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Lawyer Insights

Risky Business: Insuring Damage Awards through Judgment Preservation Insurance

By Jae Lynn Huckaba, Patrick M. McDermott and Geoffrey B. Fehling
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INTRODUCTION

A federal court recently ordered a law firm to disclose a judgment preservation insurance ("JPI") policy it obtained to protect a $185 million fee award pending appeal.[1] The plaintiffs' law firm received the fee award in its representation of two classes of health plan insurers, who alleged that the federal government did not compensate the insurers for losses incurred in their participation in the Affordable Care Act's insurance marketplace. While the case was on appeal, the plaintiffs' firm accepted a distribution of funds from the claims administrator for the full $185 million fee award.[2]

On appeal, the U.S. Court of Appeals for the Federal Circuit vacated the $185 million fee award because it found that the district court did not properly conduct a lodestar cross-check against the fee requests.[3] The appellate court remanded, instructing the district court to conduct a lodestar cross-check, including assessing whether there was sufficient justification for an implicit fee multiplier.[4] On remand, the plaintiffs' firm filed a renewed motion for attorneys' fees, and the government filed motions requesting an accounting and safekeeping of the distributed fee award and authorization to obtain additional discovery into the law firm's purchase of a JPI policy.[5]

The Court of Federal Claims denied the government's request for an accounting and safekeeping of the distributed funds, but it ordered disclosure of the JPI policy.[6] In compelling disclosure of the policy, the Court said it was erring on the side of requiring transparency, citing its fiduciary duty to protect the interests of the class in assessing reasonable fees. It explained that "[t]he JPI's terms may be relevant to the Court's task on remand if the policy provisions are inconsistent with the Court's objective 'to ensure an overall fee that is fair for counsel and equitable within the class.'"[7] Thus, the Court permitted discovery surrounding the "terms and circumstances" of the JPI policy. The Court limited the permitted discovery, however, to only the JPI policy documents.[8] The Court rejected requests for discovery into the law firm's communications with the insurer or the insurer's financial stability.[9]

This recent ruling may provide one of the first looks into how the terms of a JPI policy can be taken into account by a court when deciding a plaintiff's recovery. So-called nuclear verdicts are becoming more and more common.[10] With verdict amounts increasing, insurers have capitalized on the market, finding ways to insure the risks associated with large judgments, and more companies have purchased JPI to secure larger judgment awards. And, as the median verdict continues to increase, JPI policies will likely continue to grow in popularity. Businesses who wish to purchase JPI should evaluate the pros and cons of such policies and consider how JPI may otherwise affect the pending litigation.

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JUDGMENT PRESERVATION INSURANCE

JPI is a type of litigation risk insurance designed to protect the holder of a legal award against the risk of the award being overturned or reduced on appeal. JPI policies typically are customized to address the policyholder's distinct coverage needs, including the specific risks associated with the litigation. JPI can be used to protect a variety of awards, including summary judgment awards, trial court verdicts, and arbitration awards.

The coverage afforded by JPI allows a plaintiff who wins a significant judgment to secure some—or sometimes, all—of an award pending an appeal or other subsequent proceedings. With any damage award, there is always a risk—even if it is minimal—that the appellate court will reverse or reduce the award entered by the trial court. JPI may help mitigate the risks associated with a reversal or reduction of the award on appeal.

At times, JPI is used in conjunction with litigation funding. For example, a litigation funder may advance the costs of litigating an appeal in exchange for a portion of the plaintiff's recovery. Securing a JPI policy as part of that negotiation may enable the plaintiff to sell a litigation funder some of the interest in the award amount for a more favorable rate because of the mitigated appellate risk. In some cases, the litigation funder may even procure its own JPI policy after investing in the litigation, which protects the investment against the risk of reversal or a reduction of the award on appeal. A litigation funder may also require the plaintiff to procure JPI coverage to secure funding.

PROS AND CONS OF JPI

As with most insurance products, there is no one-size-fits-all approach; the viability of JPI as an appropriate risk mitigation tool depends heavily on a variety of factors, including the specifics of the underlying claim and judgment, potential policy wording, and the dynamics of the parties involved. We discuss some of those factors and the benefits and drawbacks of JPI below.

There are a number of benefits to securing a JPI policy. The most obvious benefit is that JPI guarantees that a prevailing party will recover at least an agreed-upon amount of a judgment or award, regardless of the outcome on appeal or in other subsequent proceedings. In other words, JPI protects against the uncertainty of appeals and permits recovery of at least some of the trial court judgment even if that judgment is reversed or subject to a reduction as a result of post-trial motion practice, an appeal, or trial court proceedings after any remand.

JPI also can alleviate the uncertainty of litigation, especially for plaintiffs with lesser financial means than their opposition. After months—and sometimes years—of litigation, plaintiffs may lack the resources to continue to litigate their case through a prolonged appeals process. A plaintiff with JPI, however, has the guarantee of at least a partial recovery from the litigation, which gives the corporation the financial security to continue litigating through an appeal. Such financial security can be created, in part, if the company is able to use the JPI to recognize judgment-related earnings in their financial statements, knowing that an agreed-upon portion of the judgment is secured under their policy. This financial security may help reduce the burdens of litigation, and in turn, allow the plaintiff to continue to fight for a final, enforceable judgment in its favor. It may also increase the plaintiff's bargaining power in settlement negotiations.

Another benefit of JPI is that the policies often are not riddled with exclusions. In fact, JPI policies often have only one exclusion—the fraud and misrepresentation exclusion. The fraud and misrepresentation exclusion may negate coverage where the policyholder misrepresents facts during the underwriting process. This exclusion is normally quite narrow, requiring proof of actual knowledge of facts that the policyholder deliberately misrepresented. Some policy forms even require the insurer to prove by "clear and convincing evidence" that a misrepresentation was made and prejudiced the insurer, which is a high burden of proof for the insurer. Thus, if an insurer has grounds to exclude coverage at all under a JPI policy, it usually requires the insurer to clear a significant hurdle before the exclusion applies to eliminate coverage for the insured risk.

But JPI does not protect plaintiffs against all risks of litigation. Unlike many types of policies, a JPI policy typically does not cover attorneys' fees or costs associated with an appeal. Policyholders, however, may be able to bargain for these coverages, as JPI policies are tailored to the policyholder's unique coverage needs. The policyholder may, for example, advocate for defense cost coverage in exchange for a higher self-insured retention. But JPI generally does not cover shortfalls due to settlement, and thus, it usually does not provide coverage where the plaintiff settles for less than the full value of the trial court's judgment prior to a final nonappealable judgment, unless the insurer consents to the settlement.

JPI also typically does not insure the collectability of the judgment. In some situations, a judgment may be affirmed on appeal, but the plaintiff is unable to collect the judgment because the defendant is judgment proof. A defendant may be judgment proof if, for example, its assets are exempt from debt collection and a creditor cannot pursue the defendant's income. JPI normally does not protect against this risk.

OTHER CONSIDERATIONS FOR MITIGATING RISKS IN LITIGATION

Corporations should also contemplate other consequences of using JPI to insure a judgment award. As the recent federal decision discussed above shows, an opposing party may try to use the terms of a JPI policy to reduce their liability. Particularly in the fee context, a defendant might attempt to use the JPI policy as evidence relevant to the court's determination of a reasonable fee award.

Under a JPI policy, the insurer may also be able to prevent settlement or substitution of counsel without first obtaining the insurer's consent. In addition to consent obligations, some JPI policies require the plaintiff to vigorously litigate the appeal. Likewise, a JPI insurer may require the plaintiff to maintain the same counsel that successfully litigated the matter before the trial court throughout an appeal and other subsequent proceedings. The terms of the JPI policy may also require the policyholder and its counsel to cooperate with the insurers in the appeal process. Consequently, depending on the policy terms, the policyholder may risk losing total control of the litigation.

CONCLUSION

Litigation risk insurance, such as JPI, can protect against the uncertainty of the appellate process. But removing that uncertainty comes with certain drawbacks. As shown by the recent decision from the Court of Federal Claims, some courts may compel disclosure of the JPI policy, especially where the case is remanded to the trial court for reevaluation of the damage award. JPI policies may also shift some control of the litigation from the policyholder to the insurer. Companies considering JPI to insure a damage award should consult with coverage counsel to navigate these hurdles and to assist in negotiating and placing customized policies specifically tailored to the unique risks of their case.

Notes

1. Health Republic Ins. Co. v. United States, No. 16-259, 2024 WL 339977, at 7–8 (Fed. Cl. Jan. 30, 2024).

2. *Id.* at 2.

3. Health Republic Ins. Co. v. United States, 58 F.4th 1365, 1373, 1377 (Fed. Cir. 2023).

4. *Id.* at 1378.

5. Health Republic Ins. Co., 2024 WL 339977, at 2.

6. *Id.* at 8.

7. *Id.* at 7 (citing Fed. R. Civ. P. 23(h)).

8. *Id.* at 7.

9. *Id.*

10. From 2010 to 2019, so-called nuclear verdicts of greater than $10 million have grown in size (with median verdicts experiencing a 27.5 percent increase during that time period) and frequency. *See* Cary Silverman & Christopher E. Appel, *Nuclear Verdicts Trends, Causes, and Solutions*, U.S. CHAMBER OF COM. INST. FOR LEGAL REFORM (Sept. 2022).

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