

**Coloring Outside the Lines:
The Limits of Extra-Contractual Obligations
in Life and Property/Casualty Reinsurance**

Session Materials

Claim Scenario
Sample ECO Clauses

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Claim Scenario

ECO Claim Scenario

Careless Corporation was sued in a wrongful death action arising from a gas explosion at a corporate farm operated by Careless Corporation and owned by a joint venture partnership between Careless Corporation and an affiliated company, Slightly Better Company. Inc.

Insurer Beleaguered Company issued a \$1 million primary policy and \$5 million umbrella policy to Company X. Both Careless Corporation and the joint venture sought coverage from Beleaguered Company for the wrongful death claims. Beleaguered Company agreed to defend and indemnify Careless Corporation but denied coverage for the joint venture.

Beleaguered Company's casualty business was reinsured under an excess of loss tower, comprised of three separate layers: \$500,000 XS \$500,000, \$1 million XS \$1 million, and \$3 million XS \$2 million. Each excess of loss treaty expressly excluded umbrella business. The umbrella business was separately reinsured under a quota share reinsurance treaty covering 90% of loss up to a \$5 million limit.

All reinsurance contracts included coverage for ECO and XPL loss. Some of the reinsurance contracts covered LAE within limits and others covered LAE in addition of limits.

Immediately prior to trial, Beleaguered Company tendered its \$1 million primary policy limit on behalf of Careless Corporation to settle the claims. During trial, the claimants in the wrongful death action made a combined demand to settle their claims against all defendants in an amount within the combined limits of the primary and limits. Before Beleaguered Company could respond, the jury rendered its verdict, awarding claimants \$12 million total against Careless Corporation and the joint venture. Beleaguered Company, Careless Corporation and Slightly Better Company subsequently settled the wrongful death claims on appeal for \$9 million, with Insurer contributing the full amount of its limits and a proportionate share of prejudgment interest, which was covered as a supplementary payment outside of limits.

Careless Corporation and Slightly Better Company subsequently sued Insurer for bad faith, based on numerous alleged wrongful acts relating to the Beleaguered Company's denial of coverage as to the joint venture, investigation, handling and defense of the wrongful death claims and trial, and failure to settle the claims within limits.

Beleaguered Company had a \$5 million E&O policy written on a defense within limits basis to which it tendered the bad faith claim, and the E&O insurer, denied the claim.

Keep in mind that Bealeaguered Company incurred \$5 million defending the bad faith claims and ultimately settled the bad faith lawsuit for \$7 million.

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Sample ECO Clauses

LH 1-2

PC 1-4

BMRA 1-4

LH-1

EXTRA CONTRACTUAL OBLIGATIONS (CONSULT AND CONCUR)

In no event, except as allowed for in the following paragraph, shall the Reinsurer participate in punitive or compensatory damages or statutory penalties or declaratory judgments (hereinafter called "Extra Contractual Obligations") which are awarded against the Company as a result of an act, omission, or course of conduct committed by or on behalf of the Company, which arise from the handling of any Claim on Policies reinsured under this Agreement.

The Company shall notify the Reinsurer in writing of any impending Claim likely to involve Extra Contractual Obligations as soon as practicable, but within ten (10) business days of the Company receiving notice of such impending Claim. The Company's notification to the Reinsurer shall include all Claim information and a suggested course of action or inaction for the Reinsurer's review. The Reinsurer then has the obligation to notify the Company in writing, within ten (10) business days from the date the Reinsurer received such notice of the impending Claim, with its decision to concur or not concur in the Company's suggested actions to be taken, or not taken. Failure of the Reinsurer to notify the Company within ten (10) business days, after acknowledgment of its receipt, of its decision shall be deemed agreement by the Reinsurer with the Company's suggested course of action or inaction. Company and Reinsurer recognize that there could be circumstances, where through no fault on the part of the Company or any of its agents, the Company requires a response from the Reinsurer in less than the time frame allowed herein. In such event, the Company shall advise the Reinsurer of the circumstances and the response time needed, and the Reinsurer shall make every reasonable effort to meet the Company's request. If the Reinsurer concurs with the Company's action, payment of such damages shall be shared by both Company and Reinsurer in the same proportions which govern this Agreement.

If the Reinsurer does not concur with the Company's action, the Reinsurer shall so state its reasons for not concurring in writing and deliver same to the Company. Company shall review such Reinsurers' response, and reassess the course of action taking into consideration the reasons so stated by the Reinsurer. If the Reinsurer and the Company agree on a mode of handling such impending extra contractual obligation, the Reinsurer shall not be afforded an opportunity to relieve itself of potential liability on the subject Claim by paying its proportionate share of the disputed Claim and attendant expenses. If the Reinsurer disagrees with the recommended action or decision that the Claim should be denied and/or defended, then the Reinsurer may discharge its liability hereunder by paying its proportionate share of the underlying Claim from which the matter arose, and will have no further liability for such matter.

The Company and the Reinsurer shall cooperate in every respect in the defense of such claim, suit, or proceeding when working in concert. At the request of the Reinsurer, the Company shall afford the Reinsurer every opportunity to be associated with the Company, at the Reinsurer's expense, in the defense of any claim, suit or proceeding involving the Reinsurer's liability hereunder toward such claim, suit or proceeding. Should the Reinsurer choose to participate in the defense, any settlement negotiation involving the Reinsurer's liability with regard to such claim, suit or proceeding shall be mutually agreed upon by the Company and the Reinsurer. The Company and the Reinsurer shall cooperate in every respect in the defense of such claim, suit or proceeding.

For purposes of this Article, the following definitions will apply:

LH-1

“Punitive damages” are those damages awarded as a penalty, the amount of which is not governed, nor fixed by statute.

“Statutory penalties” are those amounts which are awarded as a penalty but fixed in amount by statute.

“Compensatory damages” are those amounts awarded to compensate for the actual damages sustained, and are not awarded as a penalty nor fixed in amount by statute.

The language of this Article shall be deemed effective only as and to the extent permitted by the law of any applicable jurisdiction.

A loss awarded or Extra Contractual Obligations will be deemed to have occurred on the same date as the loss covered or alleged to be covered under the Policy.

Notwithstanding anything stated herein, this Agreement will not apply to any Extra Contractual Obligation incurred by the Company as a result of any fraudulent and/or criminal act by any officer or director of the Company acting individually or collectively, or in collusion with any individual or corporation or any other organization or party involved in the presentation, defense, or settlement of any claim covered hereunder.

Recoveries from any form of insurance or reinsurance maintained by the Company against claims, which are the subject matter of this Article, will inure to the benefit of this Agreement.

EXTRA CONTRACTUAL OBLIGATIONS AND EXCESS OF POLICY LIMITS

- A. This Agreement covers any Extra Contractual Obligations which are paid or payable by the Company. "Extra Contractual Obligations" means those liabilities not covered under any other provision of this Agreement, which arise from business covered hereunder, such liabilities arising because of, but not limited to, the following: failure by the Company to settle within the Policy limit, or by reason of alleged or actual negligence, fraud or bad faith in claims handling or in rejecting an offer of settlement or in the preparation of the defense or in the trial of any action against its insured or reinsured or in the preparation or prosecution of an appeal consequent upon such action.
- B. In addition, this Agreement covers amounts in Excess of Policy Limits which are paid or payable by the Company. Amounts in "Excess of Policy Limits" means any amount payable in excess of the Policy limit for reasons including alleged or actual negligence, fraud or bad faith in failing to settle or rejecting a settlement within the Policy limit, in preparation of the defense, in the trial of any action involving the insured or the Company, or in the preparation or prosecution of an appeal consequent upon such action. Coverage under this Article extends only to amounts that would have been covered had it not been for the limit of the original Policy.
- C. For the purpose of this Article, amounts in Excess of Policy Limits and/or Extra Contractual Obligations shall become payable by the Company subsequent to a judgment which the Company does not intend to appeal, or on conclusion by the Company of a settlement agreement, or when a release has been obtained by the Company as regards any Extra Contractual Obligation or Excess of Policy Limits loss.
- D. The date on which any Extra Contractual Obligation or Excess of Policy Limits loss is incurred by the Company will be deemed, in all circumstances, to be the same date established in respect of the claim from which the Extra Contractual Obligation or Excess of Policy Limits loss arose and shall constitute part of the original loss. In addition, Loss Expenses incurred in connection with any Extra Contractual Obligation or Excess of Policy Limits loss shall be paid in the same manner as paid in connection with other losses under this Agreement.
- E. This Article will not apply where the loss has been incurred due to a final legal adjudication of fraud of a member of the Board of Directors or a duly elected corporate officer of the Company acting individually or collectively or in collusion with any individual, corporation or any other organization or party involved in the presentation, defense or settlement of any claim covered hereunder.
- F. Enforcement. If any provision of this Article is rendered invalid, illegal or unenforceable by the laws, regulations or public policy of any jurisdiction, such provision will be considered void in such jurisdiction, but this will not affect the validity or enforceability of such provision in any other jurisdiction.

EXTRA CONTRACTUAL OBLIGATIONS AND EXCESS LIMITS LIABILITY

- A. This Agreement will extend to cover any claims-related Extra Contractual Obligations and/or Excess Limits Liability arising because of, but not limited to, the following:
 - 1. Failure of the Company to agree to pay a claim within the Policy limits or to provide a defense against such claims or to pay a claim under the Policy reinsured within a reasonable time.
 - 2. Actual or alleged bad faith, fraud, or negligence in investigating or handling a claim or in rejecting an offer of settlement.
 - 3. Negligence or breach of duty in the preparation of the defense or the conduct of a trial or the preparation or prosecution of any appeal and/or subrogation and/or any subsequent action resulting therefrom.
- B. “Extra Contractual Obligations” as used in this Agreement will mean those liabilities not covered under any other provision of this Agreement for which the Company is liable to its insured or a third-party claimant, or that the Company paid as its share of a claims-related extra contractual obligation awarded against one or more of its co-insurers.
- C. “Excess Limits Liability” as used in this Agreement will mean any amount for which the Company would have been contractually liable to pay had it not been for the limits of the reinsured Policy.
- D. There will be no recovery hereunder where the Extra Contractual Obligation or Excess Limits Liability has been incurred due to fraud committed by a member of the board of directors or a corporate officer of the Company, acting individually, collectively, or in collusion with a member of the board of directors, a corporate officer, or a partner of any other corporation, partnership, or organization involved in the defense or settlement of a claim on behalf of the Company.
- E. The date on which any Extra Contractual Obligation and/or Excess Limits Liability is incurred by the Company will be deemed, in all circumstances, to be the date of the original loss. Nothing in this Article will be construed to create a separate or distinct loss apart from the original covered loss that gave rise to the Extra Contractual Obligations and/or Excess Limits Liability discussed in the preceding Paragraphs. The Reinsurer’s liability as respects Extra Contractual Obligations and/or Excess Limits Liability under this Agreement will be proportionate and in addition to the other coverage set forth in this Agreement, but the Reinsurer’s additional liability as respects Extra Contractual Obligations and/or Excess Limits Liability shall not exceed an amount equal to 200% of its limit of liability as set forth in this Agreement as respects each and every loss, each and every insured, such additional liability not to exceed the Reinsurer’s share of [the limits of liability] in the aggregate under this Agreement.

CASUALTY EXCESS OF LOSS (BROKER MARKET)

NET LOSS

12. A. The term "net loss" shall mean the actual loss incurred by the Reassured under policies covered hereunder but shall exclude allocated loss adjustment expenses. Such loss shall include sums paid in settlement of claims and suits and in satisfaction of judgments, including prejudgment interest when added to a judgment. Such loss also shall include 90% of any Losses in Excess of Policy Limits and 90% of any Extra Contractual Obligations incurred by the Reassured, the remaining 10% of which shall be retained net and unreinsured.

B. All salvages, recoveries, payments and reversals or reductions of verdicts or judgments whether recovered, received or obtained prior or subsequent to loss settlement under this Contract, including amounts recoverable under other reinsurance whether collected or not, shall be applied as if recovered, received or obtained prior to the aforesaid settlement and shall be deducted from the actual losses sustained to arrive at the amount of the net loss. Nothing in this article shall be construed to mean losses are not recoverable until the net loss to the Reassured finally has been ascertained.

C. All allocated loss adjustment expenses paid by the Reassured as a result of net losses covered hereunder shall be divided between the Reassured and the Reinsurers, without regard to the limit of this Contract, in proportion to their share of the net loss. Allocated loss adjustment expenses shall include but not be limited to: a) expenses sustained in connection with settlement and litigation of claims and suits, satisfaction of judgments, resistance to or negotiations concerning a loss (which shall include the pro rata share of the Reassured's outside employees according to the time occupied in adjusting such loss and the expenses of the Reassured's employees while diverted from their normal duties to the service of field adjustment but shall not include any salaries of officers nor normal overhead expenses of the Reassured), b) all other defense, litigation and medical cost containment expenses, whether internal or external, arising out of specific claims, c) all interest on judgments other than prejudgment interest when added to a judgment and d) expenses sustained to obtain recoveries, salvages and other reimbursements, or to secure the reversal or reduction of a verdict or judgment.

EXTRA CONTRACTUAL OBLIGATIONS

13. A. The Reinsurers shall reinsure the Reassured, within the limit of this Contract, for Extra Contractual Obligations losses. Such losses are defined as those liabilities (whether they constitute compensatory, incidental, exemplary or punitive damages) not covered under any other provision of this Contract and which arise from the handling of any claim on business covered hereunder, such liabilities arising because of, but not limited to, the following: failure by the Reassured to settle within the policy limit, or by reason of alleged or actual negligence, fraud or bad faith in rejecting an offer of settlement, in the preparation of the defense or in the trial of any action against its insured or Reassured or in the preparation or prosecution of an appeal consequent upon such action.

B. The date on which any Extra Contractual Obligation is incurred by the Reassured shall be deemed, in all circumstances, to be the date of the original accident, casualty, disaster or loss occurrence. Any loss under this Article shall be deemed to be part of the original accident, casualty, disaster or loss occurrence which gave rise to the claim by the insured under the original policy; in no event shall the Reinsurers' limit of liability for any accident, casualty, disaster or loss occurrence, including Extra Contractual Obligations, exceed the limit of the Contract.

C. However, this Article shall not apply where the loss has been incurred due to the fraud of a member of the Board of Directors, or a corporate officer of the Reassured, acting individually, or collectively or in collusion with a member of the Board of Directors, a corporate officer or a partner of any other corporation or partnership.

D. If any provision of this Article shall be rendered illegal or unenforceable by the laws, regulations or public policy of any state, such provision shall be considered void in such state, but this shall not affect the validity or enforceability of any other provision of this Article or the enforceability of such provision in any other jurisdiction.

E. Recoveries or collectibles from any other form of insurance or reinsurance which protect the Reassured against Extra Contractual Obligations, shall inure to the benefit of the Reinsurers and shall be deducted from the total amount of Extra Contractual Obligations for purposes of determining the Net Loss hereunder.

LOSSES IN EXCESS OF POLICY LIMITS

14. A. The Reinsurers shall reinsure the Reassured, within the limit of this Contract, for any loss in excess of the limit of its policy, such loss in excess of the limit having been incurred because of the failure by it to settle within the policy limit, or by reason of alleged or actual negligence, fraud or bad faith in rejecting an offer of settlement, in the preparation of the defense or in the trial of any action against its insured or Reassured or in the preparation or prosecution of an appeal consequent upon such action.

B. For the purposes of Paragraph A. of this Article, the word "loss" shall mean any amounts for which the Reassured would have been contractually liable to pay had it not been for the limit of the policy.

C. The date on which any Excess of Original Policy Limits loss is incurred by the Reassured shall be deemed, in all circumstances, to be the date of the original accident, casualty, disaster or loss occurrence.

D. However, this Article shall not apply where the loss has been incurred due to the fraud of a member of the Board of Directors, or a corporate officer of the Reassured, acting individually, or collectively or in collusion with a member of the Board of Directors, a corporate officer or a partner of any other corporation or partnership.

EXTRA CONTRACTUAL OBLIGATIONS AND EXCESS LIMITS JUDGMENTS

This Agreement will extend to cover Eighty Percent (80%) of any losses arising from claims related extra contractual obligations and/or One Hundred Percent (100%) of any losses arising from claim related excess limits judgments.

“Extra contractual obligations” as used in this Agreement will mean those liabilities not covered under any other provision of this Agreement, which arise from the handling of any claim on business covered hereunder, such liabilities arising because, of but not limited to, the following: failure by the Company to settle within the policy limit, by reason of alleged or actual negligence or bad faith in rejecting an offer of settlement, in the preparation of the defense, in the trial of any action against its insured or reinsured, or in the preparation or prosecution of an appeal consequent upon such action.

“Excess limits judgments” as used in this Agreement will mean damages payable to the Company’s insured or its assignee as a result of an action brought by the same against the Company to recover damages payable to a third party claimant in excess of the Company’s original policy limit as a result of the Company’s alleged or actual negligence or bad faith in failing to settle and/or rejecting a settlement within its policy limit, in the preparation of the defense, in the trial of any action against its insured, or in the preparation or prosecution of any appeal consequent to such action. Excess limits judgments will not include any loss suffered by the insured other than loss to a third party claimant in excess of the Company’s original policy limit.

The date on which any extra contractual obligation and/or excess limits judgment is incurred by the Company will be deemed, in all circumstances, to be the date of the original occurrence.

There will be no recovery hereunder where the extra contractual obligation or excess limits judgments loss has been incurred due to the fraud committed by a member of the Board of Directors or a corporate officer of the Company or any other employee with claims settlement authority acting individually, collectively, or in collusion with a member of the Board of Directors or a corporate officer or a partner of any other corporation, partnership, or organization involved in the defense or settlement of a claim on behalf of the Company.

Nothing in this Article will be construed to create a separate or distinct occurrence apart from the original covered occurrence that gave rise to the extra contractual obligations and/or excess limits judgment discussed in the preceding paragraphs. In no event will the total liability of the Reinsurers exceed their applicable limit of liability as set forth in the Retention and Limit Article.

PC-4

Claim Notification Provision

The Company shall promptly advise the Reinsurer of the following:

1. Any time a lawsuit is instituted against the Company wherein pleadings allege unfair claim handling on the part of the company, a violation of any insurance claim handling law, statute or regulation, or any time a claim alleges "bad faith" claim handling on the part of the Company.
2. Any time a policyholder has assigned its right under a reinsured Policy to another person or entity.
3. Any time there is a verdict in excess of policy limits or an offer of settlement in excess of policy limits otherwise covered hereunder.
4. Any time the Company has offered to settle a claim in an amount equal to the reinsured policy limit and such offer has been rejected by the plaintiff.

BRMA SAMPLE CLAUSES

BRMA 1

"COMBINED" DEFINITION FOR EXCESS OF LOSS AGREEMENTS

Combined Extra Contractual Obligations

"Extra contractual obligations" means any liability for damages, including related allocated loss adjustment expenses [and any related pre or post judgment interest,]* arising out of policies reinsured by this Agreement including any loss in excess of its policy limits, but otherwise within the terms of a policy reinsured by this Agreement, paid or payable by the Company as a result of a claim against it by its insured, which claim alleges negligence or bad faith in rejecting a settlement within policy limits, or in discharging its duty to defend or prepare the defense in the trial of a lawsuit against its insured, or in discharging its duty to prepare or prosecute an appeal consequent upon such a lawsuit. ___% of any related allocated loss adjustment expenses will be handled in accordance with the Article entitled _____.

For purposes of this definition "payable" means the existence of a judgment which the Company does not intend to appeal, or existence of a settlement offer which the Company has accepted, or when a release has been obtained by the Company as respects any extra contractual obligation.

An extra contractual obligation shall be deemed to have occurred on the same date as the loss covered under the Company's original policy and shall constitute part of the original loss. All payments by the Reinsurer to indemnify the Company for an extra contractual obligation shall be subject always to the limit, retention and other terms and conditions of this Agreement.

However, this Article shall not apply where the extra contractual obligation has been incurred due to fraud and/or criminal act(s) by a member of the Board of Directors or a corporate officer of the Company acting individually or collectively or in collusion with any individual or corporation or any other organization or party involved in the presentation, defense or settlement of any claim covered hereunder.

Recoveries, whether collectible or not, including any retentions and/or deductibles, from any form of insurance which protect the Company against any loss or liability covered under this Article shall first be applied and shall be deducted from the total amount of any extra contractual obligation.

The Company shall be indemnified in accordance with this Article to the extent permitted by applicable law.#

May be required by various state laws.

*Optional - pre and post judgment interest may be addressed elsewhere in the agreement.

BRMA 2

"COMBINED" DEFINITION FOR PROPORTIONAL AGREEMENTS

(limits recovery to agreement limit)

Combined Extra Contractual Obligations

The Company may include ___% of any extra contractual obligation in calculating the loss under this Agreement.

"Extra contractual obligations" means any liability for damages, including related allocated loss adjustment expenses [and any related pre or post judgment interest,]* arising out of policies reinsured by this Agreement including any loss in excess of its policy limits, but otherwise within the terms of a policy reinsured by this Agreement, paid or payable by the Company as a result of a claim against it by its insured, which claim alleges negligence or bad faith in rejecting a settlement within policy limits, or in discharging its duty to defend or prepare the defense in the trial of a lawsuit against its insured, or in discharging its duty to prepare or prosecute an appeal consequent upon such a lawsuit. _____% of any related allocated loss adjustment expenses will be handled in accordance with the Article entitled _____.

For purposes of this definition "payable" means the existence of a judgment which the Company does not intend to appeal, or existence of a settlement offer which the Company has accepted, or when a release has been obtained by the Company as respects any extra contractual obligation.

An extra contractual obligation shall be deemed to have occurred on the same date as the loss covered under the Company's original policy and shall constitute part of the original loss. All payments by the Reinsurer to indemnify the Company for an extra contractual obligation shall be subject always to the limit and other terms and conditions of this Agreement.

However, this Article shall not apply where the extra contractual obligation has been incurred due to fraud and/or criminal act(s) by a member of the Board of Directors or a corporate officer of the Company acting individually or collectively or in collusion with any individual or corporation or any other organization or party involved in the presentation, defense or settlement of any claim covered hereunder.

Recoveries, whether collectible or not, including any retentions and/or deductibles, from any form of insurance which protect the Company against any loss or liability covered under this Article shall be deducted first from the total amount of any extra contractual obligation in determining the amount of such extra contractual obligation.

The Company shall be indemnified in accordance with this Article to the extent permitted by applicable law.#

May be required by various state laws.

*Optional - pre and post judgment interest may be addressed elsewhere in the agreement.

BRMA 3

“COMBINED” DEFINITION FOR PROPORTIONAL AGREEMENTS
(payment in addition to limit - no limit)

Combined Extra Contractual Obligations

The Company may include ___% of any extra contractual obligation in calculating the loss under this Agreement.

"Extra contractual obligations" means any liability for damages, including related allocated loss adjustment expenses [and any related pre or post judgment interest,]* arising out of policies reinsured by this Agreement including any loss in excess of its policy limits, but otherwise within the terms of a policy reinsured by this Agreement, paid or payable by the Company as a result of a claim against it by its insured, which claim alleges negligence or bad faith in rejecting a settlement within policy limits, or in discharging its duty to defend or prepare the defense in the trial of a lawsuit against its insured, or in discharging its duty to prepare or prosecute an appeal consequent upon such a lawsuit. ___% of any related allocated loss adjustment expenses will be handled in accordance with the Article entitled _____.

For purposes of this definition “payable” means the existence of a judgment which the Company does not intend to appeal, or existence of a settlement offer which the Company has accepted, or when a release has been obtained by the Company as respects any extra contractual obligation.

An extra contractual obligation shall be deemed to have occurred on the same date as the loss covered under the Company's original policy. The Reinsurer will indemnify the Company for any extra contractual obligation without regard to the limit of this Agreement, but subject to all of the other terms and conditions of this Agreement.

However, this Article shall not apply where the extra contractual obligation has been incurred due to fraud and/or criminal act(s) by a member of the Board of Directors or a corporate officer of the Company acting individually or collectively or in collusion with any individual or corporation or any other organization or party involved in the presentation, defense or settlement of any claim covered hereunder.

Recoveries, whether collectible or not, including any retentions and/or deductibles, from any form of insurance which protect the Company against any loss or liability covered under this Article shall be deducted first from the total amount of any extra contractual obligation in determining the amount of such extra contractual obligation.

The Company shall be indemnified in accordance with this Article to the extent permitted by applicable law.#

May be required by various state laws.

*Optional - pre and post judgment interest may be addressed elsewhere in the agreement.

BRMA 4

"COMBINED" DEFINITION FOR PROPORTIONAL AGREEMENTS (payment in addition to limit, but capped)

Combined Extra Contractual Obligations

The Company may include ___% of any extra contractual obligation in calculating the loss under this Agreement.

"Extra contractual obligations" means any liability for damages, including related allocated loss adjustment expenses [and any related pre or post judgment interest,]* arising out of policies reinsured by this Agreement including any loss in excess of its policy limits, but otherwise within the terms of a policy reinsured by this Agreement, paid or payable by the Company as a result of a claim against it by its insured, which claim alleges negligence or bad faith in rejecting a settlement within policy limits, or in discharging its duty to defend or prepare the defense in the trial of a lawsuit against its insured, or in discharging its duty to prepare or prosecute an appeal consequent upon such a lawsuit. _____% of any related allocated loss adjustment expenses will be handled in accordance with the Article entitled _____.

For purposes of this definition "payable" means the existence of a judgment which the Company does not intend to appeal, or existence of a settlement offer which the Company has accepted, or when a release has been obtained by the Company as respects any extra contractual obligation.

An extra contractual obligation shall be deemed to have occurred on the same date as the loss covered under the Company's original policy. The Reinsurer will indemnify the Company for any extra contractual obligation without regard to the limit of this Agreement, but subject to all of the other terms and conditions of this Agreement. However in no event will the Reinsurer's liability for any extra contractual obligation exceed \$_____ (use dollar limit, or cession amount, or Agreement limit or multiples thereof as negotiated).

However, this Article shall not apply where the extra contractual obligation has been incurred due to fraud and/or criminal act(s) by a member of the Board of Directors or a corporate officer of the Company acting individually or collectively or in collusion with any individual or corporation or any other organization or party involved in the presentation, defense or settlement of any claim covered hereunder.

Recoveries, whether collectible or not, including any retentions and/or deductibles, from any form of insurance which protect the Company against any loss or liability covered under this Article shall be deducted first from the total amount of any extra contractual obligation.

The Company shall be indemnified in accordance with this Article to the extent permitted by applicable law.#

May be required by various state laws.

*Optional - pre and post judgment interest may be addressed elsewhere in the agreement.