

Client Alert

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Policyholder Can Recover Damages For Aggravation And Inconvenience Caused By Insurer's Wrongful Refusal To Defend

The Fourth Circuit recently held that a policyholder may recover damages under West Virginia law for "aggravation and inconvenience" resulting from its insurer's wrongful refusal to defend an underlying liability action. *Graham v. Nat'l Union Fire Ins. Co.*, 2014 WL 350147 (4th Cir. Feb. 3, 2014).

Background

Robert Graham, the former executive director of Council on Aging Inc. and another nonprofit corporation, was sued by the state of West Virginia for allegedly manipulating the members of the boards for each corporation in order to improperly inflate his salary and benefits.

Graham sought a defense and indemnification under a liability insurance policy issued by National Union. National Union denied coverage and refused to defend Graham in the state's suit. Graham defended himself in the litigation until it was ultimately dismissed as moot due to Graham's removal and an accompanying mutual release of liability between Graham and the corporations.

Graham sued National Union, alleging that National Union breached the insurance policy by refusing to provide a defense to Graham in the underlying lawsuit. After finding that the policy obligated National Union to defend Graham, the Fourth Circuit remanded the case to the district court to determine Graham's damages.

The district court awarded damages to Graham for the attorneys' fees he incurred in defending the underlying suit and for the attorneys' fees he incurred in the litigation against National Union. However, the district court denied Graham's request for aggravation and inconvenience damages resulting from National Union's failure to defend. Graham appealed the denial of aggravation and inconvenience damages to the Fourth Circuit.

The Fourth Circuit's Opinion

The Fourth Circuit reversed the district court's refusal to award aggravation and inconvenience damages. The court based its decision, in part, on a prior ruling from the Supreme Court of Appeals of West Virginia holding that policyholders may recover aggravation and inconvenience damages where those damages are a consequence of a property insurer's failure to pay policy benefits. *Hayseeds, Inc. v. State Farm Fire & Casualty*, 352 S.E.2d 73 (W. Va. 1986). The court also looked to the seminal West Virginia decision on policyholder remedies for insurers' breaches of contract, *Aetna Casualty & Surety Co. v. Pitrolo*, 342 S.E.2d 156 (W. Va. 1986), where the court found broadly that a policyholder could recover not only the attorneys' fees incurred in his defense of the underlying negligence actions, but also the attorneys' fees he incurred in the coverage litigation with Aetna.

Applying these precedents, the Fourth Circuit found it was error for the district court to draw a distinction between types of consequential damages sought by Graham. As the court explained, "there is no logical

reason to authorize an award for one item of consequential damages — attorney fees in the enforcement litigation — while simultaneously denying recovery for aggravation and inconvenience, which are merely other items in the same category.”

The Fourth Circuit also rejected the district court’s attempt to distinguish *Hayseeds* on the grounds that decision involved first-party insurance and, thus, did not involve a duty to defend. The Fourth Circuit found that distinction to be immaterial to the types of consequential damages that would flow from a contractual breach. In either case, the court explained, the policyholder is “entitled to the full array of consequential damages ordinarily available to the insured in a breach-of-contract proceeding.” Accordingly, the Fourth Circuit remanded the case to the district court for further proceedings to determine Graham’s aggravation and inconvenience damages.

Insurance Implications

Graham illustrates the significant consequences of an insurer’s breach of its contractual obligations. These consequences include not only the coverage that would have been provided had there been no breach, but also the consequential harm inflicted on the policyholder by the insurer’s improper conduct. These damages stand as a powerful deterrent to carrier malfeasance. Policyholders, therefore, should remain vigilant about identifying, quantifying and pursuing all types of damage that result from an insurer’s refusal to defend or otherwise honor the policy, thereby ensuring that policyholders are put into the same position they would have been had the insurer fulfilled its contractual obligations.

Contacts

Walter J. Andrews
wandrews@hunton.com

Lon A. Berk
lberk@hunton.com

Lawrence J. Bracken, II
lbracken@hunton.com

John C. Eichman
jeichman@hunton.com

Robert J. Morrow
rmorrow@hunton.com

Syed S. Ahmad
sahmad@hunton.com

Michael S. Levine
mlevine@hunton.com

Sergio F. Oehninger
soehninger@hunton.com

William T. Um
wum@hunton.com

Patrick M. McDermott
mcdermottp@hunton.com