
Counsel Fees In Declaratory Judgment Actions: Clearly Complicated? Nah!
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Declaratory judgment actions are brought by a party to determine the obligations of an insurance company. While the insurance company and the insured basically have the unlimited right to bring these actions, the right is also granted to entities that are strangers to the insurance policy in certain limited circumstances. There are some general rules that provide guidance in determining when an insurance company is obligated to pay counsel fees to another party.

Counsel fees to a non-insured.

An insurance company, unless possibly liable for a violation of General Business Law § 349, or when found to have acted in bad faith, will not be obligated to pay the counsel fees of a non-insured which is involved in coverage litigation. This is the rule regardless of whether the insurance company or anyone else brought the action on coverage.

When the insurance company prevails.

If no coverage obligation is owed, then the insurance company need not worry about paying anything but its own counsel fees. This again is the rule regardless of whether the insurance company or anyone else brought the action on coverage (*see U.S. Underwriters Ins. Co. v City Club Hotel, LLC*, 3 NY3d 592 [2004]).

When coverage is owed and the insurance company brought the action.

The insurance company is obligated to pay the legal fees of the insured. The reasoning behind this rule is that the insured was cast in a defensive posture by the conduct of the insurance company and the insurance policy is obligated to pay for the representation of the insured in such circumstances (*U.S. Underwriters Ins. Co.*, 3 NY3d at 596; *see Mighty Midgets, Inc. v Centennial Ins. Co.*, 47 NY2d 12, 21[1979]; *U.S. Fid. & Guar. Co. v New York, Susquehanna & W. Ry. Corp.*, 277 AD2d 1026, 1026 [4th Dept 2000]; *Chase Manhattan Bank v Each Individual Underwriter Bound to Lloyd's Policy No. 790/004A89005*, 258 AD2d 1, 5 [1st Dept 1999]).

But suppose the insured, in addition to reacting to the affirmative steps taken by the insurance company, takes affirmative steps of its own, such as asserting a counter-claim for coverage? We have not found a case that separates out these fees and finds them to be non reimbursable. But why should they be reimbursable? After all, isn't the assertion of a counterclaim simply a functional complaint? (*National Grange Mut. Ins. Co. v T.C. Concrete Constr., Inc.*, 43 AD3d 1321 [4th Dept 2007]; *see e.g. U.S. Underwriters Ins. Co.*, 3 NY3d at 597, quoting *Mighty Midgets*, 47 NY2d at 21; *see also U.S. Fid. & Guar. Co.*, 277 AD2d at 1026-1027)).

When coverage is owed and a claimant brought the action.

Here, the question hinges on the role of the legal services. If the insured asserted a cross-claim against the insurance company then those fees are not recoverable. If, however, the insured incurred counsel fees in defending against the action brought by the claimant, or against cross-claims asserted against it by the insurance company, then the insurance company must reimburse the insured for those fees (*see Johnson v General Mut. Ins. Co.*, 24 NY2d 42, 46 [1969]).

When coverage is owed and the insured brought the action.

The law is clear that the insured cannot recover for the affirmative action it took to secure coverage (*see Mighty Midgets*, 47 NY2d at 21-22; *Hedaya Home Fashions, Inc. v American Motorists Ins. Co.*, 12 AD3d 639, 640-641 [2d Dept 2004], *lv denied* 4 NY3d 708). This rule applies even if the insured is successful in its attempt to compel its insurance company to comply with the duty to defend and indemnify under the policy (*see Mighty Midgets*, 47 NY2d at 21; *Kramarik v Travelers*, 25 AD3d 960, 963 [3d Dept 2006]).

But what about the fees incurred by defending against affirmative steps taken by the insurance company? We see no reason why the reimbursement of these fees should be treated any differently than the reimbursement of fees incurred by the insured in defending against affirmative steps taken by the insurance company, when the action was commenced by a claimant. Take, for example, a case where the insurance company appeals an award of summary judgment to an insured in a case brought by the insured. But for the appeal, the case is over. From the perspective of the insured, the case is over once it was awarded summary judgment. Although the application of superficial criteria (who is the plaintiff) might be an easy and attractive way to resolve this question, such an approach lacks logical merit (*see City of New York v Zurich-American Ins. Group*, 27 AD3d 609 [2d Dept 2006]; *Hurney v Mattson*, 59 AD2d 934 [2d Dept 1977]).

Conclusion.

Although the law appears to apply clear cut rules to answer the question of payment of counsel fees, precedent from the Court of Appeals and the Appellate Divisions indicate that a deeper evaluation is needed. The key issue is what were the services attempting to accomplish? To the extent that the insured is seeking affirmative relief then the insured should not be able to prevail. Where, however, the insured is responding to affirmative steps by the insurance company, the insurance company faces the risk of having to pay the counsel fees incurred by the insured for those particular services.