In Search of Consistency in Insurance Claims Handling: Discovery of Insurance Companies' Files on Reserves and Other Policyholders' Claims

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The authors discuss the value in obtaining discovery of other policyholders' claims files and insurance company reserve information.

All too often, getting an insurance claim paid becomes a surreal journey into a world seemingly unbound by the laws of reason. It is a world of doubt and uncertainty, completely disconnected from the "good hands" and "piece of the rock" insureds thought they were getting when they paid their premiums. It is the feeling one has that the insurance company's loss adjuster knows that a claim is worth more than the amount the insurance company is offering to pay, and is trying to "lowball" with the current offer. It is the feeling that a policyholder is not getting the same treatment as other similarly situated policyholders. The quest for answers to such vexing concerns probably will not cause Leonard Nimoy to produce a new episode of "In Search Of…" — but

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finding out the answers is not exactly as hard as getting a photo of the Loch Ness Monster or Bigfoot, either.

When forced to sue their insurance company for breach of contract or bad faith, smart policyholders often seek discovery from the insurance company regarding other policyholders' claims files and the insurance company's calculation of reserves for their claim. The insurance company's handling of other, similar claims can demonstrate how it has interpreted key terms and conditions in the policy at issue, and inconsistencies can provide evidence of bad faith. Reserve information can demonstrate whether the insurance company intended to pay the underlying claim, the thoroughness of the investigation, and how the insurance company viewed its own liability and obligations under the policy. In response, it is not unusual for insurance companies to refuse to produce such material, and there are many cases in various courts across the United States that address these important issues.

Generally, under the rules of civil procedure, parties are entitled to discovery of any information that is not privileged and that is relevant to any claim or defense.[1] However, discovery of information is not unlimited or open-ended — a court can limit discovery of relevant material if it determines that the information sought is unduly burdensome or unreasonably duplicative.[2] Various courts have allowed policyholders to obtain information regarding reserves and other policyholders' claims by balancing that information's relevance to the particular policyholder's case against the insurance company's concerns regarding privilege, confidentiality, and burdensomeness. This article addresses general considerations regarding these issues and examines two recent rulings supporting the discoverability of this information.

DISCOVERY OF "OTHER" CLAIMS FILES

Typically, other policyholders' claims files are sought in insurance coverage litigation to demonstrate that the insurance company has acted in an inconsistent manner in resolving claims where similar policies were involved.[3] Insurance companies often object to the production of these files on the following grounds: (1) differences between the claims or pol-

icy language at issue renders the insurance company's handling of one claim irrelevant to its handling of the other; (2) the "other" claims files contain confidential or proprietary information regarding the other policyholder's business; and (3) it would be unduly burdensome for the insurance company to compile the requested information.

Where the information sought by the policyholder is deemed relevant to the particular facts of the coverage case, courts typically address the confidentiality issue by requiring the insurance company to redact confidential information from the documents and generate a privilege log before turning over the requested documents.[4] Courts typically have addressed the burden issue by limiting the scope and extent of the production in order to balance the importance to the policyholder with the burden on the insurance company.[5]

Although insurance companies generally are unhappy with such outcomes, when the shoe is on the other foot, they themselves take the position that "other" claims files are discoverable. For example, in a recent reinsurance case in New York, Zurich Insurance Company moved the court to compel its reinsurance company to produce comparable "other" claims files. In *Zurich American Ins. Co. v. Ace American Reinsurance Co.*,[6] Zurich alleged that its reinsurer did not pay its share of a settlement reached with Zurich's policyholder. Zurich alleged that the refusal to pay was evidence of the reinsurer's pattern of behavior and that it had similarly refused to pay other reinsureds. Zurich moved to compel the reinsurer to produce documents relating to two lawsuits in which the reinsurer was found to have wrongly denied payment to its reinsureds, as well as all documents on any claims denied by it on the basis of allocation (which was at issue in the dispute with Zurich). While noting that motive and, thus, "similar acts" evidence is usually immaterial to breach of contract claims, the court found that the reinsurer's handling of similar claims could provide evidence of how it had interpreted its obligation to follow the settlements of its reinsureds in similar circumstances by shedding light "on the meaning that the parties ascribed to the terms that they incorporated into the policies at issue."[7] Consequently, the court found that the requested information was relevant and discoverable.

The reinsurer also opposed the production of "other" claims files on

grounds of burdensomeness. The reinsurer argued that its computer system was incapable of segregating claims, the type of claim, or the reason the claim was denied. While the court recognized that the "volume of data accumulated" by the defendant made a "search of its entire database infeasible," it nevertheless found that "a sophisticated reinsurer that operates a multimillion dollar business is entitled to little sympathy for utilizing an opaque data storage system, particularly when, by the nature of its business, it can reasonably anticipate frequent litigation."[8] Ultimately, the court ordered the parties to "propose a protocol for sampling" the reinsurer's claim files in order to obtain examples of claims files in which issues of the allocation of policy limits had been addressed.

DISCOVERY OF RESERVE INFORMATION

The claims file for a given claim typically includes documentation regarding the setting of reserves, which basically is the amount of money the insurance company sets aside on its books to ensure the ability to pay the claim. As noted in *Nicholas v. Bituminous Casualty Corp.*:

> Setting reserves is a method of managing litigation in which attorneys, claims adjusters and/or line personnel compile their mental impressions and opinions concerning the substance of the litigation as well as the cost of litigation. Specifically, when setting a reserve, attorneys and claims personnel not only assess the value of the claim based on the available evidence and the strengths and weaknesses of the claim, but also take into consideration the probability of an adverse judgment, the jurisdiction, and the fees and expenses that may be incurred in defense of the claim.[9]

Reserve information is particularly relevant in bad faith cases because it provides insight into the thoroughness of the insurance company's investigation of the policyholder's claim and how it viewed its obligations to the policyholder.

Many courts have held that reserve information is prepared in the ordinary course of business and, therefore, is discoverable.[10] Other courts, however, have held that reserve information is prepared in antici-

pation of litigation and, therefore, is protected from discovery by the work-product privilege.[11]

In one noteworthy recent case, the United States District Court in Georgia ordered an insurance company being sued for bad faith to turn over reserve information, as well as documents describing how employees are paid for handling claims. In *Central Georgia Anesthesia Servs., P.C. v. Equitable Life Assurance Society of the U.S.*,[12] a corporate policyholder filed an insurance coverage action to obtain its coverage under a disability income protection policy that insured one of its shareholders. The policyholder alleged that the insurance company agreed to pay $400,000 if the shareholder became disabled before age 60, and that the insurance company refused to pay the maximum benefit after the shareholder became disabled at age 43. The insurance company took the position that the shareholder was entitled to only $18,000. The policyholder sued for breach of contract and bad faith.

During discovery, the policyholder learned that the insurance company was losing money on its policies, and that the insurance company's employees might have been given incentives to deny or take hard stances on claims. The policyholder moved the court to compel the discovery of various documentation relevant to the case — including reserve information. The court held that the insurance company had to disclose the amount of its reserves and the method it used to set those reserves. Although the court noted that other courts have differed on whether reserves are discoverable, it observed that the "overwhelming majority of courts" find reserves discoverable in cases involving bad faith claims, because "reserves bear some relationship to the insurer's calculation of its potential liability."[13] The court reasoned that, since the parties were disputing the intended value of the benefits payable under the policy, the reserve information might reveal what the insurance company understood that benefit to be at the time the insurance contract was signed.

CONCLUSION

Discovery of other policyholders' claims files and insurance company reserve information could make or break a policyholder's insurance

coverage case. Obtaining this information is not the stuff of urban legend. Policyholders can rely on experienced coverage counsel to search for — and find — the answers to the perplexing issues that arise when a policyholder is looking for answers (and claims payments) from its insurance company.

NOTES

[1] *See, e.g.,* F.R.C.P. 26(b)(1).

[2] *See, e.g.*, F.R.C.P. 26(b)(2)(i)-(iii).

[3] *See, e.g. Nestle Foods Corp. v. Aetna Cas. & Sur. Co.,* 135 F.R.D. 101, 106-07 (D.N.J. 1990) (holding that information regarding other policyholders' claims is relevant for purposes of discovery, since it may show that identical language has been afforded various interpretations by the insurance company).

[4] *See, e.g., West Virginia Fire & Cas. Co. v. Karl*, 202 W. Va. 471 (1998) (holding that a policyholder in an automobile liability case was entitled to discovery of redacted copies of claims files; insurance company could adequately protect the privacy interests of nonparties by redacting names, addresses, and other personal information).

[5] *See, e.g., Marisol v. Travelers Indem. Co.*, No. L-3893-93, slip op. at 6-7 (N.J. Super., Law Div., Middlesex Cty., Dec. 9, 1996), reprinted in Mealey's Litig. Rep. — Ins., at I-1 (Jan. 14, 1997) (ordering the production of the insurance company's 10 earliest claims files for a particular site and its 10 latest claims files at that site).

[6] 2006 WL 3771090 (S.D.N.Y. Dec. 22, 2006).

[7] 2006 WL 3771090 at *1.

[8] 2006 WL 3771090 at *2.

[9] 235 F.R.D. 325, 329-30 (N.D.W. Va. 2006) (internal citations omitted).

[10] *See, e.g., Country Life Ins. Co. v. St. Paul Surplus Lines Ins. Co.,* 2005 WL 3690570 (2005 D.C. Ill.) (holding that documents regarding the setting of reserves are "reasonably calculated to lead to discovery of admissible evidence" and are therefore discoverable, and that reserves are prepared in the "'ordinary business' of an insurance company" and, therefore, are not privileged).

[11] *See, e.g., Peco Energy Co., et al. v. Ins. Co. of North America, et al.*, 852 A.2d 1230 (Pa. Super. 2004).

[12] 2007 WL 2128184 (M.D. Ga. July 25, 2007).

[13] 2007 WL 2128184 at *2.

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