is available only to a party acting in good faith and in the reasonable protection of its own interests. It is not available where there has been an accord and satisfaction,

83. Id. at 695–96 (citations omitted).
84. See RLLI, supra note 1, § 21, Comments and Reporters' Note.
or where a performance with reservation of rights is inadequate to discharge the claimant's obligation to the recipient.85

As noted in the italicized portion of § 35(1) above, restitution is available only if the contract party's performance is not in fact due pursuant to the agreement. The Nautilus majority construed this wording to mean that if an insurer was ultimately found not to have had a duty to defend, performance was not "due," within the meaning of § 35. But this is not quite correct in the insurance context, marking another reason why the more insurance-centered RLLI should be favored over the more general R3RUE.

The design, structure, function, and historical application of a liability insurance policy with defense obligations create a situation in which the policyholder faced with a lawsuit tenders the claim to the insurer. The insurer is then obligated under the contract to assess the tender and make a determination whether to defend the matter, either with or without reservation. That is the performance due under the insurance policy contract. Even if the insurer defending under a reservation of rights ultimately prevails in a declaratory judgment action, the insurer nonetheless always owed the policyholder the performance of evaluating the tender and responding fairly and in good faith.

Consequently, the insurer in these situations always owed at least this quantum of performance in the form of an obligation to make the duty to defend decision. The insurer has options: defend without reservation; defend with reservation; refuse to defend; or negotiate with the policyholder so long as this is done in a non-coercive manner consistent with duties of good faith and fair dealing.86 As the Nautilus majority noted, choosing often puts the insurer in a difficult position. But this is why insurers get the metaphorical "big bucks" of substantial premium payment from customers who may never make a claim, make claims paid in inflated dollars, or make claims years or decades later after insurers have profited, often handsomely, on the investment yield of premium dollars.

Negotiating with the policyholder poses some risk that the insurer will be seen as abusing its bargaining power, which is substantial now that the policyholder is in immediate need of a defense and can no long shop for insurance on the open market. It is rather clearly at the mercy of the insurer.

85. R3RUE, supra note 52, § 35 (emphasis added).
86. Negotiating with the policyholder poses some risk that the insurer will be seen as abusing its bargaining power, which is substantial now that the policyholder is in immediate need of a defense and can no long shop for insurance on the open market. It is rather clearly at the mercy of the insurer. The Nautilus majority failed to appreciate this possibility, although it was most sensitive to the problems insurers face by risking extra-contractual liability if they make the incorrect choice in refusing to defense.
Another shortcoming of the *Nautilus* majority opinion was that it failed to appreciate this result, although it was most sensitive to the problems insurers face by risking extra-contractual liability if they make the incorrect choice in refusing to defense. The asymmetry is disturbing. Insurance is a consistently profitable commercial activity, in states rejecting recoupment as well as those permitting it, which suggests insurers are relatively adept in selecting among duty to defend options.

More important, this selection and choice-making is a core part of contract performance for liability insurers. An insurer's mere eventual win on the duty to defend, even in a non-mixed claim situation, does not entitle it to restitution according to the very terms of R3RUE § 35 invoked by the insurers. The *Nautilus* majority thus misread the black letter of § 35—but so, too did the R3RUE in its commentary and illustration supporting recoupment of defense costs by liability insurers.\footnote{See R3RUE, supra note 52, § 35, cmt. c. In an extensive explanation and illustration, the R3RUE provides the following analysis and illustrations:}

\begin{quote}
[D]isputes between insurers and policyholders over the insurer's duty to pay a claim, or to settle or defend a claim brought against the policyholder, present special difficulties for the law of restitution, because the insurer's duty to indemnify and defend is subject to extensive regulation under local insurance law.

Public policy strongly favors the prompt discharge of an insurer's obligations to its policyholder. If the insurer intends to dispute coverage, protection of the policyholder requires prompt notice of the insurer's legal position. . . .

An insurer deciding whether to accept liability in a doubtful case may face a risk of increased exposure—exceeding the original amount in controversy—if a denial of coverage is later found to be wrongful. Because the denial of a justified claim is made more costly to the insurer than the payment of a claim it might successfully have resisted, the insurer has a legal incentive, in a marginal case, to settle or defend a doubtful claim; but an accord and satisfaction between insurer and policyholder is no less valid because it is negotiated against this legal background. . . .

In the absence of compromise, however, the risk of enhanced liability in coverage disputes may compel a performance by the insurer that is outside the scope of the insurance contract. If the insurer, by denying coverage, risks a potential liability greater than the amount initially in controversy—and if the insurer is obliged to take action before the coverage issue can be adjudicated—the effect of the applicable legal rules may be to subject the insurer to an extracontractual liability. Such a result distorts the parties' allocation of risks and creates the sort of unjust enrichment with which the present section is concerned.

Three forms of recourse enable the insurer to prevent such an outcome. A coverage dispute is normally justiciable in a suit for declaratory judgment. If an insurer is required to act (for example, to accept a tendered defense) before the coverage dispute can be adjudicated, the insurer may proceed subject to reservation of rights. If the policyholder refuses to enter a "nonwaiver agreement" or to accept a defense under reservation of rights, the insurer may protect its position unilaterally. See Illustration 10. If the insurer—having given adequate notice that it is proceeding under reservation of rights—eventually prevails in the underlying coverage dispute, it may recover that part of its outlay that exceeds its policy obligation by a claim in restitution within the rule of this section. See Illustrations 11 and 12.
\end{quote}
The R3RUE reflects an incomplete understanding of insurance in operation and the realistic vulnerabilities of the policyholder, a shortcoming reflected in the Reporter’s Note as well.


Remarkably, the R3RUE Reporter’s Note reads as though the California Supreme Court’s Buss v. Superior Court decision was the unquestioned norm in U.S. law. But the R3RUE was approved in 2011. By that time, in the nearly fifteen years since Buss, state supreme courts in Wyoming,89

Illustrations:

12. Policyholder A demands that liability insurer B defend an action brought by C against A. B takes the view that C’s claims are not even potentially covered by its policy, putting the C lawsuit outside B’s duty to defend. By local insurance law, an insurer has no duty to defend a suit that creates no risk of a covered liability under the policy; but if an insurer refuses to defend a suit that is subsequently determined to have been within its duty to defend, the insurer may be obliged to settle the underlying claims against the policyholder without regard to coverage defenses and even, in some circumstances, without regard to policy limits. To protect itself against additional exposure, B offers to defend the C action, reserving the right to seek reimbursement of defense costs that are held to be outside its contractual obligation. A repudiates the obligation to reimburse B, no matter what the outcome, but accepts B’s defense of C’s claims. B proceeds to defend A, having notified A that it is acting pursuant to a unilateral reservation of rights. B subsequently obtains a declaratory judgment that the C lawsuit is outside the scope of B’s duty to defend, because it states no claims that are even potentially covered under the policy. B has a claim under this section to recover the amounts reasonably expended in the defense of the C lawsuit.

As reflected in this excerpt, the R3RUE as not uninformed about insurance and its stance in favor of recoupment is not unreasonable. But for the reasons set forth in this article, I do think it is quite wrong, particularly in cases such as Nautilus in which there not only is a controlling contract with no provision for recoupment and language best read to the contrary but also where the case for urgency is undermined by insurer delay in asserting recoupment rights and the finding of no duty to defend is questionable.

Further the Nautilus majority’s concerns about insurers facing undue risk of extra-contractual liability or excess of policy limits liability are exaggerated. If an insurer’s refusal to defend is reasonable but unsuccessful, punitive damages are highly unlikely. And while failure to defend gives claimants a better chance of obtaining a large award, they are unlikely to frequently obtain judgments significantly larger than those resulting in defended cases. The claimant’s reasonable range of damages that is subject to policing by the trial court (via judgment as a matter of law and new trial motions, including remitter) remains the same regardless of whether an insurer provides a defense.

88. R3RUE, supra note 52, § 35, Reporter’s Note to Comment a.
Illinois\(^90\) and Pennsylvania\(^91\) had all reached opposite conclusions about the wisdom of recoupment. The R3RUE seems to have overlooked this trend away from \textit{Buss} and been unaware of the general disapproval of \textit{Buss} among insurance scholars.\(^92\)

To a degree this outcome is unsurprising given its focus; the R3RUE was not the work of insurance experts. Although reporter and Michigan Law Professor Andrew Kull is a nationally recognized authority on equitable remedies, he is not an active insurance scholar or teacher.\(^93\) Neither, insofar as it can be determined by readily available information, were many of the Advisors\(^94\) to the R3RUE project.\(^95\) The same is largely true of the Members Consultative Group\(^96\) for the R3RUE. While there were persons


\(^92\) For example, the R3RUE Reporter's Note cites Professor Jerry's article favoring recoupment (\textit{see supra} note 14), cites no secondary literature to the contrary, and does not note that, notwithstanding the prestige of Professor Jerry and insurance expert Douglas Richmond, who allies with him in large part, the bulk of full-time insurance law professors appear to disapprove of the \textit{Buss} holding and rationale.

\(^93\) See University of Texas School of Law website, https://law.utexas.edu/faculty/andrew-kull, which lists his specialties as Contracts, Payment Systems, Remedies, and Restitution and indicates teaching in all of these areas as well as Property. It appears that he has not taught Insurance or Insurance Law or devoted a scholarly article, treatise, or other book to insurance.

\(^94\) At the outset of a Restatement project, the ALI selects a Reporter or Reporters as well as a group of Advisors to serve, as the designation implies, as sources of advice and commentary for written drafts and the substantive content of the Restatement.

\(^95\) See R3RUE, \textit{supra} note 52, at VII–VII. Advisors on the project were Judge Morris Arnold (8th Cir); Attorney Helen Davis Chaitment (Becker & Poliakoff, New York, NY); Professor Melvin A. Eisenberg (Cal-Berkeley); the late Professor E. Allan Farnsworth (Columbia Law); Attorney Susan M. Freeman (Lewis & Roca) (primarily a commercial law firm but one with an insurer side law firm), Professor Daniel Friedman (Tel Aviv University); Professor Mark Gergen (Cal-Berkeley), Attorney R. Nicholas Gimbel (McCarter & English, Philadelphia), Judge D. Brock Hornby (D. Me.), Attorney Richard Hulbert (Clerry Gottlieb, New York, NY); Judge Jack Jacobs (Delaware Supreme Court) (who was also an Advisor to the RLLI); Professor Gareth Jones (Trinity College, Cambridge); Judge Sim Lake (S.D. Tex.); Professor Douglas Laycock (Univ. of Virginia School of Law); Professor John D. McCamus (Osgood Hall Law School, York University, Toronto); the late Justice Pamela B. Minzer (New Mexico Supreme Court), Attorney Philip C. Neal (Neal, Gerber & Eisenberg) (a policyholder-side law firm); Judge Ellen Ash Pesters, Connecticut Supreme Court; Professor Eric Posner (U. Chicago Law School); Judge James Queenan, Jr. (D. Mass. Bkcy); Professor Douglas Rendleman (Washington and Lee School of Law); Judge Judith Rogers, (D.C. Circuit); Professor Peter Schlechtriem (Univ. of Freiburg); Professor. Emily Sherwin (Cornell Law School), Attorney Michael Traynor (Berkeley, CA); Attorney Joseph Wheelock, Jr. (Williamstown, MA); and Professor William F. Young (Columbia Law).

\(^96\) Unlike the Advisors, who are limited in number and expressly invited to participate in a Restatement project, the Members Consultative Group (MCG) is open to any ALI member wishing to volunteer. Reporters developing a Restatement typically meet multiple times over several years with both Advisors and the MCG. Because MCG participation is voluntary, it can be unbalanced in terms of group perspective or loyalty in that there could a disproportionate number of, for example, insurer side or policyholder side MCG members involved with the RLLI.
with considerable insurance background in the Consultative Group, they were largely persons identified with insurers or support for recoupment. Thus, those involved in promulgating the R3RUE that reached the ALI Annual Meeting for approval were largely persons with considerably less knowledge of and “feel” for liability insurance than those involved in the RLLI project. I am not suggesting that the R3RUE group lacked any insurance knowledge. But its insurance expertise pales when compared to that of those involved in the RLLI.

The *Nautilus* majority defends its decision by clothing itself in California precedent that it regards as the “majority” rule, citing at 2006 law review article on the point without recognizing that important anti-recoupment decisions were rendered by the supreme courts of sister states in 2008.

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97. Among the many ALI members participating in the nearly 200-member R3RUE MCG were a number of prominent insurance experts: Attorney William Barker (insurer side); Professor Jay Feinman (Rutgers Law), Attorney Douglas Houser (insurer side), Professor David Hyman (Georgetown Law), Professor Robert H. Jerry, II (Missouri Law); Professor Gregory Maggs (George Washington University Law); Attorney Kurt Melchior (policyholder side); Attorney Richard L. Neumeier (insurer side); Attorney Thomas R. Newman (insurer side); and Tenth Circuit Judge Timothy Tymkovich.

But while not devoid of insurance expertise, the R3RUE Advisors clearly have an expertise deficit when compared to the RLLI Advisors and MCG. This is true even if my assessment has failed to give some Advisors their due on this point. There was far more insurance specialization reflected by the Advisors and MCG members involved with the RLLI. Among the notable insurance experts on the R3RUE MCG, there were four insurer-side lawyers and one policyholder-side lawyer along with a judge and four law professors, one of whom (Professor Jerry) was an avowed supporter of recoupment of counsel fees by insurers.

98. See R3RUE, supra note 52, at VII-VII; University of Texas School of Law website, supra note 93. My rough count based on admittedly streamlined examination of the Advisors finds eight judges, one of whom is known for insurance expertise, twelve law professors, with one (Prof. Young) holding an insurance specialization, and seven practicing attorneys, one working for an insurer side firm and one working at a policyholder side firm.

Insurance issues were but a minor part of a single section in the 2000-page R3RUE. It would be odd to find the Advisor or MCG membership on that project dripping with insurance devotees just as it would be odd to find many restitution or remedies or property scholars among the RLLI Advisors. Without disparaging those who worked so hard on the R3RUE, it simply must be recognized that this group was not one as “tuned into” insurance history, background, structure, function, operation, law, doctrine, and policy as were the RLLI Advisors and MSG.

99. See Angela R. Elbert & Stanley C. Nardoni, *Buss Stop: A Policy Language Analysis*, 13 CONN. INS. L.J. 61, 90 (2006). Apparently lost on the *Nautilus* majority was the article’s overall conclusion that *Buss* was a very poorly reasoned decision that ignored policy language. See id. at 79–100; see also *Buss v. Superior Court*, 939 P.2d 766, 784 (Cal. 1997) (Kennard, J., dissenting) (noting that policy at issue obligated the insurer to defend “suits” and not merely isolated “claims” raising a potential for coverage).

2010, 2013, 2016 as well as federal court decisions predicting rejection of recoupment in other states in 2005, 2009, 2010, 2015, 2016, and 2017. The majority also fails to note that the same article cited for the proposition that recoupment is the majority rule skewers the rationale of recoupment.

In addition to frequently made arguments against recoupment, the article also raises an argument against recoupment based on the Supplementary Payments provision of typical general liability policies that has been insufficiently appreciated by commentators and courts.


102. See Nat’l Sur. Corp. v. Immunex Corp., 297 P.3d 688, 695 (Wash. 2013) (“[I]nsurers may not seek to recoup defense costs incurred under a reservation of rights defense while the insurer’s duty to defend is uncertain.”). A conventional wisdom of the law is that state courts are often more influenced by decisions of neighboring or regional courts than the decisions of distant tribunals. Historically, Nevada law has often been favorably influenced by California precedent. But Washington, another Western state, has also been viewed with favor. See, e.g., Palmer v. Pioneer Inn Assoc., Ltd., 59 P.3d 1237 (Nev. 2002) (embracing the “managing-speaking agent” test for application of Nevada Rule of Professional Conduct 4.2 that was enunciated in Wright by Wright v. Group Health Hospital, 691 P.2d 564 (Wash. 1984)). One wonders why the Nautilus majority was so attracted to the California decisions in Buss and Scottsdale but did not even cite Immunex, the Washington Supreme Court’s more recent and well-reasoned recoupment analysis consistent with the ALI’s analysis.

103. See Attorneys Liab. Prot. Soc’y, Inc. v. Ingladson Fitzgerald, P.C., 370 P.3d 1101 (Alaska 2016) (holding that the Alaska independent-counsel statute means that an insurer cannot obtain recoupment for defense costs even if the insurance policy contains a recoupment provision).


105. Perhaps this result is unsurprising in that the authors are noted policyholder side counsel. But the fact remains that this article cited by the Nautilus majority to support its holding is one that when actually read makes a strong case against recoupment.
Courts permitting reimbursement, such as the California Supreme Court in *Buss*, have proceeded from the premise that standard liability policies are silent as to reimbursement and these courts have been willing to imply such a right by operation of law. Both sides have overlooked key policy language that runs expressly against a right of reimbursement, rendering the policy language-based approach stronger than the courts have presented it.

Not only do standard liability policies generally not include recoupment provisions, they usually expressly disclaim the idea in their supplementary payments clauses. Those clauses promise that the insurer will bear the full cost for cases it defends. This promise precludes allocation of defense costs among claims and forecloses reimbursement.

Standard commercial general liability policies contain supplementary payments provisions stating: “We will pay, with respect to any claim or ‘suit’ we defend: 1. All expenses we incur.” . . .

These supplementary payments clauses unambiguously promise that the insurer will pay “all expenses” that it incurs in connection with suits it defends. The clause is flatly inconsistent with the allocation of defense costs in mixed actions as was done in the *Buss* case. The *Buss* court was willing to allocate defense costs among claims in a suit because the court saw no contractual promise to pay for the defense of all claims in a mixed action. . . .

[But by] promising that the insurer will bear all defense costs for claims and suits it defends, the supplementary payments clause also precludes an insurer’s claim for reimbursement in non-mixed actions. Under the plain terms of the clause, if the insurer defends (whether it acted because its duty was clear or it thought that the question of coverage was close enough so that it would be dangerous to refuse to defend), it must bear those costs. Allowing the insurer to shift defense costs back to the insured through reimbursement would contravene the clause’s express promise that the insurer will pay them. Accordingly, contrary to what a reader may conclude from reviewing cases on both sides of the question, standard liability policies are not silent about allocation or recoupment. They expressly disclaim it.

. . . Given that the insurer has expressly promised to pay all defense costs in any suit it defends, shifting those costs cannot be accomplished by a promise implied in fact or law.106

Put another way, the language of the typical general liability policy (promising to defend “suits” and to pay defense expenses via the supplementary payments clause) leaves the insurer with no “right” to recoupment

106. Elbert & Nardoni, supra note 99, at 94 (footnotes omitted); see also ISO CGL Form CG 00 01 04 13 (ISO 2012) (Supplementary Payments provision in which insurer promise to pay “[a]ll expenses we incur . . . with respect to any claim we investigate or settle, or any ‘suit’ against an insured we defend”). A “suit” is defined as a “civil proceeding” seeking damages and included arbitration and other forms of alternative dispute resolution. Id.
that can be reserved in a defense under reservation as a prelude to seeking recoupment. During the twenty years of recoupment litigation, the supplementary payments provision has been too often overlooked—a sin the *Nautilus* majority perpetuated even as it was citing an article making this very point.

To be fair, the majority also cites the RLLI regarding case counting and recoupment as the majority rule, the RLLI conceding that more courts have permitted recoupment than rejected it. But the *Nautilus* majority makes no express recognition that the recoupment “majority” is thin indeed, particularly when one appreciates that many of the pro-recoupment cases are federal court decisions that may be erroneously predicting state law or the numbers may be inflated by California decisions bound by *Erie v. Tompkins* to follow the *Buss* precedent regardless of its persuasiveness. As the dissent observes, opposition to recoupment “is consistent with a growing number of jurisdictions that reject [*Buss* and] *Scottsdale Insurance*” and California’s approach.107

Viewed with a broad lens, the *Nautilus* majority, although among the more sophisticated analyses favoring recoupment, is less persuasive than the dissent or RLLI § 21 in large part because it reflects functional analysis (i.e., sympathy for insurers needing to decide whether to defend a borderline claim of potential coverage) seeking to justify itself in formalist terms (i.e., the majority’s positively strange assertion that no contract governs the dispute).

The majority opinion would have been more analytically sound had it dispensed with its misplaced, erroneous formalism (i.e., that no contract applies), that permitted the majority to deploy R3RUE § 35 (albeit erroneously) to rescue the insurer from having sold a policy with a broad duty to defend rather than adopting the more obviously applicable RLLI § 21. The *Nautilus* majority opinion would have been better off eschewing misplaced formalism and resting on its functional argument bemoaning the difficult lot of liability insurers as a matter of public policy.

Although more intellectually defensible, such a revised majority opinion would nonetheless be wrong. Prohibiting recoupment absent an enforceable provision in the policy itself is not a rule oppressing insurers, entities that figuratively hold the keys to their own cell through the ability to revise the take-it-or-leave it adhesion contracts that they sell to policyholders. Contra the four-justice *Nautilus* majority, the equities of recoupment auger in favor of policyholders, as concluded by the ALI and numerous state supreme court justices as well as the three Nevada Justices comprising the *Nautilus* dissent.

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In addition, as noted by the ALI, insurers gain substantial advantages by shouldering a broad duty to defend obligation even in the absence of a mandatory rule of recoupment:

(a) the insurer can defer its determination of coverage issues, thus avoiding being estopped to deny its indemnity obligation if it later turns out that it did have a duty to defend;
(b) the insurer can control defense expenditures;
(c) the insurer can ensure that the claim is effectively defended, thus minimizing its potential indemnity exposure;
(d) the insurer can participate in, and perhaps control, settlement negotiations; and
(e) the insurer can gain access to otherwise-privileged communications.\textsuperscript{108}

If handkerchiefs are to be unfurled in reaction to the tears occasionally inflicted by the business and litigation world, they should be saved for a better cause than insurer recoupment of defense costs. Admittedly, insurers face something of a dilemma in deciding how to respond to a tendered case that appears on the boundary of or outside the duty to defend. But this is a dilemma for which the insurer signed on as a cost of doing business, a cost it tends to replenish many times over in the form of premium payments and investment income.\textsuperscript{109}

\textsuperscript{108} See RLLI, supra note 1, § 21, cmt. b Reporters' Note (citing KENNETH S. ABRAHAM & DANIEL SCHWARCZ, INSURANCE LAW AND REGULATION 584–86 (6th ed. 2015)); see also id. § 21, cmt. b (“[A]n insurer that chooses to defend under a reservation of rights receives substantial benefits from exercising that choice, beyond avoiding the risk of enhanced liability that could accompany a breach of the duty to defend that causes an excess verdict, or a breach found to be in bad faith. These benefits include maintaining control over the cost, quality, and direction of the defense, obtaining access to privileged defense-related materials, and participating in settlement discussions. All of these benefit the insurer in the event that the legal action is later determined to be within the scope of coverage.”).

\textsuperscript{109} Warren Buffett, who has described his company Berkshire-Hathaway as primarily an insurance company, notes that the insurers owned by Berkshire-Hathaway earn most of their profits not from underwriting but from the float of premiums collected well before claims are paid under the policies for which those premiums were charged. See Letter from Warren Buffett to Shareholders 8–1 (2000), http://www.berkshirehathaway.com (last visited Oct. 18, 2021); see also Richard E. Stewart & Barbara D. Stewart, The Loss of Certainty Effect, 4 RISK MGMT. & INS. REV. 29, 32 (2003) (insurers have explicitly recognized that “the earnings on funds reserved for claims [are] the most significant component of earnings for a property liability insurance company” and “[i]nsurance managements are more than sufficiently intelligent to see that delaying the payment of claims increases the float period and denying claims decreases the cost”); SCOTT E. HARRINGTON & GREGORY R. NIEHAUS, RISK MANAGEMENT AND INSURANCE ch. 6, Insurance Pricing 123–35 (1999) (insurers profit on investment income and delayed payment of claims; underwriting cycles can vary according to changes in investment return and in reaction to previous pricing strategies as well as “capital shocks” from large losses); MARK R. GREENE, RISK AND INSURANCE 147 (4th ed. 1977) (“In property and liability insurance, investment income has accounted for a very substantial portion of total profits and has served to offset frequent underwriting losses.”).
An analogy to tort theory is instructive. More than fifty years ago, then-Professor, now Judge Guido Calabresi persuasively argued that a sensible means of assigning tort liability was to place it upon the party best able to reduce the social costs of injury. In the insurance context, this view augers against recoupment, even in cases where a court ultimately sides with the insurer regarding duty to defend. The RLLI recognized this outcome in determining its position on recoupment.

As previously noted, the insurer by virtue of contract (the insurance policy that it drafted that does not address recoupment) is obligated to perform a duty to defend analysis. To be sure, that analysis can be difficult where the insurer believes that there is no potential for coverage but faces a risk that a court could disagree, resulting in loss of indemnity coverage defenses or protection of the policy limits as cabining payment obligations or other statutory or common law liability for failing to defend.

But, as discussed above, a difficult situation is not necessarily an unfair or unwarranted situation. Insurers are in the business of accepting transferred risk and pooling it, distributing it so that their exposure is not unduly concentrated and is spread in time and space so that it is very unlikely to undermine company solvency even where the insurer faces unusual amounts of policyholder liability or adverse court decisions regarding defense obligations or insurer conduct. As compared to the typical policyholder, the typical insurer possesses comparatively substantial wealth and can spread risk more effectively than policyholders.

Resolving close questions in favor of policyholders (who could be ruined by either the absence of a defense or an obligation to reimburse insurers for defense expenditures) makes socioeconomic and practical sense. Even if faced with higher than anticipated financial responsibility for claims eventually deemed not to have triggered defense obligations, insurers can

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111. See supra note 6.

112. Risk transfer and distribution is the essential description of what insurers do in using a business model in which the policyholder incurs a small but fixed loss (payment of premiums) in return for the insurer's commitment to provide coverage (up to the policy limits along with other clearly stated limitations on coverage) in the event that the policyholder is faced with a contingent but larger loss such as being sued or suffering a property loss. See Jeffrey W. Stempel, Erik S. Knutsen & Peter N. Swisher, Principles of Insurance Law § 1.03, at 17–20 (5th ed. 2020).

113. See Richard V. Erichson et al., Insurance as Governance 5–6 (2003) (noting that insurance industry standing alone would be the fourth largest economy in the world).

usually weather whatever storm ensues. Further, there is to date little or no evidence suggesting that the unavailability of recoupment in states like Illinois or Pennsylvania has caused significant cost to insurers operating in those states. If it did, insurers would presumably note this in their briefs in recoupment cases (which has not happened) or write policies establishing clear rights to recoupment, something that they have consistently eschewed for general liability policies.

IV. CONCLUSION: THE POTENTIALLY LIMITED VOYAGE OF NAUTILUS

Although Nautilus is a significant blow against RLLI § 21, it is hardly a knockout punch. The specific facts of the case favoring the insurer and the closeness of the decision, particularly in light of insurer resources expended, undermine the influence of the decision. Future courts will be better served by embracing the Nautilus dissent and the ALI’s analysis of the recoupment issue.

Regarding resources and advocacy, future courts would also do well to appreciate that imbalance between the insurance industry and individual policyholders. In the Nautilus litigation, for example, both the insurer and the insurance industry invested substantial resources in their successful search for a favorable state law ruling.

Primary counsel for the insureds was an attorney in a two-person firm, albeit one with connections to two well-respected small firms with considerable insurance expertise. In contrast, Nautilus retained a 300-lawyer national firm with a local office of more than twenty lawyers.

115. Insurers have survived what may be termed avalanches of claims obligations stemming from mass torts such as asbestos and pollution as well as the constant flow of automobile collisions, suffering some at the bottom line but retaining their capital, solvency, and market niche. Consider asbestos, the largest tort source in human history. Many policyholders manufacturing, using, or distributing the product became defunct even if insured. Insurers incurred only the episodic and isolated company failure. See Jeffrey W. Stempel, Assessing the Coverage Carnage: Asbestos Liability and Insurance After Three Decades of Dispute, 12 CONN. INS. L.J. 349, 363 n.34 (2006) (asbestos crisis inflicted only a 1.5–3% drag on insurer earnings).

116. Jordan Schnitzer, now in a two-person firm, appeared to take the most prominent role in representing Access Medical in the Nautilus litigation. He has ties to Kravitz, Schnitzer, Johnson Watson & Zeppenfield (ksjattorneys.com), a six-lawyer firm with an office in Las Vegas that is affiliated with Christian, Kravitz, Dichter, Sluga & Johnson, which has a dozen lawyers, another office in Las Vegas and one in Phoenix. Name partner Martin Kravitz, who has vast insurance litigation experience (usually deployed on behalf of insurers), was also involved. Access Medical had more than competent counsel, but its legal team was substantially smaller than that of Nautilus, and it lacked the support received by Nautilus from industry groups.

117. Nautilus counsel Selman Breitman LLP, although concentrated in the West, is a nationally known insurer-side law firm with nine offices and more than one hundred attorneys. According to data compiled by Lex Machina, insurance is the firm’s dominant practice area.
gained additional support from an insurer-sponsored amicus brief which included the state's arguably most accomplished appellate advocate\(^{118}\) and was authored by one of the nation's pre-eminent insurer side coverage counsel,\(^{119}\) who was also permitted oral argument. Notwithstanding the quality of policyholder counsel submissions and advocacy, *Nautilus* was marked by an asymmetry of advocacy.

In future cases dealing with important insurance questions of first impression, courts should strongly consider soliciting non-insurer amicus briefs when necessary to provide a more balanced perspective and thorough examination of insurance law questions of first impression. Policyholder interests simply lack the same institutional structure that insurers possess and use to make sure their voice is heard.

At a minimum, future courts should appreciate that whatever persuasive force attaches to a recoupment action where the lawsuit lacks any potentially covered claims is completely absent in mixed claims that contain at least one potentially covered claim. Unless and until insurers revise their policy language in sufficiently express terms, a single potentially covered claim in a "suit" should be sufficient to require defense of the entire action without the prospect of recoupment.

There is no textual basis in the policy for apportioning the duty to defend (which is generally viewed as indivisible) on a claim-by-claim basis. Where this defense obligation is imposed by the insurer's own choice of policy language, permitting recoupment on misplaced equitable grounds stemming from asymmetric sympathy favoring insurers deprives policyholders of the benefit of the bargain made when buying liability insurance as well as undermining effective risk management and the public policy goals of efficient dispute resolution.

\(^{118}\) Involved in the amicus brief supporting the insurer were Daniel F. Polsenberg and Joel D. Henried. In Nevada appellate litigation, Polsenberg is perhaps the State's closest thing to frequent U.S. Supreme Court advocate John W. Davis. He has been involved in more than 200 cases before the Nevada Supreme Court, with Henried involved in almost 50. Their firm, Lewis Roca Rothgerber Christie, which began in Phoenix, now operates nine offices with 300 attorneys, 35 of whom are in the firm's Nevada offices.

\(^{119}\) In addition to *Nautilus* and its elite legal team, insurance industry participation in the matter involved not only accomplished Nevada counsel but also nationally prominent attorney Laura Foggan (who had been the insurance industry's representative in the RLLI drafting process and has written extensively on the RLLI and recoupment); see *Insurer Recoupment of Defense Costs: Why the Restatement Adopts the Wrong Approach*, 68 Rutgers U.L. Rev. 193 (2015) on brief and participating in oral argument. Her firm, Crowell & Moring, has nine offices, more than 500 lawyers and is one of the 100 largest in the United States. The amicus brief was filed under the auspices of two insurer organizations. See Brief of Amici Curiae Complex Ins. Claims Litig. Ass'n & Am. Prop. Cas. Ins. Ass'n, 2021 WL 2498591 (Nev.).