MEDIATING THE COVERAGE/BAD FAITH DISPUTE

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I. OVERVIEW

The term “mediate” is derived from the Latin "mediare" which means, “to be in the middle". Mediation is appropriate for cases ranging from small to the complex and multi-party litigation. Mediation is a forum in which an impartial person, the mediator, attempts to facilitate and assist the parties in resolving their disputes themselves. The authority for referral of cases to mediation is found in Texas Civil Practice & Remedies Code §154.001, *et seq*. The parties to a civil suit can be ordered to participate in mediation. Section 154.022 of Texas Civil Practice and Remedies Code authorizes an objection, which must be filed within ten days of the court’s order. TEX. CIV. PRAC. & REM. CODE ANN. § 154.022(b).

Although parties can be ordered to participate in a mediation conference, they cannot be forced to make demands or offers, or to settle the case. *Decker v. Lindsay*, 824 S.W.2d 247, 251 (Tex. App.- Houston [1st Dist.] 1992, orig. proceeding). The courts often believe that mediation may be beneficial even if the parties do not believe that the process will resolve the lawsuit.

Confidentiality of the mediation process is addressed in section 154.073 of the Texas Civil Practice and Remedies Code. This section does not use the word "privileged," but the matters discussed and revealed in a mediation are confidential and not subject to disclosure. However, if parties become aware of information at mediation, that information may become discoverable. *See In Re Learjet Inc*. 59 S.W.3d 842, 845 (Tex. App.—Texarkana 2001, orig. proceeding).

A mediated settlement agreement is enforceable in the same manner as a contract. The settlement agreement must be in writing. TEX. R. CIV. P. 11; TEX. CIV. PRAC. & REM. CODE ANN. § 154.071(a). A party has the right to revoke consent to a settlement agreement where the settlement agreement has not been signed or filed part of the record. An agreement is enforceable if it is "complete within itself in every material detail, and contains all of the essential elements of the agreement." *Padilla v. LaFrance*, 907 S.W. 2d 454, 460 (Tex. 1995). Written mediation agreements protect the interest of all and the integrity of the dispute resolution process.

Insurance disputes, whether between insurer and insured, or between multiple carriers, are peculiar in various aspects. For this reason, the mediation process may need to be tweaked to fit the specific scenario. However, the mediation process can serve the parties to an insurance dispute just as well as other types of disputes.

II. PURPOSE OF MEDIATION

How can mediation serve parties to an insurance dispute? Mediation is a very effective form of dispute resolution because it is quick, practical, comprehensible, confidential and usually inexpensive compared to trial.

The Texas Civil Practice & Remedies Code § 154.002 sets out the policy of the state of Texas to encourage the peaceable resolution of disputes by the use of alternative dispute resolution procedures such as mediation. “Peaceable” in the context of resolution of an insurance coverage or bad faith dispute usually doesn’t mean the same thing as “peaceable” in a family law dispute or personal injury dispute, which usually involve a higher level of emotional investment. There are less emotional considerations in a coverage or bad faith dispute. “Peaceable” in an insurance dispute is achieved when the parties come to an agreement that benefits each other, reduces the need for further litigation, which results in both cost and time benefits to everyone, but very little emotional energy. Mediation benefits the court by reducing its docket load. Mediation benefits the insured by resolving the liability claims without the cost, time and emotional resources for trial. Mediation benefits the third party claimant because he gets money more quickly from mediation than from trial. And usually the insurance company benefits from mediation because the claim no longer incurs litigation expenses and can be “closed”. Mediation is

always a plus in bad faith cases, especially where a jury in state court might be more inclined to rule against an insurance company.

III. PECULIARITIES OF INSURANCE DISPUTES

All insurance disputes are basically contract related. First party insurance disputes usually involve the insured versus the insurance company or vice versa. This can be in the context of a dispute on any type policy including commercial, residential and auto property policies, uninsured/underinsured motorist coverage, life insurance, health insurance, and even workers compensation. The dispute may involve coverage issues or contentions about value of the claim or both. Most property policies allow for an appraisal process when the dispute is limited to the value of damages. However, mediation is often less expensive and equally beneficial to the parties than the appraisal process.

Third-party liability insurance disputes are a little more complicated because they involve not only a dispute between the insured and the insurance company, but the outcome of the insurance dispute can affect the outcome of the underlying third-party claim against the insured. Recall that third-party liability insurance is designed to defend/indemnify the insured against a claim made by a third party. If there is a dispute about coverage (i.e., whether the insurer has a duty to defend and/or indemnify the insured), resolving the insurance dispute will likely spur resolution of the liability claim against the insured. On the other hand, if the insurance dispute is not resolved, the underlying liability claim is more likely to go to trial or settle with the insured paying out of pocket, resulting in subsequent litigation to resolve the coverage/bad faith dispute.

Sometimes the dispute involves multiple insurance companies battling out their respective obligations to a mutual insured. This is often seen in the context of construction defect lawsuits where one defendant is a named insured on a string of consecutive policies that may or may not have been issued by the same carrier. That same defendant is an additional insured on another string of policies issued to a third-party. The carriers may rely upon "other insurance" clauses in their respective policies to argue priority of coverage among the policies, which may be complicated by a scenario involving continuous or progressive loss that spans over multiple policy periods, potentially triggering multiple policies issue by several different insurers.

The insurers may attempt to exercise their subrogation rights. Sometimes there is a dispute among carriers about the value of the underlying case against a mutual insured. With the Texas Supreme Court ruling of *Mid-Continent v. Liberty Mutual*, 236 S.W.3d 765 (Tex. 2007), the law is not so clear what rights insurers have against other insurers. *See also Truck Ins. Exchange v. Mid Continent Cas. Co.*, Cause No. 03-08-000526, 2010 Tex. App. LEXIS 7061 (Tex.App.- Austin, August 27, 2010); *Amerisure Ins. Co. v. Navigators Ins. Co.*, 611 F.3d 299, 305 (5th Cir. 2010) (Fifth Circuit held that insurers can create contractual subrogation rights by agreement or contract, granting the right to pursue reimbursement for payment of a loss and not precluded by *Mid-Continent v. Liberty Mutual* precedence). For example, it is not clear whether the prohibition on contribution and subrogation between insurers applies when those insurers issued consecutive policies and not concurrent. Also, it may be questionable whether that prohibition applies when one party has wrongfully denied coverage. These insurance disputes involve very complex factual scenarios and legal arguments that all parties, including the mediator, must explore during the mediation process. Furthermore, a multi-party mediation may require more private caucuses to avoid sharing with other parties each offer. This may serve well to get each carrier in a multiple carrier dispute to access their exposure, without considering another's exposure, which results in a more reasonable offer.

IV. TIMING -WHEN TO MEDIATE

Mediating insurance disputes can be effective at any time from "pre-suit" through the appeal. The most common benefit of mediation is cost-savings. However, all sides need to have enough information to properly evaluate their position. It is often not feasible in an insurance dispute to mediate a case pre-suit as the parties have not engaged in meaningful discovery, which is necessary for a successful mediation. Case preparation and development must be completed to the point that the parties have a good grasp of the risk and benefits of not resolving their dispute. Early mediation has greatly improved chances of success, if damages do not justify the expense of protracted litigation, or liability is clearly established, especially in cases where damages may be statutorily capped. Even when liability is fairly clear, because insurance is involved it may still take time to properly process the matter through the appropriate channels and obtain the necessary authority to have a meaningful mediation. It is important that the parties have everything they need to make a well-informed decision at mediation.

V. SELECTING THE MEDIATOR

The first and most important consideration in mediating an insurance bad faith and/or coverage dispute is choosing the right mediator. Insurance disputes involve very specific and often complicated scenarios and complex legal issues. For this reason, choosing the mediator is highly important to the success of mediating the insurance dispute. The mediator must understand the legal issues, the complexities and purposes of different types of insurance coverage, and the potential variances among jurisdictions in interpreting the policy language. This is necessary to help the parties understand the strengths and weakness of their positions in a case.

The mediator must be impartial. According to Texas Civil Practice & Remedies Code § 154.023, mediation is:

> "a forum in which an impartial persona facilitates communication" and "may not impose his own judgment on the issues".

Texas Civil Practice & Remedies Code requires that the mediator be an "impartial person" who facilitates communication among the parties. The mediator may not impose his own judgment of the issues. The good mediator facilitates communication among the parties, which should serve to facilitate a peaceable resolution. Still, the mediator involved in an insurance dispute must be knowledgeable and understand the insurance law. With such knowledge and expertise, the insurance mediator can serve the parties not only in communication, but also in expounding the range of options for resolving the dispute. An insurance dispute will best be served by a mediator who can address the factual and legal issues with a clear understanding of the law.

Mediators do not control the outcome. They control the process. On this basis, an impartial mediator is more likely to better facilitate the process successfully through clear and open communication among the parties because the parties trust the mediator. .

VI. PREPARATION FOR MEDIATION

It is important that the parties and attorneys be prepared for any mediation conference. A poorly prepared lawyer can hurt his or her position with both the opposing side, as well as their own client, if the necessary time to prepare is not dedicated before the actual mediation. The assumption may be that if one is not prepared for mediation, he or she is not taking the case seriously, or will not be prepared for other important matters in the handling of the lawsuit. If the client is not properly prepared for the process they may develop unrealistic expectations or become entrenched in an unrealistic position.

The exchange of documents and other information before mediation is imperative to a successful outcome. Expert reports need to be properly considered when evaluating positions

and obtaining the necessary authority to resolve claims. Not knowing the amount of any potential liens and/or damages can also greatly hamper the chance of resolving a case at mediation. Defendants and adjusters need to know the amount of any potential Medicare/Medicaid lien to insure they are protected. Plaintiffs need to investigate and share this information so the defendants can realistically access the settlement range and make sure everyone is totally protected, if a resolution is to be reached.

Take the time to educate the mediator. Providing meaningful information before the actual mediation will better prepare him or her to do their job. Expert reports and selected documents such as insurance policies and other attachments are a quick and easy way to get the disputed issues in front of the mediator. Most good mediators don't have the time to read complete depositions, but they will spend the time reading specific information about the facts in dispute. Also, the parties should educate the mediator about the particular legal issues and the state of the law relevant to each particular issue. A mediation position statement that outlines the legal arguments and the supporting law is a useful tool to educate the mediator in an insurance dispute.

Mediation is often an effective form of discovery. It is not a good forum to pry secrets out of an opposing party, but it is an excellent place to ask questions. For example, in a construction defect case, the insurance parties may be able to isolate the defense attorneys and get information about dates of damages based upon dates of construction, completion, sell of the property, types of alleged damages, other available insurance such as additional insured coverage for each of the parties, etc. Therefore, utilize the time spent at mediation to help isolate the stronger coverage defenses from the weak defenses and help the parties see the value of each position. In order to do this, the parties should know in advance of mediation what facts need further exploration.

VII. CONFIDENTIALITY

There are three bases for mediation confidentiality. Texas Rules of Evidence 408 (Rule 408), and Texas Civil Practice & Remedies Code, §§154.053(b) and (c) and 154.073.

A. Rule 408:

This rule provides only limited protection, since it only forbids admission into evidence of "conduct or statements made in compromise negotiations." However, statements may be admissible in evidence to prove other relevant issues.

B. Civil Practice and Remedies Code 154.053(b) provides:

> Unless expressly authorized by the disclosing party, the impartial third party may not disclose to either party information given in confidence by the other and shall at all times maintain confidentiality with respect to communications relating to the subject matter of the dispute.

This provision prohibits a mediator or any other person that facilitates an alternative dispute resolution procedure from disclosing information to any other party that was given in confidence. In fact, the mediator is required to maintain confidentiality at all times.

C. Civil Practice and Remedies Code 154.053(c) provides:

> Unless the parties agree otherwise, all matters including the conduct and demeanor of the parties and their counsel during the settlement process, are confidential and may never disclosed to anyone, including the appointed court.

Confidentiality is of utmost importance, so much so that even the conduct and demeanor of the parties and their counsel at mediation is confidential. The mediator is prohibited from sharing any information about the mediation to anyone, including the appointed court.

Note that 154.053(c) has no language addressing situations where non-parties have a legitimate reason for attending mediation. Examples include, family members and structure settlement brokers, etc. If a settlement is reached and confidentiality is one of the conditions, how do you bind a non-party to confidentiality? This is best addressed before the mediation begins, with the observing party agreeing in writing to confidentiality before he or she is allowed to observe, and with the further understanding they will not interject their views or opinions.

D. Civil Practice and Remedies Code 154.073 provides in part:

> (a) Except as provided by Subsections (c), (d), (e) and (f), a communication relating to the subject matter of any civil or criminal dispute made by a participant in an alternative dispute resolution procedure, whether before or after the institution of formal judicial proceedings, is confidential, is not subject to disclosure, and may not be used as evidence against the participant in any judicial or administrative proceeding.
>
> (b) Any record made at an alternative dispute resolution procedure is confidential, and the participants or the third party facilitating the procedure may not be required to testify in any proceedings relating to or arising out of the matter in dispute or be subject to process requiring disclosure of confidential information or data relating to or arising out of the matter in dispute.
>
> (c) Any oral communication or written material used in or made a part of an alternative dispute resolution procedure is admissible or discoverable if it is admissible or discoverable independent of the procedure.

The confidential requirement and nature of alternative dispute resolution proceedings makes mediation an inviting and safe forum for all parties. Section 154.073 clearly mandates that all communications, recordings, written materials made at a mediation are confidential. However, section 154.053(b) suggests that even post-mediation communications, such as those made in furtherance of settlement negotiations are confidential because they are "communications relating to the subject matter of the dispute."

With these governing statutes in mind, mediators advocate protecting confidentiality, by reemphasizing the need for confidentiality when sensitive information is discussed with the mediator.

VIII. STRATEGIES

A. Opening Session

The opening caucus is an important and necessary part of the process for all parties and the mediator. The mediator can establish trust, communication and a constructive atmosphere. The mediator also defines and clarifies expectations of the parties, as well as going through the ground rules and procedures. Obviously, if there is high animosity or other extenuating circumstances it may be best to forgo this part of the process. However, this is the time the parties can show the opposing side the seriousness of the matter at hand, make all necessary and compelling legal arguments, and demonstrate any intent to continue forward with the litigation if an acceptable compromise cannot be reached.

Remember that the decision makers are sizing up opposing counsel and his/her client based on preparedness, ability to present the case, and how the parties present themselves. If the attorney does not put on a good presentation, the other side may discount his/her ability and resolve to continue forward with the litigation. Hearing supportive testimony of key witnesses that may have been under appreciated by the opposing side can help open the lines of communication, and may impact the ultimate resolution. Remember, the decision maker was probably not at the deposition. This is an opportunity to remind him or her of what key witnesses have said. Threats and verbal assaults tend to be polarizing to the parties, and are not productive. Avoid giving the opposing side a reason to get mad.

B. Negotiations

The attorney, client, and mediator must have a grasp of the facts, legal issues and damages. The attorney must be able to articulate a reasonable expectation of a jury verdict, including chances of success. Obviously there are numerous negotiation styles and strategies that are used in mediation. Parties should be prepared for "testing the water", where both plaintiffs and defendants make demands and offers that are in response to what they anticipate or what they hear dollar wise rather than a true evaluation of risk. This simply has to be worked through with the help of the mediator. If both sides trust the mediator he or she can help the parties get into the range where the real risk is appreciated by both sides. The mediator advocates not making demands shortly before mediation. If no meaningful talks have already taken place wait until after the opening session to convey numbers through the mediator. If attorneys fall into a pattern of negotiating the same way every time the opponent will remember for future cases. Be flexible and adapt to the situation.

Be careful of what is said, and how it is said. It is amazing how many people on both sides of the docket try to read messages into comments like " We'll never take X" or " We'll never pay X". These comments can be detrimental to resolving a case. If attorneys make comments before mediation to opposing counsel they will assume that the decision maker will follow the advice of its attorney. If you don't know it for sure, don't say it.

Don't fall into a pattern of negotiation style. When attorneys and adjusters get into a patent of negotiating a certain way, it tends to hurt the chances of early resolution in future cases. Be flexible and willing to adapt to the scenario presented. See Texas Bar Online CLE; #000093819 Gaining the Edge! Latz: Five Golden Rules of Negotiation Part 3 (excellent one hour ethics course to help refine negotiation styles).

A good mediator will be creative. If he understands the issues he can present various options to the parties that would resolve some of the issues, if not all. The goal is to work on the problem, not on the people. This is especially effective in an insurance dispute involving complicated legal issues.

The mediator in an insurance dispute should encourage the parties to identify the coverage issues, down to the particular language of each provision that is at issue. He/she will ask the parties to deconstruct, analyze and reconstruct the issues. The mediator will invite the parties to present the legal authority upon which they rely for their propositions. The mediator should know the law so that he/she can pinpoint the strengths and weaknesses of each argument, which ultimately leads to concessions on the value of each position. The mediator should ask questions about the factual circumstances. By the end of a well prepared and fully contested insurance mediation, the parties should know more about insurance law than before the mediation. Through this process, mediation is successful when it reduces the litigation time and expense by helping the parties isolate the true issues and discard the irrelevant and minor issues.

IX. MEDIATION IMPASSE/RECESS

Mediation is an evolving process. Litigants seem to be more skeptical that mediation will result in a settlement than they did a few years ago. Many cases that do not resolve at mediation do ultimately resolve prior to trial. Mediation opens communications. Once the settlement range is defined at mediation one or both sides often rethink their position and remain willing to negotiate further. This is the perfect opportunity to use the mediator to continue to work the matter toward a resolution. Mediators should be receptive to staying involved without the need for a second mediation.

X. CONSIDER EMOTIONS

After the current case concludes the lawyers will move on to the next case, but not the client. Be aware of how the client is dealing with the litigation, and whether emotionally it is in their best interest to continue past mediation and go through a trial. Also make the mediator aware if these issues exist, so he or she can help reduce the stress for the client. Evaluate if there is any chance for the parties to have future communications, such as unrelated claims under the same insurance policy, or continued business relationships between insureds and third party claimants and/or insureds and their insurance companies. If the potential is there, extra care needs to be taken in an attempt to minimize bad feelings and maximize healthy future relations. Let the parties get closure if at all possible.

XI. CONCLUSION

Mediation serves as a valuable tool assisting in the resolution of all disputes. Utilize the mediator before, during and after the mediation. Having a mediator that is knowledgeable, and that all parties trust is a large part of having a successful mediation. Remember the mediator knows what is going on with the other parties, and is in the best position to know how to best move a case toward final resolution.