



ILLINOIS STATE
BAR ASSOCIATION

THE POLICY

The newsletter of the ISBA's Section on Insurance Law

In this issue

The Insurance Section of the Illinois State Bar Association typically reviews the majority of insurance decisions announced by Illinois courts. There are five co-editors of *The Policy* who work tirelessly on these case summaries and never fail to meet a deadline. Their names appear on the back of this issue. I would like to thank them for their hard work. This issue gives them a well-earned break

for a moment.

The Illinois Supreme Court issued an interesting opinion regarding the faxing activity of an insured and the Illinois Appellate Court issued two decisions in the long string of Targeted Tender cases. This issue address these cases in depth. The next issue of *The Policy* will again bring you the latest in Illinois opinion. As we approach the new year for the ISBA, (June) I encourage all inter-

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ested readers to consider joining the Insurance Section and if you have an idea for an article or would like to work on *The Policy*, please do not hesitate to contact the Chair. Thank you. David Roe.

The Illinois Supreme Court holds that fax blasting may be potentially covered under a commercial liability policy

In *Valley Forge Ins. Co. v. Swiderski Electronics, Inc.*, 2006 WL 3491675 (Ill. 2006), the Illinois Supreme Court held that allegations against an insured for unsolicited faxes potentially fell within the insured's

commercial general liability "advertising injury" coverage as a "publication," and "material that violates a person's right of privacy." The "right of privacy" in the "advertising injury" provision connoted both an interest in seclusion and an interest in the secrecy of personal information.

In *Swiderski*, Swiderski Electronics sent Rizzo, a private detective, and others a fax advertisement with sales information on various types of electronic equipment. This type of advertising still occurs with unsuspecting new businesses or those that simply do not realize that it may be illegal. In response to this advertising, Rizzo filed a class action suit alleging that, by faxing copies of the advertisement without first obtaining the recipients' permission, Swiderski violated section 227 of the Telephone Consumer Protection Act (TCPA) (47 U.S.C. § 227 (2000)). The

complaint sought damages, attorney fees, and injunctive relief on behalf of all individuals who received an unsolicited fax advertisement from Swiderski.

Swiderski tendered defense of the suit to its primary insurer, Valley Forge, and its excess insurer, Continental Casualty Corporation. The policies provided similar coverage. Under the Valley Forge policy, Valley Forge had a duty to defend Swiderski against any suit seeking damage caused by "personal and advertising injury." Personal and advertising injury included injury that arose from "oral or written publication, in any manner, of material that violates a person's right of privacy."

Swiderski argued that the complaint alleged facts potentially within policy coverage so that the insurer had a duty to defend.

The essence of a TCPA fax-ad claim is that one party sends another an unso-

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licited fax advertisement. The receipt of an unsolicited fax advertisement implicates a person's right of privacy insofar as it violates a person's seclusion, and such a violation is one of the injuries that a TCPA fax-ad claim is intended to vindicate. The harm from unsolicited faxes involves protection of 'privacy.' The court found that the TCPA's private right of action was meant to remedy and prevent the twin harms of damage to privacy and economic damage. The court found that it was clear that the TCPA aimed in part to protect privacy. With the TCPA, Congress took aim at the intrusive nature of unsolicited faxes.

The complaint implicitly alleged a violation of a privacy interest. Based on the plain, ordinary, and popular meaning of those words, the court believed that this type of injury fell potentially within the coverage of the "advertising injury" provision.

The policy did not define the terms "publication," "material," or "right of

privacy." The court found that the "right of privacy" connoted both an interest in seclusion and an interest in the secrecy of personal information. The policy language "material that violates a person's right of privacy" could reasonably be understood to refer to material that violated a person's seclusion. Unsolicited fax advertisements, the subject of a TCPA fax-ad claim, fall within this category.

By faxing advertisements, Swiderski engaged in the "written * * * publication" of the advertisements. The "material" that Swiderski allegedly published, advertisements, qualified as "material that violated a person's right of privacy," because, according to the complaint, the advertisements were sent without first obtaining the recipients' permission, and therefore violated their privacy interest in seclusion. The language of the "advertising injury" provision was sufficiently broad to encompass the conduct alleged in the complaint.

The court noted that its conclusion was in agreement with the majority of federal courts of appeals that have considered "advertising injury" coverage for fax-ad claims. State courts remain incongruent in their holdings due to varying policy language and a mixed application of the law.

In this case, what may have seemed like an innocent advertising action, can cause significant downstream damage. Here, an insured was merely sending out a notice of a sale and some rental information. This generated a private cause of action on the part of each recipient. A class action suit followed, triggering coverage under a liability policy.

Most businesses are now aware of the TCPA and refrain from this activity. For those few remaining companies, as well as new start-up companies, a fax-ad campaign could lead to a series of suits and potential coverage under a liability policy.

Update on Illinois Targeted Tenders under *John Burns*: Businesses reduce costs through the shifting of defense and indemnification costs

With two additional decisions on targeted tenders and an answer to the decade-old question of horizontal exhaustion, it seems an appropriate time to review where we are with targeted tenders. Business owners, officers and risk managers have a unique tool at their disposal in Illinois for shifting defense and indemnification costs away from their insurance policy and targeting another company's policy—the Targeted Tender. In 1992, the Illinois appellate court reached a decision that resulted in confusion, litigation and unexpected results ever since. Under Illinois' unique rule, when a business is covered by two or more policies, it can select or target one insurer to respond to a claim. The Targeted Tender stops the selected insurer from recovering from any other policy including the business's own policy.

The ability to exercise this election arises where multiple avenues of insurance coverage exist including additional insureds and multiple policies covering one insured. An additional insured situation can arise from any contractual agreement wherein a business requires one of its vendors, sub-contractors or business partners to name it as an insured under the vendors, sub-contractors or business partner's policy.

For example, If ABC, Inc. is the owner of a property under development and is insured under a liability policy, and is also an insured under the general contractor, 123's policy, ABC, Inc. can elect to have 123's policy provide a defense and indemnification for a claim or suit. By requiring to be named an additional insured in a contract and selecting 123's insurer to pay for the costs, ABC, Inc. reduces its loss history, shifts defense and indemnification costs

and saves money.

The Targeted Tender rule is unique to Illinois. The action of shifting defense and indemnification costs has been referred to by various names including a "Selective Tender," "Targeted Tender," "Institute Tender," and "John Burns Tender." The names Institute and Burns arise from the two primary decisions creating and supporting what has been referred to as an insured's paramount right to select which insurer will respond to a loss. The court in *Institute of London Underwriters v. Hartford Fire Ins. Co.*, 234 Ill. App.3d 70, 599 N.E.2d 1311, 175 Ill. Dec. 297 (1st Dist. 1992), adopted the rule that an insured has the right to elect which of a multitude of insurance policies must defend and indemnify a claim by tendering its defense to only one of the insurers. An insured may select an insurance policy that additionally insures it to be the

insurance policy obligated to defend and indemnify. This selection forecloses the selected insurer from obtaining contribution from the non-selected insurer. The Supreme Court adopted this rule in *John Burns Construction Co. v. Indiana Insurance Co.*, 189 Ill. 2d 570 (2000).

In *Institute of London*, a contractor hired an engineering company to perform repairs on a dockwall. The contract required that the engineering firm secure insurance and list the contractor as an additional insured, which it did with Institute of London Underwriters. In addition, the contractor had its own policy of insurance with Hartford. When a tort action was filed against the contractor, the contractor tendered the action to the engineering firm for its defense and indemnification. The contractor also notified its own insurance carrier, Hartford, of the action. Following the court approval of a \$75,000 settlement, the vice president of the contracting company told the attorney representing the contractor, as well as the contractor's insurance carrier, Hartford, that Hartford should not contribute to the settlement in any way. Ill.App.3d. at 73. Further, the vice president told an adjuster for Hartford that it did not want the Hartford policy to respond to the settlement, but rather, the contractor elected to have the engineering firm and its insurer, Institute of London, pay for the indemnification and defense costs for that litigation. The court allowed the insured to select one policy to the exclusion of another.

Based upon the *Institute of London* decision, an insured that is covered by more than one policy of insurance has the right to forgo the assistance of one or more of the insurers. In order to tender to only one insurer, the insured must expressly state their intentions to the non-selected insurer and tender the matter to the selected insurer. The choice by the insured to tender to only one insurer will be upheld by the courts on the basis that there is no coverage under a policy which is not triggered.

Horizontal Exhaustion Rules Supersede The Targeted Tender Doctrine

In 2006, the first district settled a dispute that had been brewing for years. The issue of targeting an umbrella policy to the exclusion of a

primary policy had been hotly contested and litigated since 1993. Prior to the ruling in *Kajima Const. Services, Inc. v. St. Paul Fire and Marine Ins. Co.*, --- N.E.2d ---, 2006 WL 2662703, (Ill. App. 1 Dist., Sep 15, 2006), which held that primary policies must be exhausted horizontally before umbrella policies are impacted, circuit courts and federal district courts announced conflicting decisions.

In *Cincinnati Ins. Co. v. Boller Const., Inc.*, 2006 WL 695459 (N.D.Ill. Mar 15, 2006), the court applied principles of horizontal exhaustion when it held that an insured should not be permitted to target an umbrella policy to the exclusion of a primary policy. A contrary rule would permit an insured to convert an umbrella policy into a primary policy without regard for the "unique and special" status of coverage afforded by an umbrella policy. The court relied in part upon *Illinois Emcasco Ins. Co. v. Continental Casualty Co.*, 139 Ill.App.3d 130, 133, 93 Ill.Dec. 666, 487 N.E.2d 110, 112 (1st Dist. 1985), which found that an umbrella or "catastrophe" policy "remains excess over and above all other applicable insurance.

For years, the question persisted as to whether a second layer or umbrella policy could be targeted to the exclusion of the primary or first layer coverage. In 2006, the first district appellate court settled this dispute. The issue of targeting an umbrella policy to the exclusion of a primary policy had been hotly contested and litigated since 1993. Prior to the ruling in *Kajima Const. Services, Inc. v. St. Paul Fire and Marine Ins. Co.*, --- N.E.2d ---, 2006 WL 2662703, (Ill.App. 1 Dist., Sep 15, 2006), a pharmacy effectively targeted an umbrella policy to the exclusion of a primary policy and several circuit court decisions had rendered conflicting opinions. *Aetna Casualty and Surety Co. v. Chicago Ins. Co.*, 994 F.2d 1254 (7th Cir. 1993). The issue was settled in *Kajima*, when a general contractor, *Kajima Construction Services, Inc.*, and its insurer brought a declaratory judgment action against its subcontractor's insurer, seeking reimbursement for payments made to settle a suit.

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indemnity payment made to settle a bodily injury lawsuit filed against it by an employee of the subcontractor. St. Paul Fire and Marine Ins. Co. issued primary and excess policies the subcontractor that named Kajima as an additional insured. Kajima made a "targeted tender" also known as a "targeted election" to St. Paul Fire and Marine Ins. Co. for its defense and indemnification. St. Paul Fire and Marine Ins. Co. paid its primary limits of \$2 million to settle the underlying case and Kajima's own primary insurer paid the remaining \$1 million for total settlement of \$3 million. Kajima and its carrier then sought recovery of the \$1 million from St. Paul Fire and Marine Ins. Co.'s excess policy. The trial court rejected the targeted tender and instead applied principals of horizontal exhaustion requiring that primary policies be exhausted before coverage from excess policies would apply. The Illinois Appellate Court affirmed the trial court and found that the targeted tender rule did not trump horizontal exhaustion rules.

Although this issue has been addressed by prior courts, the *Kajima* court framed the issues as one of first impression and stated that:

The question, however, of whether an insured that selectively tenders its defense and indemnification to an insurer will be required to exhaust its primary limits and reach its excess limits before a deselected insurer will be obligated to contribute its primary limits has yet to be answered.

Plaintiffs also conceded that no published case or court in Illinois extended the selective tender rule to preempt the horizontal exhaustion doctrine and require an insurer to vertically exhaust its primary and excess coverage limits. The decision in *Aetna v. Chicago*, *supra*, was not discussed by the court.

Horizontal exhaustion is operative when an insured has coverage under multiple primary policies and one or more excess policies. Under the principle of horizontal exhaustion, the insured must exhaust all available primary coverage before seeking coverage under an excess policy that covers a common risk. If a covered claim occurs, the insured must exhaust all primary policy limits before invoking excess coverage. See *Illinois Emcasco*

Insurance Co. v. Continental Casualty Co., 139 Ill.App.3d 130, 134 (1985); *United States Gypsum Co. v. Admiral Insurance Co.*, 268 Ill.App.3d 598, 652- 53 (1994). In *Illinois Emcasco*, the court recognized differences between primary coverage policies and umbrella policies and took underlying policy considerations into account and then concluded that an umbrella policy was unique in that it always remained excess over and above other contracts with few exceptions and could not be activated until all primary coverage was exhausted. *Illinois Emcasco*, 139 Ill. App.3d at 133-34.

Under the principle of vertical exhaustion, an insured may seek coverage from an excess insurer after exhausting the primary limits beneath the excess policy as identified in the excess policy's declaration page, have been exhausted, regardless of whether other primary insurance may apply.

Consequently, the *Kajima* court was faced with two irreconcilable rules of law. One creating the insured's paramount right to select which policy would apply and the other that required the insured to exhaust primary coverage before invoking excess coverage. The preverbal irresistible force met an immovable object. This apparent omnipotent paradox was easily broken in 33 words from the court when it held:

[T]hat the selective tender rule does not entitle an insured to vertically exhaust consecutive insurance policies and deselected primary insurers must answer for a loss before an excess insurance policy will be activated.

In the court's view, the selective tender rule should be applied to circumstances where concurrent primary coverage exists for additional insureds. It cannot be exercised to upwardly exhaust coverage when primary policies exist. The question left unanswered is the fundamental reason that *Institute of London* and *John Burns* exist; an insured can forego coverage by failing to provide notice to an insurer which relieves the insurer from taking action. A case will certainly arise where an insured decides to withhold notice to its primary carrier altogether without reference to a targeted tender. In that situation, the insurer would be free to deny the claim due to a lack of notice. The

effect would be a vertical exhaustion of a primary and excess policy to the exclusion of another primary policy.

Targeted Tender Permitted With Excess Policies After Exhaustion of Primary Policies

The extension of a targeted tender was reviewed by the court in *North River Ins. Co. v. Grinnell Mut. Reinsurance Co.*, --- N.E.2d ---, 2006 WL 3545139 (Ill.App. 1 Dist., 2006). The rule was adopted by the court as applied to concurrent excess policies. The *North River* court stated that it could not articulate a reason why the Targeted Tender rule cannot or should not be applied to concurrent excess insurance coverage. It found no authority prohibiting an insured's right to select or deselect a particular policy when it had concurrent coverage. Because the selective tender rule was applied only concurrently at either the primary or excess level and not consecutively, the concerns about blurring the line between primary and excess insurance policies is not applicable. In so finding, the court held that once an insured has exhausted its concurrent primary insurance coverage, it may selectively tender its indemnity to concurrent excess insurers.

Future Attacks Upon *Institute of London*

If dissatisfaction with *Institute of London* grows, a retreat by the courts may take place. This may take place through limitations on the use of *Institute of London* to specific commercial policies or indirect limitations are applied by the courts. These limitations will most likely grow from well reasoned theories that were in existence well before *Institute of London*. The limits will likely arise from equitable arguments such as estoppel, prejudice to the insurer, failure to trigger a policy within a reasonable time and law arguments such as waiver of a known contractual right.

Proposed Legislation Changes

Several attempts have been made by the legislature to amend the targeted tender rule through legislative intervention. Recently, Illinois State Senator William R. Haine introduced a bill on January 20, 2006 that would require an insured to tender to all carriers. The text

of the bill provides as follows:

215 ILCS 5/143.33 new.

Amends the Illinois Insurance Code. Provides that in instances where 2 or more commercial liability policies provide coverage for the same claim or loss, a party seeking coverage under one policy must also tender the defense and indemnity of the claim or loss to any other insurer that may also provide coverage. Provides that the allocation of defense costs and indemnity payments shall be determined by the terms of the policies of insurance. Provides that the failure of an insured to comply with the requirements of the Section does not preclude an insurer from seeking contribution from other insurers that also provide coverage for the claim or loss. Effective immediately.

The proposed bill had its first reading and was referred to the Rules Committee on the date of its introduction. No further action was taken. A similar bill was introduced several years ago and did not make it out of the Rules Committee. Based upon this history, it appears that there is little support for a statute that controls the contractual relationship between the parties and the ability to target a specific insurer.

Estoppel And Prejudice To The Insurer

The appearance of prejudice to an insurer may serve to limit the advance of *Institute of London* or even signal its end. If an insured makes a targeted tender to an insurer and then fails to keep its own insurer or other insurers that were not triggered informed of the status of the case, the insured may be estopped from retendering to its own insurer or any other insurer that was not kept advised of the progress of the case. The insurer will likely raise a claim of prejudice and allege that the insured is estopped from retendering the claim.

Application With Consecutive Policies

Where a continuing bodily injury or property damage claim exists along with the potential for consecutive coverage, an Illinois court would be required to reconcile the Targeted Tender rule with the *Kajima* decisions requiring the exhaustion of primary

coverage before tendering to umbrella policies. An excess carrier could force the triggering of all primary policies before the insured could spike the coverage up into an umbrella policy. Further, a court may not permit an insured to select one insurer among multiple consecutive policies spanning several years.

Failure To Trigger A Policy Within A Reasonable Time

The policy defenses available to an insurer are not abrogated by *Institute of London*. An insurer may still raise the policy defense of late notice or lack of proper notice as required by the policy. In addition, an insurer will likely soon claim that a targeted tender was made to a different insurer thus relieving it of its duty to defend and indemnify.

Upon the retender to the first insurer for some reason, the insurer that was not triggered in the first instance will likely claim a failure on the part of the insured to trigger the policy within a reasonable time. This claim is closely related to the prejudice issued stated above.

Pre-Contract Waiver Of A Right To Selectively Trigger A Policy

Finally, liability insurers will likely take a proactive approach to *Institute of London* and include endorsements within their policies requiring the insured to tender to all insurers contractually required to provide coverage to the insured. The targeted tender is a right based in contract that is held by the insured. An insured is free to contract and free to waive any contractual right that it holds. Illinois courts have recognized a contractual right of the insured to tender to a policy of their choice while electing to not trigger their own policy or even deselect their previously triggered policy. This right has been exercised against commercial liability policies, umbrella policies, professional liability policies and risk pooling agreements.

Although the decision in *Institute of London* has received broad acceptance, there have been several notable exceptions including the decision in *American Country Ins. Co. v. Kraemer Bros., Inc.*, 298 Ill.App.3d 805, 699 N.E.2d 1056, 232 Ill. Dec. 871 (1st Dist., 1998) and the concurring opinion authored by Judge Quinn in *Chicago*

Hospital Risk Pooling Program v. Illinois State Medical Inter-INS Exchange, 325 Ill.App.3d 970, 758 N.E.2d 353, 259 Ill. Dec. 230 (1st Dist., 2001). The decision in *Kraemer Brothers* and concurring opinion of Judge Quinn provide guidance for avoiding a targeted tender. From these decisions, liability insurers have begun including endorsements designed to avoid a targeted tender.

We may soon see this right exercised under non-commercial policies such as rental car insurance or homeowner policies. The targeted tender is a right based in contract that is held by the insured. Insurers may react to this trend with their own policy language. An insured is free to enter into contracts and potentially free to waive any contractual right that it holds. With the enforcement of unambiguous policy language, we will soon see contractual waivers of certain rights including the right to selectively tender to an insurer.

An endorsement offers a possibility of avoiding a targeted tender under *Institute of London* from an insured. Pursuant to an anti-tender endorsement, if an insured desires to retain the coverage that is available from its insurer, the insured must also retain all other coverage. If the insured fails to tender to other insurers, the insurer is not obligated to defend or indemnify the insured.

The common factor reviewed by each court addressing *John Burns* and *Institute of London*, is "Whether the policy of insurance was triggered." The decisions applicable to commercial policies uniformly hold that an insured who is insured under multiple policies may elect to trigger only one policy and forgo the assistance of its own insurer. There is no contractual basis for a court to prohibit the use of a Targeted Tender in a personal lines policy nor to limit pre-loss waivers of the right. Future decisions will likely address these issues.

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