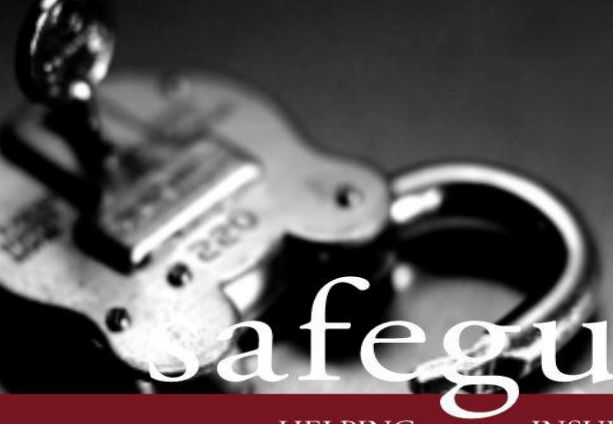

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safeguards

HELPING INSURERS PROTECT THEIR CLIENTS

Court of Appeals clarifies when a carrier's belated assertion of a coverage defense constitutes a waiver

By Drew W. Broaddus **March 6, 2017**

For over a century, it has been settled Michigan law that "when a loss under an insurance policy has occurred and payment refused for reasons stated," the insurer must "fully apprise the insured of all of the defenses it intends to rely upon, and its failure to do so" waives all coverage defenses "other than those of which it has thus given notice." *Smith v Grange Mut Fire Ins Co*, 234 Mich 119, 122-123 (1926). This principle can be traced back as far as *Castner v Farmers' Mut Fire Ins Co*, 50 Mich 273, 275 (1883) (stating that when the insurance company has asserted two grounds for denying coverage at the time the suit was initiated it "was not at liberty thereafter to vary their grounds and offer new or additional objections").

But there is another line of insurance cases, itself nearly a century old, holding that "waiver or estoppel will not operate against an insurer where doing so would require coverage that is not provided by the policy or is expressly excluded by the policy." *Amerisure Mut Ins Co v Carey Transp Inc*, 578 F Supp 2d 888, 893 (WD Mich 2008). In Michigan law, this line of cases starts with *Ruddock v Detroit Life Ins Co*, 209 Mich 638, 654 (1920). In *Ruddock*, the plaintiff brought an action on a life insurance policy where the insured had died in military service in World War I. The policy excluded coverage while the insured was in the "naval or military service in time of war." The plaintiff asserted the defendant had waived this provision by initially taking steps to process the claim. *Id.* at 652-653. The Court suggested that the defendant likely did not have knowledge of the insured's military service but declined to rest its holding on that ground. *Id.* at 653. Rather, the Court held that waiver and estoppel could not be used to create a new contract. "To apply the doctrine of estoppel and waiver here would make this contract of insurance cover a loss it never covered by its terms, to create a liability not created by the contract and never assumed by the defendant under the terms of the policy. In other words, by invoking the doctrine of estoppel and waiver it is sought to bring into existence a contract not made by the parties,

SECREST WARDLE NOTES

Bartlett Investments, Inc v Certain Underwriters at Lloyd's, __ Mich App __; __ NW2d __ (2017) (Docket No. 328922) underscores that certain grounds for denying coverage are waived if they are not stated in the initial denial letter.

Bartlett Investments also reiterates that a catch-all or boilerplate reservation of rights clause is generally not sufficient to preserve grounds for denying coverage that are not otherwise specified in the denial letter. *Id.* at __; slip op at 4.

However, a waiver cannot create coverage for "risks that were not included in the policy." *Id.*

to create a liability contrary to the express provisions of the contract the parties did make." *Id.* at 654. *Ruddock* was later followed in *Kirschner v Process Design Assoc, Inc*, 459 Mich 587, 593-594 (1999), where the Court found that "the application of waiver and estoppel is limited, and, usually, the doctrines will not be applied to broaden the coverage of a policy to protect the insured against risks that were not included in the policy or that were expressly excluded from the policy."

In insurance litigation these two principles often come into conflict. In *Bartlett Investments*, the Court of Appeals provided some guidance as to how these two lines of cases can be reconciled. In *Bartlett Investments*, the insured was the owner of a vacant building for which it purchased a commercial property insurance policy. Because vacant buildings carry a significantly greater risk for vandalism and damage than occupied buildings do, Bartlett Investments had to obtain a policy that carried special certificates of coverage regarding vacant buildings. Two provisions of that coverage are relevant here. First, the policy provided that "any loss or damage caused by Vandalism must be reported to [Lloyd's] within ten (10) days after the Insured first learns of the loss or damage." *Bartlett Investments*, __ Mich App at __; slip op at 1. Second, the policy provided that, as a condition of coverage, the insured must assure that the building "be fully secured against unauthorized entry at all times" and that "the insured property shall be inspected regularly by the Insured or the Insured's agent during the policy period." *Id.* On or about February 1, 2013 the insured discovered extensive vandalism damage to the building and submitted a claim to the insurer. The insurer rejected the claim.

The insurer, Lloyd's, stated in its denial letter that the damage was "a combination of overlap with" an earlier covered loss (which it had already paid) and "wear and tear, maintenance and theft." *Id.* The denial letter also noted some "indication of long-term water damage," and concluded that "none of these are Covered Causes of Loss…." *Id.*

The insured then filed suit. Once the claim was in litigation, Lloyd's relied on two grounds for denial that had not been referenced in the denial letter: (1) failure to comply with the ten-day notice provision and (2) failure to comply with the requirement to make "regular inspections" and to keep the building secured. *Bartlett Investments*, __ Mich App at __; slip op at 2. Lloyd's prevailed on summary disposition, and the insured appealed.

On appeal, the panel unanimously found that Lloyd's argument regarding the ten-day notice requirement had been waived, because Lloyd's did not raise it in its initial denial letter. However, the panel affirmed the summary disposition ruling based on the insurer's failure to make "regular inspections." *Id.* at __; slip op at 5-6.

In finding that the ten-day notice issue had been waived, the panel rejected Lloyd's argument that although not expressly stated, this defense to coverage had been preserved by the following clause in the denial letter: "By stating the above, Minuteman Adjusters, Inc. and [Lloyd's] do not waive any of their rights or defenses that they now have or may discover in the future. All rights, defenses and privileges afforded by the above-referenced policy or by law are expressly reserved." *Id.* at __; slip op at 4. The panel cited *Meirthew v Last*, 376 Mich 33, 37-38 (1965) for the proposition that "general reservation of rights language was not sufficient to comply with an insurer's notice obligations…." *Bartlett Investments*, __ Mich App at __; slip op at 4. "If general reservation of rights language like that relied upon by defendant were sufficient to comply with an insurer's obligations, then insurers would be able to issue overly broad and vague denial letters without giving their insureds any indication of what provisions in the policy they ultimately intend to rely upon in denying coverage." *Id.* at __; slip op at 4.

But with respect to the insured's failure to make regular inspections, the panel noted that the above-referenced waiver doctrine "has an exception for waivers that would protect the insured against risks that were not included

in the policy." *Id.*, citing *Kirschner*, 459 Mich at 593-594. This exception did not apply to the ten-day notice requirement because a failure to meet this *after-loss* requirement did not expand the type or extent of risks undertaken by the insurer. On the other hand, "requiring defendant to provide coverage for repeated vandalism to a vacant building that, contrary to the explicit requirements of the policy, was not secured or regularly inspected would substantially expand the degree of risk undertaken by the insurer." *Bartlett Investments*, __ Mich App at __; slip op at 4. Unlike the notice requirement, "these actions were to take place before the loss and were specifically directed at reducing the likelihood and possible extent of the type of loss actually suffered." *Id.* The opinion went on to explain that the insured failed to create a question of fact as to whether the inspection requirement had been satisfied.

Had Lloyd's issued a true reservation of rights letter – as opposed to a coverage denial letter with a reservation of rights clause included – the panel may have reached a different result regarding Lloyd's waiver of the ten-day notice issue. This is because "a reservation of rights," as "contrasted with an actual denial of coverage," does "nothing more than to preserve for future decision the question of whether insurance coverage does or does not exist…." *Salazar v Bocanegra*, 2012 WL 12892780, at *2 (D NM July 27, 2012), quoting *Native American Arts, Inc v Bundy-Howard, Inc*, 2003 WL 16524649, at *2 (ND Ill March 20, 2003).

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