



Intervention Denied to Seek Special Verdicts or Jury Interrogatories

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In *Ex parte Builders Mut. Ins. Co.*, No. 2019-000238, 2020 WL 2464838 (S.C. May 13, 2020), *reh'g granted* (Aug. 12, 2020), *opinion withdrawn and superseded on reh'g*, No. 2019-000238, 2020 WL 4672541 (S.C. Aug. 12, 2020) insurers were denied the right to intervene in a construction defect lawsuit for the purpose of proffering a special verdict form or special interrogatories to go with a general verdict form. The purpose of the proposed special verdict or jury interrogatories was to determine which construction defect damages were covered by the applicable commercial general liability insurance policies. The Supreme Court held that the insurers were not entitled to intervene as a matter of right, and the trial court did not abuse its discretion in denying permissive intervention.

Palmetto Pointe is a condominium development. The property owners' association became aware of damage to the buildings. The association filed a construction defect action against the insureds (construction contractors and subcontractors) for negligence, breach of implied warranties, and unfair trade practices. The association sought actual and consequential damages to repair or replace various components of the condominiums.

The insureds were defended by independent counsel, and the insurers defended subject to a reservation of rights to later contest whether the damages were covered.

At the tail end of the discovery period, the insurers moved to intervene in the action to participate in preparing a special verdict form, or a general verdict form accompanied by interrogatories to be submitted to the jury during trial.

S.C. R. Civ. P. 24 governs intervention. Rule 24 (a) sets out the rules for intervention as a matter of right.

(a) Intervention of Right. Upon timely application anyone shall be permitted to intervene in an action: (1) when a statute confers an unconditional right to intervene; or (2) when the applicant claims an interest relating to the property or transaction which is the subject of the action and he is so situated that the disposition of the action may as a practical matter

impair or impede his ability to protect that interest, unless the applicant's interest is adequately represented by existing parties.

As to intervention as a matter of right, under South Carolina case law, the proposed intervenor must (1) establish timely application; (2) assert an interest relating to the property or transaction which is the subject of the action; (3) demonstrate that it is in a position such that without intervention, disposition of the action may impair or impede its ability to protect that interest; and (4) demonstrate that its interest is inadequately represented by other parties. The second element of this test under South Carolina law requires that the party must have an interest with "constitutional standing" in that the intervenor must be a "real party in interest." A real party in interest is one with a real, actual, material or substantial interest in the subject matter of the action, to be distinguished by one who has only a nominal, formal or technical interest in, or in connection with, the action. The interest must be direct, immediate and significantly protectable, rather than remote or contingent. The court held that the insurers were not "real parties in interest" in the construction defect action, and thus did not satisfy the four-part test.

The court cited several other decisions addressing the intervention as of right issue. In *Restor-A-Dent Dental Labs., Inc. v. Certified Alloy Prod., Inc.*, 725 F.2d 871, 872 (2d Cir. 1984) the court denied an insurer's motion to intervene in a products liability action against its insured. The stated purpose of intervention was to propose interrogatories to the court for submission to the jury in the event that the jury returns a verdict for the insured. In that matter, the insurer was defending the insured under a reservation of rights that it had no duty to indemnify certain "intangible losses" which the insurer claimed were the bulk of the damages. The insurer argued that without the interrogatories, it would be extremely difficult, if not impossible, to determine what items the jury awarded were covered and uncovered. While the insured took the position the interrogatories might be proper, the plaintiff opposed them. The court focused on the "interest" requirement. The interest must be "significantly protectable," and it must be "direct," as opposed to "remote" or "contingent." The insurer did not have an interest in the subject matter of the action, the alleged delivery of defective alloy to a producer of dental products. Its only interest was in how much it would have to pay. Also, its interest depended on two contingencies: first a jury verdict for plaintiff; second a finding in future coverage litigation about the insurer's liability to the insured.

In *Davila v. Arlasky*, 141 F.R.D. 68, 69 (N.D. Ill. 1991) a patent holder sued officers and shareholders of a corporation for patent infringement and inducement to infringe. The patent holder had already obtained a default judgment against the corporation. Three insurers which had insured the corporation moved to intervene as of right under Fed. R. Civ. P. 24(a). The insurers argued that the coverage for the officers was excluded by exclusions for willful or deliberate acts, and willful violations of a penal statute. The insurers sought to intervene and obtain a declaration that they had no obligation to defend or indemnify the officers.

The court noted that the key issue was whether the insurers had an interest that may be impaired. An interest must be direct and substantial, and not remote. The court noted that some circuits flatly

deny intervention when there is any contingency. Other courts allow intervention when interests are contingent on the outcome of the litigation but not too remote.

The court categorized these cases as follows. Insurers who have paid claims are allowed to intervene in suits by the insured against the tortfeasor. The rationale was that the insurer would have a right of subrogation in whatever proceeds the plaintiff recovered and may intervene to protect that interest. But where the insurer is defending a suit on behalf of its insured (with a reservation of rights), but wants to intervene as a party to submit interrogatories to the jury, courts have denied intervention. Finally, the court categorized the case at bar as one where the insurer is not defending the insured and wants to intervene, which the court characterized as a less common scenario.

In this case the court found that a conflict existed between the insurers who would be just as happy to see willful conduct proved, and the insured, who wants any liability to be covered by the policy. In this circumstance, the insurers cannot obtain a decision on the coverage issues until after the trial in the underlying suit. Since they could resolve the coverage issue in the declaratory judgment action, there was no impairment of their interest if they are not allowed to intervene. The court denied the motion to intervene.

In *Fid. Bankers Life Ins. Co. v. Wedco, Inc.*, 102 F.R.D. 41, 43 (D. Nev. 1984) errors and omissions insurers of insurance agents and a broker sought to intervene, among other things, to propose special interrogatories and verdicts. The purpose of knowing the jury's bases for any verdicts would be to make possible a division of the money damages between covered and non-covered acts of the insureds. The agents and the broker had allegedly participated in deceiving the plaintiff life insurer – which issued six large life policies – as to the health of the insured individual – who died approximately two years after issuance. The life insurer paid on four policies, then sought restitution and rescission. The beneficiaries filed suit against the insurer and agents. Since the insurers were defending under a reservation of rights, the court found that the disposition of the action would not impair or impede their ability to protect themselves from having to indemnify their insureds for acts excluded from the coverage. The court denied intervention as a matter of right. That court did, however, allow for permissive intervention.

S.C. R. Civ. P. 24 sets forth the rule for permissive intervention:

(b) Permissive Intervention. Upon timely application anyone may be permitted to intervene in an action: (1) when a statute confers a conditional right to intervene; or (2) when an applicant's claim or defense and the main action have a question of law or fact in common.
* * * In exercising its discretion the court shall consider whether the intervention will unduly delay or prejudice the adjudication of the rights of the original parties.

Under South Carolina law a party seeking permissive intervention must (1) establish timely application; (2) assert a claim or defense that has a question of law or fact in common with the underlying action; and (3) prove its participation in the underlying action will not delay or

prejudice the adjudication of the rights of the original parties. The court affirmed denial of permissive intervention. The court noted that there were facts in the record showing that intervention would “(1) unnecessarily complicate the construction defect action, including altering the Association’s burden of proof and possibly delaying the trial, and (2) create a conflict of interest for the Insureds’ counsel, who were supplied to them by the Insurers.”

As to “complication,” the association need not categorize its damages absent this proposed intervention. It could simply seek a general verdict. The proposed verdict form or jury interrogatories would impose on the association the burden to categorize its damages. Further, the association argued, it had conducted three years of discovery, asking questions without this burden to categorize in mind.

In a follow-on declaratory judgment action, the insureds and insurers have the “collective burden” to show which parts of a general verdict are covered. The insured must prove that a loss is covered, and once that is done the insurer must prove that exclusion applies. An insured has the burden to prove that an exception to an exclusion restores coverage.

As to the “conflict of interest” issue, the court noted that attorneys asserted that verdict form with special interrogatories would put defense counsel in an untenable position of essentially conceding liability to focus on damages. And they asserted that defense counsel would have to push as much of the damages into “covered, consequential damages (e.g. water intrusion *resulting from faulty workmanship*), thereby conceding” faulty workmanship.

The court concluded that the record supported the trial court’s determination that permissive intervention would present conflict of interest concerns and likely cause undue delay and prejudice to the association and the insurers.

The insurers argued that intervention was mandated by *Auto Owners Ins. Co. v. Newman and Harleysville Group Ins. v. Heritage Communities, Inc.* The court limited the holding in the former case. It concerned an arbitration award in a construction defect case. In a subsequent coverage lawsuit, the court had found that there were covered and uncovered damages, but refused to review or parse the award because such awards are generally conclusive. The Supreme Court modified *Newman* to allow a subsequent declaratory relief action to resolve the coverage dispute. *Harleysville* concerned a coverage action about a construction defect lawsuit. The Special Referee ordered the insurer to pay the entire verdict – covered and uncovered damages – because it would be “improper and purely speculative” to allocate covered and uncovered damages. Alternatively, the court found that the insurer should pay because of an inadequate reservation of rights letter that impliedly waived the right to contest coverage. It was only on the latter point that the Supreme Court affirmed. The Supreme Court here states that *Harleysville* does not mandate intervention, nor does it foreclose a declaratory judgment action to resolve coverage disputes.

Finally, the court addressed the insurers’ concern that they not be bound by factual determinations in the construction defect lawsuit. Under South Carolina law the insurer with notice of a lawsuit

and an opportunity to defend is bound by material facts established against the insured. However, this rule does not apply where the insurer defends under reservation of rights.

There is a conflict of interest between the insurers and insureds as to what portions of damages are covered or not. The insurers and insured are not precluded from introducing evidence as to which damages are covered or not. The parties are only bound by the total amount of the jury verdict in the underlying construction defect lawsuit.

Given these constraints, the court first noted that the parties can agreed to a framework for allocation subject to court approval. If that does not happen, the court set out a default framework. The primary source of evidence should be the transcript of the trial or other merits hearing. Additional evidence may be presented relevant to the coverage issue such as expert testimony. But this additional evidence must be narrowly tailored. The trier of fact must then make a determination allocating on a percentage basis what portion of the verdict is covered damages and what portion is non-covered damages. Perfect precision is not always attainable. Where not attainable a “fair approximation” must be made.

Insurers here were denied the right to intervene as of right or permissively. But they were permitted to argue allocation of covered and uncovered damages in a subsequent declaratory judgment action. If the law in a jurisdiction is unclear an insurer should consider the value of filing a motion to intervene. Sometimes courts will hold that failure against the insurer – that it had a chance to parse the verdict by way of a motion to intervene and it cannot try to do so after the fact.

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