

## 2023 Nevada Assembly Bill 398 (AB 398) Will Soon Prohibit Liability Insurance Policies from Reducing Liability Limits by Defense Costs

As Nevada's 2023 legislative session came to close, Governor Joe Lombardo signed Assembly Bill No. 398 (AB 398; ch. 121) into law, which will soon prohibit insurers from issuing or renewing a liability insurance policy containing a provision that reduces the stated policy limit by the costs of defense, including legal fees and costs, or otherwise limits the availability of coverage for such defense costs.

This piece of legislation flew under the radar of the various insurance trades chambers of commerce in the state.

The following is intended to alert Nevada credit unions to this change that will take effect on October 1, 2023, address some key questions about the law and what it means for credit unions and credit union service organizations (CUSOs), and provide an update on steps being taken to provide further clarification and guidance.

### Background

Effective October 1, 2023, AB 398 adds the following language to Chapter 679A of the Nevada Revised Statutes (NRS):

*Notwithstanding any other provision of law, an insurer, including, without limitation, an insurer listed in NRS 679A.160, shall not issue or renew a policy of liability insurance that contains a provision that:*

- 1. Reduces the limit of liability stated in the policy by the costs of defense, legal costs and fees and other expenses for claims; or*
- 2. Otherwise limits the availability of coverage for the costs of defense, legal costs and fees and other expenses for claims.*

AB 398 will not apply to any contract for liability insurance existing on October 1, 2023, but will apply to any renewal of such a contract.

### How AB 398 Could Impact Credit Unions and CUSOs

According to the Division of Insurance, liability policies expected to be impacted by AB 398 include but are not limited to: Errors and Omissions (E&O) and other professional liability policies; Directors and Officers (D&O); Cyber Liability; Employment Practices Liability; Fiduciary Liability; and Excess and Umbrella policies. Currently, it is common for liability policies such as these to contain a defense within the limits (DWL) provision whereby the stated coverage limit is available to cover not only the underlying claim, but the costs of defense, including attorney fees and related expenses.

With the objective of greater transparency and increased choice, AB 398 will prohibit an insurer from issuing or renewing a liability policy that includes a DWL provision, or from otherwise limiting the availability of coverage for such defense costs, requiring defense costs to be subject to separately stated limits. However, this will necessarily impact insurance underwriting and rating practices, which raises concerns for insureds due to its potential to adversely impact both the cost and availability of liability policies and separate defense costs coverage. And defense costs are notoriously unpredictable.

The Nevada Division of Insurance has issued an [Emergency Regulation](#) and [Guidance to Insurers](#) to help clarify the language of AB 398, along with a [Proposed Regulation](#) that, once adopted, will replace the Emergency Regulation.

## Emergency Regulation

The Division of Insurance [Emergency Regulation \(LCB File No. E002-23A\)](#), set to expire on November 21, 2023, was issued to respond to three (3) immediate concerns:

### **1) What is meant by “policy of liability insurance?”**

“Liability insurance” is a type of casualty insurance coverage “against legal liability for the death, injury or disability of any human being, or for damage to property, including liability resulting from negligence in rendering expert, fiduciary or professional services...” [NRS 681A.020.1(b)] offered by an insurer authorized to offer the casualty line of authority for third-party liabilities. [NRS 680A.060; NRS 694C.230]

### **2) What insurers will AB 398 not apply to based on existing state and federal law?**

AB 398 does not apply to risk-retention groups for which “liability” is defined to include defense costs or captive insurance that does not cover third-party liability. [15 USC §3901]

### **3) How will defense coverage be made available?**

A liability policy that must be filed with the Division must make defense coverage available at the defense coverage limit selected by the insured, if any. Any defense coverage limit selected, including \$0, must be included on the declaration page. This does not apply to policies that do not limit defense costs coverage.

## Guidance to Insurers

The Nevada Division of Insurance also issued [Guidance to Insurers](#) to address immediate questions as the industry moves to quickly adapt its policies and practices to the new requirements. Some of the key clarifications include:

- **Separate Limits for Defense.** Under AB 398, a liability insurance policy must include defense costs outside of the stated liability limits. While defense coverage must be available, it need not be unlimited. Unless the policy provides for unlimited defense costs, the limit for defense costs may be selected by the insured, including a limit of \$0.
- **Deductibles and Self-Insured Retention.** AB 398 does not prohibit an insurer from issuing policies that include self-insured retentions or deductibles on liability coverage and/or defense costs.
- **Cancellation Requirements; Division Review.** Under existing law, an insurer that intends to withdraw from offering insurance for a particular class of insureds is required to notify the Commissioner at least 60 days before providing the required notice of cancellation or non-renewals to insureds. [NRS 687B.410] The Division recognizes that AB 398’s October 1, 2023 effective date would make it impossible for any insurer to comply with this 60-day advance notice requirement, but notes that it has no authority to change the effective date. It will therefore prioritize reviewing new policy language impacted by AB398.
- **Cyber Liability Policies.** The Division notes that cyber liability policies include both first-party indemnity to the insured and third-party liability coverage, often under the same per occurrence and annual aggregate limits. Under AB 398, defense costs coverage for third-party liability insurance must be offered separate from the liability limit. However, nothing prevents first-party indemnity and third-party liability from sharing the same policy coverage limit. Defense costs may not erode the per occurrence or annual aggregate limit of liability coverage.

- **Policy Exclusions.** AB 398 does not mandate specific coverages that must be included or may be excluded in a policy of liability insurance; it only mandates that the limits for the types of liability that are included in the contract cannot be eroded by costs of defense.
- **Surety and Fidelity Bonds.** Surety and fidelity bonds are not considered casualty insurance and do not typically include the obligation to defend third party liability. Accordingly, they are not subject to the AB 398 prohibition unless the bond included defense in the surety contract.

Additional information can be found in the in the [Guidance to Insurers](#).

### **Proposed Regulation**

The [Revised Proposed Regulation \(LAB File No. R029-23; August 25, 2023\)](#) is substantially similar to the Emergency Regulation with a few additional clarifications. Specifically, it clarifies that AB 398 applies to a liability insurance policy issued to a policyholder in the State of Nevada.

### **Next Steps and Recommendations**

The Nevada Division of Insurance held a public meeting on September 12, 2023 but the proposed regulation has not yet been adopted. Stakeholders may submit additional comments through September 27, 2023 by email at [regs@doi.nv.gov](mailto:regs@doi.nv.gov). The Legislative Committee has a meeting scheduled for 10am on September 28, 2023. They must also approve the regulation for it to take effect, which could happen before or after Division approval. The Division has indicated its intention to have a final regulation in place before the emergency regulation expires.

As AB 398 impacts Nevada businesses and industries across the board, there are a large number of stakeholders working to address the various concerns and minimize any potential negative impact. It is likely, however, that any significant improvement will require a legislative fix, and the next legislation session doesn't begin until 2025.

Credit unions and CUSOs are strongly encouraged to carefully track all upcoming liability policy renewal dates and to reach out to their insurance carriers well in advance to discuss policies affected by AB 398 and what it might mean in terms of premiums, coverage, or even the continued availability of current policies. It is important to be proactive in this area in case it becomes necessary to consider alternative policies and/or insurers. Understanding how much has been allocated to defense costs in prior claims will help the credit union better understand the amount of defense costs coverage that may be needed going forward.

We will provide you with updated information as it becomes available.

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