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Insurance Law Alert

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In This Issue

Eleventh Circuit Rules That Insurer Cannot Be Held Vicariously Liable For Appointed Counsel's Negligence

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***– The Legal 500* 2017**

Arizona Court Rules That Excess Insurer's Obligation Does Not Arise Until Underlying Limits Are Actually Paid

An Arizona court ruled that an excess insurer had no coverage obligation until the underlying policy limits were actually paid. *Certain Underwriters at Lloyds London v. Republic Services Inc.*, No. CV 2017-005489 (Ariz. Superior Ct. Jan. 30, 2018). (Click here for full article)

Second Circuit Clarifies That Right To Privacy Of Medical Records Is Not Solely Dependent On Content Of Records

The Second Circuit vacated a district court decision rejecting a constitutional right to privacy claim based on the improper accessing of personal medical records. *Hancock v. County of Rensselaer*, 2018 WL 798471 (2d Cir. Feb. 9, 2018). (Click here for full article)

Eighth Circuit Rules That Contamination Of Landscaping Materials Does Not Constitute Covered Property Damage

The Eighth Circuit affirmed an Iowa federal district court decision holding that contamination of landscaping materials caused by defective plastic storage bags does not constitute physical injury to tangible property under a liability policy. *Decker Plastics Corp. v. West Bend Mutual Ins. Co.*, 880 F.3d 1017 (8th Cir. 2018). (Click here for full article)

Insurer's Rejection Of Proof Of Loss Started Running Of Statute Of Limitations, Says Third Circuit

The Third Circuit ruled that an insurer's rejection of a policyholder's proof of loss constituted a claim denial sufficient to start the running of the statute of limitations. *Migliaro v. Fidelity National Indem. Ins. Co.*, 880 F.3d 660 (3d Cir. 2018). (Click here for full article)

Ohio Supreme Court Rules That Statute Of Limitations On Negligent Procurement Claim Against Agent Begins To Run Upon Policy Issuance, Not Claim Denial

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The Tenth Circuit predicted that the New York Court of Appeals would find that damage caused by a subcontractor's negligence would constitute a covered occurrence under a liability policy containing a subcontractor exception. *Black & Veatch Corp. v. Aspen Ins. (UK) Ltd.*, 2018 WL 843284 (10th Cir. Feb. 13, 2018). (Click here for full article)

Oklahoma Supreme Court Upholds Attorneys' Fee Award To Policyholder In Successful Declaratory Judgment Action

The Oklahoma Supreme Court held that a policyholder is entitled to recover attorneys' fees after successful pursuit of a declaratory judgment action against its insurer. *JP Energy Mktg., LLC v. Commerce & Industry Ins. Co.*, 2018 WL 703483 (Okla. Feb. 5, 2018).
(Click here for full article)

Defense Alert:

Eleventh Circuit Rules That Insurer Cannot Be Held Vicariously Liable For Appointed Counsel's Negligence

The Eleventh Circuit ruled that even assuming that appointed counsel was negligent in defending the policyholder, the insurer cannot be held vicariously liable, so long as appointed counsel was "competent and qualified." *Kapral v. Geico Indem. Co.*, 2018 WL 509308 (11th Cir. Jan. 23, 2018).

Kapral was sued by a party injured in an automobile accident. Geico appointed counsel to represent Kapral in the suit. When judgment was issued against Kapral in an amount above policy limits, Kapral sued Geico, asserting that Geico failed to adequately defend him, among other claims. Following a trial, the district court granted Geico's motion for a directed verdict on the inadequate defense claim. The Eleventh Circuit affirmed, holding that "[u]nder Florida law, an insurer is not vicariously liable for the negligence of the attorney it retains to

defend the insured, so long as the attorney is competent and qualified." Thus, even assuming counsel was negligent, the court held that Geico could not be liable because the record established that the attorney had substantial legal experience in practicing personal injury law. The court acknowledged that governing precedent involved outside counsel, rather than staff counsel (as was the case here), but deemed that distinction immaterial. The court explained: "Nor should the result be different [based on the use of staff counsel] because under Florida law an insurer has no more right to exercise control over staff counsel's professional conduct and independent judgment than it does over outside counsel's conduct and judgment."

Excess Alert:

Arizona Court Rules That Excess Insurer's Obligation Does Not Arise Until Underlying Limits Are Actually Paid

As reported in previous Alerts, courts have addressed whether excess policies are triggered once the insured has incurred liability in excess of primary policy limits, or whether underlying limits must actually be paid out and exhausted in order for excess coverage to be implicated. *See* June 2016 Alert, Jan. 2014 Alert, June 2013 Alert, Oct. 2012 Alert. Last month, an Arizona court weighed in, ruling that an excess insurer had no coverage obligation until the underlying policy limits were actually paid. *Certain Underwriters at Lloyds London v. Republic Services Inc.*, No. CV 2017-005489 (Ariz. Superior Ct. Jan. 30, 2018). The court noted that the language of the excess policy at issue was "not 100% clear" on this requirement, but concluded that the excess insurer's position that underlying limits must be fully paid was the more reasonable interpretation of the policy language.

The excess policy required the Underwriters to "pay on behalf of the Insured excess of the Underlying Policies any claim or loss which triggers coverage under the Underlying Policies, and is not otherwise excluded." For purposes of the instant motion, the court assumed that the insured incurred losses exceeding the primary limit of $25 million and that the primary insurer had yet to pay such an amount. In finding that actual payment was required to trigger excess coverage, the court noted that other provisions of the excess policy "speak in terms of the payment of claims" by the primary insurer, thus suggesting that "payment is the key event." Although the parties disputed whether New York law or Arizona law applied, they agreed that there was no difference between those states' law on this issue of policy interpretation.

Privacy Alert:

Second Circuit Clarifies That Right To Privacy Of Medical Records Is Not Solely Dependent On Content Of Records

The Second Circuit vacated a district court decision rejecting a constitutional right to privacy claim based on the improper accessing of personal medical records. *Hancock v. County of Rensselaer*, 2018 WL 798471 (2d Cir. Feb. 9, 2018).

The complaint alleged that the personal medical records of county jail employees were secretly accessed without their consent by at least one co-worker in violation of the Due Process Clause of the Fourteenth Amendment and the Computer Fraud and Abuse Act ("CFAA"). A New York federal district court dismissed the CFAA claim on the pleadings, and later granted summary judgment to the defendants on the constitutional privacy claim. The district court concluded that the privacy claim failed because the plaintiffs did not have a "constitutionally protected interest in medical privacy because the medical conditions described in their records were insufficiently stigmatizing." The Second Circuit affirmed the dismissal of the CFAA claim but vacated the ruling as to the constitutional privacy claim.

Clarifying precedent in this context, the Second Circuit ruled that the presence of a stigmatizing condition, while relevant to the analysis, is not a threshold prerequisite to a constitutional privacy claim. The court expressly rejected the notion that "only sufficiently serious medical conditions give rise to any interest in privacy at all." Rather, the court explained, individuals have a fundamental interest in maintaining the confidentiality of medical information generally. Alleged privacy violations are evaluated by a case-specific balancing test that considers the strength of the privacy interest (based on the content of the personal information) as weighed against the government's proffered justifications for accessing that material. "The stronger the individual interest, the more compelling the government actor's reasons must be. But even the weakest privacy interests cannot be overridden by totally arbitrary or outright malicious government action." Applying this framework, the Second Circuit concluded that issues of fact exist as to why the breaches of confidentiality occurred, and thus vacated the district court's dismissal of the privacy claim. More specifically, the court noted that regardless of the content of the plaintiffs' medical records, there was likely a violation if the records were accessed for improper or malicious purposes, as was alleged here.

The right to privacy as to personal medical information was also at issue in the recently-settled matter of *Beckett v. Aetna, Inc.*, 2017 WL 3701844 (E.D. Pa. Compl. filed Aug. 28, 2017). That lawsuit alleged that Aetna "carelessly, recklessly, negligently, and impermissibly revealed HIV-related information of their current and former insureds" through postal mailings that revealed personal medical information in the envelope window. In the proposed class action settlement, Aetna agreed to pay more than $17 million and establish "best practices" to prevent future privacy violations.

Property Damage Alert:

Eighth Circuit Rules That Contamination Of Landscaping Materials Does Not Constitute Covered Property Damage

The Eighth Circuit affirmed an Iowa federal district court decision holding that contamination of landscaping materials caused by defective plastic storage bags does not constitute physical injury to tangible property under a liability policy. *Decker Plastics Corp. v. West Bend Mutual Ins. Co.*, 880 F.3d 1017 (8th Cir. 2018)

Decker, a manufacturer of plastic storage bags, was sued by a landscape supplier after it discovered that the bags were defective and deteriorated in sunlight. The deterioration caused small pieces of plastic to commingle with landscaping materials. Decker settled the lawsuit with the landscape supplier and sought coverage from West Bend. The insurer denied coverage, arguing that there was no "occurrence" under the policy. The district court agreed and granted West Bend's summary judgment motion. The Eighth Circuit reversed, ruling that deterioration of the bags was a covered occurrence and

that covered property damage (if any) was to property other than the bags. *See* Sept. 2016 Alert. On remand, the district court ruled that there was no covered property damage and that, in any event, coverage was barred by policy exclusions. The Eighth Circuit affirmed.

The court held that existence of covered property damage turned on whether there was "physical injury" to "tangible property." Noting that "the question is not free from doubt," the court concluded that the landscaping materials did not suffer physical injury. Although the landscaping materials were no longer saleable because they were contaminated with shreds of plastic from the deteriorated bags, the rock and sand were not "physically altered or destroyed." Rather, the contamination diminished only the value of the materials and thus did not trigger coverage under the policies.

Statute of Limitations Alerts:

Insurer's Rejection Of Proof Of Loss Started Running Of Statute Of Limitations, Says Third Circuit

The Third Circuit ruled that an insurer's rejection of a policyholder's proof of loss constituted a claim denial sufficient to start the running of the statute of limitations. *Migliaro v. Fidelity National Indem. Ins. Co.*, 880 F.3d 660 (3d Cir. 2018).

Migliaro sought coverage under a Standard Flood Insurance Policy for Hurricane Sandy damage. The insurer reimbursed him based on its adjuster's recommendation. Months later, Migliaro submitted a proof of loss claiming additional damage. The insurer responded with a letter entitled "Rejection of Proof of Loss," contesting the additional amount claimed, but expressly stating that "[t]his is not a denial of your claim." The notice also indicated that Migliaro could provide further documentation to support the claim, but he did not do so. Instead, nearly two years after receiving the letter, Migliaro filed suit against the insurer. (He had previously sued the insurer within one year of receiving the letter, but voluntarily dismissed that action). A New Jersey federal district court granted the insurer's summary judgment motion, finding that the suit was barred by the one-year statute of limitations set forth in the Standard Flood Insurance Policy. The Third Circuit affirmed.

The Third Circuit held that an insurer's rejection of a proof of loss is not a *per se* denial of claim. However, the court held that where, as here, the policyholder treats the rejection of proof of loss as a claim denial by filing suit after receiving the proof of loss, it should be construed as such for statute of limitations purposes. The court explained that "the very act of bringing suit signaled that, to Migliaro's mind, his claim had been denied." The court rejected the policyholder's argument that even if a rejected proof of loss could constitute a denial of the claim in some cases, the rejection letter at issue did not because it expressly stated that it was "not a denial of [the] claim." The court reasoned that the statement was "technically true at the time it was made," because the possibility of additional compensation still existed. However, "Migliaro closed the door by failing to seek an appraisal, file an amended proof of loss . . . or submit additional documentation. Instead, he sued, and in doing so acknowledged that, by virtue of the letter rejecting his proof of loss, his claim had been denied."

Ohio Supreme Court Rules That Statute Of Limitations On Negligent Procurement Claim Against Agent Begins To Run Upon Policy Issuance, Not Claim Denial

The Ohio Supreme Court ruled that negligence claims against an insurance agency accrue at policy issuance rather than when the insurer denies coverage. *LGR Realty, Inc. v. Frank & London Ins. Agency*, 2018 WL 656095 (Ohio Jan. 16, 2018).

A realty company utilized the services of an insurance agency to obtain an Errors and Omissions policy from Continental Casualty. When a claim was filed against the realty company, it sought coverage under the policy. Continental denied the claim pursuant to an exclusion. Thereafter, the realty company sued the insurance agency for negligent procurement, alleging that it negligently misrepresented the coverage provided by the policy. An Ohio trial court ruled that the action was time-barred by the applicable four-year statute of limitations. The trial court reasoned that the cause of action against the agency accrued on the date the policy went into effect, which was five years prior to the lawsuit filing. An intermediate appellate court reversed, finding that under the "delayed-damage" rule, the cause of action did not accrue until the plaintiff "suffered an injury," which occurred when Continental denied the claim for defense and indemnity. The Ohio Supreme Court reversed the appellate court decision.

Under Ohio law, the statute of limitations begins to run when "the injurious act complained of is perpetrated, although the actual injury is subsequent." One exception to this rule is the "delayed-damage" rule, which provides that "where the wrongful conduct complained of is not presently harmful, the cause of action does not accrue until actual damage occurs." The Ohio Supreme Court ruled that the "narrow circumstances" under which the delayed-damages exception would apply were not present here. The court explained that the realty company "was damaged the moment it entered into the contract and became obligated to pay a premium for a professional-liability insurance policy that was less than the coverage that it believed it would receive." In so ruling, the court emphasized that the policy specifically excluded the type of claim that the realty company believed was covered, distinguishing precedent in which the delayed-damage exception was applied to a negligent insurance procurement claim based on the lack of clarity as to the scope of coverage after consolidation of a property policy into an omnibus policy.

Faulty Workmanship Alert:

Tenth Circuit Predicts That Subcontractor's Faulty Work Would Constitute Covered Occurrence Under New York Law

The Tenth Circuit predicted that the New York Court of Appeals would find that damage caused by a subcontractor's negligence would constitute a covered occurrence under a liability policy containing a subcontractor exception. *Black & Veatch Corp. v. Aspen Ins. (UK) Ltd.*, 2018 WL 843284 (10th Cir. Feb. 13, 2018).

The dispute centered on whether Aspen Insurance was obligated to reimburse Black & Veatch ("B&V"), an engineering and construction company, for the costs it incurred due to damaged reactor equipment constructed by one of its subcontractors. A Kansas federal district court ruled that there was no coverage under Aspen's policy, reasoning that there was no occurrence because the only damages involved were to B&V's own work product. The Tenth Circuit vacated the district court's

determination and remanded the matter for further consideration.

The Tenth Circuit held that the damage to the reactors constituted an occurrence for two reasons. First, B&V did not expect or intend the subcontractor to cause damage. Second, there was damage to third-party property because the reactors were the property of another subcontractor (American Electric Power) that had also been hired to work on them. The court rejected the argument that American Electric Power's listing as an Additional Insured under the policy meant that the reactors were not third-party property.

In addition, the court ruled that its occurrence holding comports with New York's rule against surplusage. The court explained that if subcontractor-related damage was not a covered occurrence, several policy provisions would be rendered meaningless. In particular, the court reasoned that the "subcontractor exception" to the "Your Work" exclusion would be rendered superfluous if the initial grant of occurrence-based coverage did not encompass property damage caused by a subcontractor's negligence.

The court distinguished New York appellate case law in which courts found no coverage for similar claims, citing several distinctions, including the following: (1) the policies at issue did not include a subcontractor exception; (2) the policies at issue predated the 1986 standard form revisions; and (3) the underlying claims alleged faulty work by a contractor, rather than a subcontractor. Finally, the court noted that state supreme courts that have considered this issue in recent years have reached "near unanimity" that property damage caused by subcontractor negligence can be a covered occurrence under a liability policy issued to a contractor.

Attorneys' Fee Alert:

Oklahoma Supreme Court Upholds Attorneys' Fee Award To Policyholder In Successful Declaratory Judgment Action

Ruling on a matter of first impression under Oklahoma law, the Oklahoma Supreme Court held that a policyholder is entitled to an attorneys' fee award after it has successfully pursued a declaratory judgment action against its insurer. *JP Energy Mktg., LLC v. Commerce & Industry Ins. Co.*, 2018 WL 703483 (Okla. Feb. 5, 2018).

The policyholder sought declaratory relief from its insurers after they denied coverage and a defense in an underlying action. An Oklahoma trial court granted the policyholder's summary judgment motion and an appellate court affirmed. Thereafter, the policyholder sought attorneys' fees and costs.

Oklahoma statutory law provides for an attorneys' fee award to a "prevailing party" in an insurance dispute. Okla. Stat. tit. 36. § 3629 (2011). Citing federal court decisions applying Oklahoma law, the Oklahoma Supreme Court concluded that section 3629 applies to prevailing policyholders in declaratory judgment actions, and is not limited to first-party actions where the insurer has denied coverage for a claim. The court also ruled that the policyholder satisfied the statutory requirement for submitting a "proof of loss" by issuing a request for defense and indemnity.

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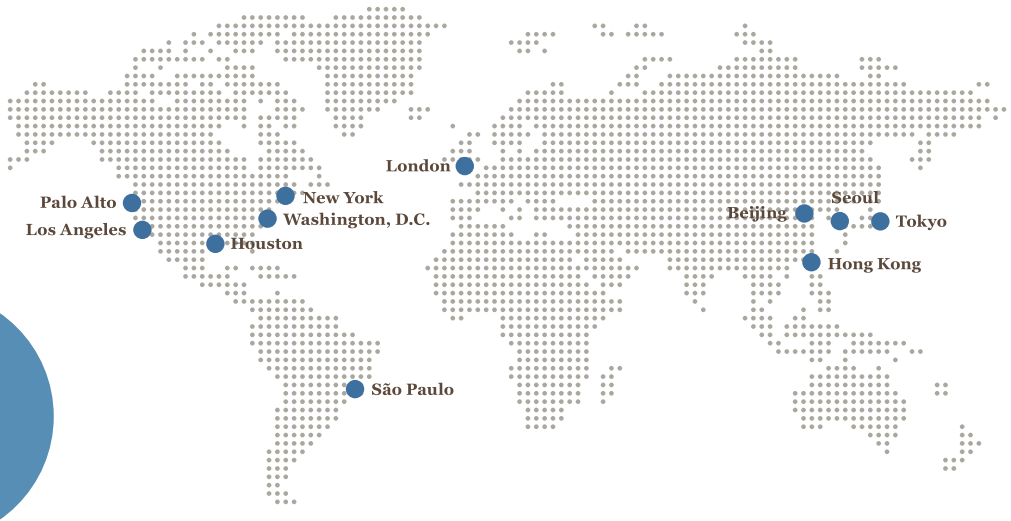

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