***CUMIS* RATES: WHEN DO THEY APPLY?**

Are insurers always entitled to rely upon the *Cumis* statute's rate cap when paying for an insured's independent counsel? As discussed below, depending upon how a particular policy is worded, the answer may be "No."

1. The *Cumis* Statute

By way of brief background, California Civil Code § 2860 (the *Cumis* statute) was enacted by the California Legislature in 1987, and codified the California Court of Appeal's earlier landmark decision in *San Diego Navy Federal Credit Union v. Cumis Ins. Society, Inc.*, 162 Cal. App. 3d 358 (1984). The statute protects an insured against conflicts of interest that may arise when an insurer conducts the insured's defense under a reservation of rights.

The statute provides that if a policy imposes a "duty to defend" upon an insurer, and the insurer reserves its rights on a coverage issue that could be controlled by its panel counsel, the insurer is required to provide the insured with "independent counsel." *See* § 2860 (a) and (b). The statute further provides, at subsection (c), that the insurer's obligation to pay fees to the insured's independent counsel is limited to those hourly rates the insurer pays its panel counsel to defend similar actions. These rates are often referred to as "panel rates."

Importantly, subsection (c)'s rate cap includes an often-overlooked qualifier. It provides that the rate limitation provision does "not invalidate other *different or additional* policy provisions pertaining to attorney's fees . . . ." (Italics added.)

2. The *Cumis* Statute Only Applies To Insurers That Have A "Duty To Defend"

Not all liability policies impose on the insurer a "duty to defend." For example, many Directors & Officers policies only require the insurer to advance or reimburse the insured's defense expenses, while the insured assumes responsibility for selecting its own counsel and controlling its own defense. *See, e.g.*, *National Union Fire Ins. Co. of Pittsburgh, PA v. Stiles Professional Law Corporation*, 235 Cal. App. 3d 1718, 1727 (1991) (noting that "the insurance policy principally obligated [the insurer] to reimburse the insured for the costs of the defense.").

Because the *Cumis* statute expressly applies only if an insurance policy imposes a "duty to defend" upon the insurer, it follows that the statute's rate cap

has no application to a policy that only requires an insurer to advance or reimburse defense expenses. Under such a policy, absent language to the contrary, an insurer's obligation to advance or reimburse its insured's defense costs should be limited only by common law requirements that fees be reasonable.

3. The *Cumis* Statute's Rate Cap May Not Apply Where A Policy Defines "Defense Expenses"

As noted, the *Cumis* statute's rate cap states that it does "not invalidate other *different or additional* policy provisions pertaining to attorney's fees . . . ." (Italics added.) Thus, where they conflict, an express provision of a policy pertaining to the payment of attorney fees should override the statutory rate provision.

While Commercial General Liability policies typically contain no provision pertaining to the attorney fees payable by the insurer, there are other policies that do include such a provision. For example, some Directors & Officers, Errors & Omissions and Employment Practices Liability policies expressly define the fees and expenses an insurer will pay in discharging its duty to defend. Frequently, such policies will define "Defense Expenses" to mean *"reasonable and necessary"* legal fees and expenses.

There would seem to be a clear difference between a promise made in a policy to pay *"reasonable and necessary"* fees, and a statutory provision that narrowly limits an insurer's obligation to pay only panel rates to an insured's independent counsel. The policy provision reflects an objective measure of reasonableness, *i.e.*, market rates. *See PLCM Group v. Drexler*, 22 Cal. 4th 1084, 1095 (2000) ("Reasonable rates" are rates "prevailing in the community for similar work"). The statutory provision, in contrast, reflects a subjective measure based upon the insurer's experience in negotiating rates with its panel defense counsel. *See Foxfire, Inc. v. New Hampshire Ins. Co.*, 91 2940 (N.D. Cal. July 1, 1994) (distinguishing between "marketplace rates" and "those [an insurer] can negotiate by reason of its position").

Accordingly, a policy provision requiring payment of *"reasonable and necessary"* fees should be considered a *"different or additional"* provision that controls over the statutory rate cap. *See generally Compulink Management Center, Inc. v. St. Paul Fire & Marine Ins. Co.*, 169 Cal. App. 4th 289, 301 (2008) (noting that a policy's promise to pay "reasonable expenses" was "an additional policy provision," albeit not one pertaining to fees).

In summary, when confronted with an insurer's attempt to apply the *Cumis* statute's rate cap, an insured is well advised to review the precise terms of its liability policy, and answer the following two questions. First, does the policy impose on the insurer a "duty to defend"? If not, then the *Cumis* statute, including its rate cap, does not apply. And second, does the policy include any *"different or additional"* provision pertaining to the payment of attorney fees? If so, then such a provision may control over the *Cumis* statute's rate cap.