

## **Illinois Coverage Basics**

### *What Every Insurer Needs to Know about Declaratory Judgment Actions in Illinois State Courts*

In Illinois, most insurance coverage disputes are litigated in declaratory judgment actions. Perhaps because declaratory judgment actions are so common, we sometimes tend to lose sight of the strategic options and limitations of this unique form of action. Getting the most out of a declaratory judgment action requires a clear understanding of the requirements and options that are available under the Declaratory Judgment Act.

#### **The Illinois Declaratory Judgment Act**

An insurer's right to bring a declaratory action is based upon a state statute. The Illinois Declaratory Judgment Act broadly authorizes insurance companies to file declaratory judgment actions to resolve coverage disputes in the following terms:

“The court may, in cases of actual controversy, make binding declarations of rights, having the force of final judgments, whether or not any consequential relief is or could be claimed, including the determination, at the instance of anyone interested in the controversy, of the construction of any ... contract or other written instrument, and a declaration of the rights of the parties interested.”

#### **Prerequisites for Filing a Declaratory Judgment Action**

The Illinois Declaratory Judgment Act has few formal requirements for maintaining a declaratory judgment action, but one absolute requirement is that every declaratory judgment action must present an “actual controversy.” Great West Casualty Co. v. Cote, 365 Ill.App.3d 100, 105, 847 N.E.2d 858, 862 (1st Dist. 2006). That requirement has particular importance for insurance coverage disputes. It means that in most insurance coverage cases, a declaratory judgment action *can* be used to determine an insurer's duty to defend, because an insurer's duty to defend is based upon the allegations of the underlying complaint. However, it also means that a declaratory judgment action usually *cannot* be used to determine an insurer's duty to indemnify until the underlying claims have been resolved. Travelers Insurance Co. v. Eljer Manufacturing, Inc., 197 Ill.2d 278, 298, 757 N.E.2d 481, 494 (2001). The rationale of this rule is that, until a judgment or settlement is entered, the question of indemnity is purely hypothetical.

#### **Right to a Jury**

Although most insurance coverage declaratory judgment actions are decided by summary judgment, the Declaratory Judgment Act provides for jury trials in at least some declaratory

judgment actions. The Illinois declaratory judgment statute states that if a declaratory judgment action involves the determination of issues of fact, they shall be tried and determined in the same manner as issues of fact are tried and determined in other civil actions. 735 ILCS 5/2-1007 (d). However, a party that fails to file a timely jury demand in a declaratory judgment action waives its right to a jury trial. Bituminous Casualty Corp. v. Wilson, 119 Ill.App.3d 454, 459, 456 N.E.2d 696, 700 (2nd Dist. 1983). If a timely jury demand is filed, then the right to a jury depends upon (a) the existence of an unresolved question of fact, and (b) whether the claim is one for which the state constitution guarantees a trial by jury. Berk v. Will County, 34 Ill.2d 588, 591-592, 218 N.E.2d 98, 100 - 101 (1966).

### **When an Insurer Must File a Declaratory Judgment Action**

Although declaratory judgment actions are generally governed by Illinois' ten-year statute of limitations governing disputes on written contracts, the State's estoppel rule effectively requires insurers seeking declaratory judgments to file suit much earlier. By case law, the rule has evolved that an insurer may be estopped from denying coverage unless it files a declaratory judgment action to determine its obligations within "a reasonable time." L.A. Connection v. Penn-America Insurance Co., 363 Ill.App.3d 259, 266, 843 N.E.2d 427, 433 (3rd Dist. 2006).

### **Necessary Parties**

In Illinois state courts, the party making a claim against an insured for damages must be joined as a defendant in an insurer's declaratory judgment action. Society of Mount Carmel v. National Ben Franklin Insurance Co. of Illinois, 268 Ill.App.3d 655, 661, 643 N.E.2d 1280, 1285 (1st Dist. 1994). Yet, no such rule exists for coverage actions in the federal courts in Illinois.

### **What Relief Is Available in a Declaratory Judgment Action**

If an insurer wins a declaratory judgment action, it cannot recover its costs of prosecuting or defending the declaratory judgment action. Id., 268 Ill.App.3d at 675, 643 N.E.2d at 1294. Further, even if the court rules that the insurer owes no duty to defend, the insurer cannot recover the defense expenses that it incurred while defending the insured under reservation of rights. General Agents Insurance Co. of America, Inc. v. Midwest Sporting Goods Co., 215 Ill.2d 146, 162, 828 N.E.2d 1092, 1101-1102 (2005). What an insurer gets when it wins a declaratory judgment action against its insured is simply the declaratory judgment itself; not money.

In contrast, a prevailing insured in a declaratory judgment action may recover its defense costs, reimbursement for paid settlements or judgments, and sometimes even its expenses for litigating the coverage dispute. Significantly, a judicial declaration that an insurer owes such amounts is not the procedural equivalent of a money judgment against the insurer. An insurer wishing to appeal an adverse declaratory judgment may avoid filing an appeal bond if it seeks to overturn a declaratory judgment on appeal, while under Supreme Court Rule 305 an insurer must provide security if it seeks to stay enforcement of a money judgment pending appeal.

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If you have questions or would like to discuss the implications of this report further, please feel free to contact James K. Horstman at Cray Huber Horstman Heil & VanAusdal LLC, 303 West Madison, Suite 2200, Chicago IL 60606; 312-332-8494; [jkh@crayhuber.com](mailto:jkh@crayhuber.com).