Simpson Thacher

Insurance Law Alert

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The California Supreme Court ruled that an insurer must defend a suit alleging negligent hiring and supervision of an employee who intentionally injured a third party, finding that such claims allege an "occurrence" under a general liability policy. *Liberty Surplus Ins. Corp. v. Ledesma & Meyer Construction Co., Inc.*, 418 P.3d 400 (Cal. 2018). (Click here for full article)

"Overall they are excellent. Their work is timely, well thought out and strategic."

***– Chambers USA* 2018 (quoting a client)**

Finding "Arising Out Of" Ambiguous, First Circuit Rules That Insurer Must Defend Cosby Defamation Suit

The First Circuit ruled that that an insurer was obligated to defend defamation claims related to sexual misconduct allegations because a sexual misconduct exclusion was ambiguous. *AIG Prop. Cas. Co. v. Cosby*, 2018 WL 2730762 (1st Cir. June 7, 2018). (Click here for full article)

Defending Insurer May Sue Insured's Appointed Counsel For Malpractice, Says South Carolina Supreme Court

Answering a certified question, the South Carolina Supreme Court ruled that an insurer may bring a direct malpractice action against counsel hired to represent its insured. *Sentry Select Ins. Co. v. Maybank Law Firm, LLC*, 2018 WL 2423694 (S.C. May 30, 2018). (Click here for full article)

Arizona Appellate Court Rules That Injuries Caused By Several Independent Acts Are A Single Occurrence

An Arizona appellate court ruled that under applicable policy language an accident caused by several independent acts is a single occurrence. *Cincinnati Indem. Co. v. Southwestern Line Constructors Joint Apprenticeship & Training Program*, 2018 WL 2440627 (Ariz. App. May 31, 2018). (Click here for full article)

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Director Acting In Multiple Capacities Not Entitled To D&O Coverage, Says North Dakota Court

A North Dakota federal district court ruled that a director is not entitled to coverage under a directors and officers policy because he was not alleged to have acted solely in his capacity as a director. *Security National Ins. Co. v. H.O.M.E., Inc.*, 2018 WL 2325406 (D.N.D. May 18, 2018). (Click here for full article)

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A Massachusetts federal district court ruled that a statutory claim against an insurer for unfair and deceptive business practices accrues no later than the date of the last alleged settlement misconduct. *Hong v. Northland Ins. Co.*, 2018 WL 2435196 (D. Mass. May 30, 2018). (Click here for full article)

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The Colorado Supreme Court ruled that a statutory claim for the unreasonable delay or denial of insurance benefits is not subject to the one-year statute of limitations applicable to actions brought under any penal statute. *Rooftop Restoration, Inc. v. American Family Mutual Ins. Co.*, 2018 WL 2407591 (Colo. May 29, 2018). (Click here for full article)

Simpson Thacher News Alerts

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Coverage Alert:

California Supreme Court Rules That Insurer Must Defend Negligent Hiring Claim Arising Out Of Employee's Intentional Acts

The California Supreme Court ruled that an insurer must defend a suit alleging negligent hiring and supervision of an employee who intentionally injured a third party, finding that such claims allege an "occurrence" under a general liability policy. *Liberty Surplus Ins. Corp. v. Ledesma & Meyer Construction Co., Inc.*, 418 P.3d 400 (Cal. 2018).

A construction company ("L&M") was hired to manage a school building project. A student sued L&M, alleging sexual abuse by a project supervisor. L&M's insurers defended the negligent hiring and supervision claims under a reservation of rights and sought a declaration of no coverage. A California federal district court granted the insurers' summary judgment motion, finding that the alleged injury was not caused by an "occurrence" because the injury-causing event was intentional molestation. The district court reasoned that L&M's alleged negligent hiring and supervision were "too attenuated" from the injury to establish causation. L&M appealed, and the Ninth Circuit sought the California Supreme Court's guidance.

The California Supreme Court ruled that the insurers were obligated to defend the suit because a potential for coverage exists, notwithstanding the employee's alleged intentional acts. The court rejected the district court's causation analysis, holding that under California law, causation is established so long as the defendant's conduct is a "substantial factor" in causing injury. Applying this framework, the California Supreme Court reasoned that "a finder of fact could conclude that the causal connection between L&M's alleged negligence and the injury inflicted . . . was close enough to justify the imposition of liability on L&M." Additionally, the court noted that in deciding whether underlying claims allege an accident under an insurance policy, the relevant viewpoint is that of the insured; thus, the supervisor's intentional conduct may be deemed an unexpected consequence of L&M's independent act of negligent hiring.

As discussed in last month's Alert, the Wisconsin Supreme Court recently ruled that a liability policy does not cover negligent supervision claims that are based solely on an employee's intentional conduct.

Defense Alerts:

Finding "Arising Out Of" Ambiguous, First Circuit Rules That Insurer Must Defend Cosby Defamation Suit

Our November 2016 Alert reported on a Massachusetts federal district court's holding that that an insurer was obligated to defend defamation claims related to sexual misconduct allegations because a sexual misconduct exclusion was ambiguous. *AIG Prop. Cas. Co. v. Green*, 2016 WL 6637694 (D. Mass. Nov. 8, 2016). This month, the First Circuit affirmed. *AIG Prop. Cas. Co. v. Cosby*, 2018 WL 2730762 (1st Cir. June 7, 2018).

The coverage dispute arose out of several lawsuits against Bill Cosby alleging defamation and intentional infliction of emotional distress. The plaintiffs claimed that Cosby made public statements that injured their reputations in response to their allegations of assault and rape. AIG sought a declaration that it had no duty to defend or indemnify the suits, arguing that the claims fell within a sexual misconduct exclusion, which bars coverage for personal injury "arising out of any actual, alleged, or threatened . . . sexual molestation, misconduct, or harassment." The court disagreed and denied AIG's summary judgment motion and granted Cosby's motion in part.

Although Massachusetts law has not clearly defined the scope of the phrase "arising out

of," the First Circuit held that it indicates a wider range of causation than proximate causation, but requires a "sufficiently close relationship" between the injury and relevant event. Here, AIG argued that the defamation claims were "inextricably intertwined" with the excluded sexual assault allegations so as to trigger the sexual misconduct exclusion. In contrast, Cosby maintained that the causal link between the excluded conduct and the defamation claims was too attenuated to implicate the exclusion.

Noting that there was no "easy answer" to the question, the court concluded that the exclusion was ambiguous in light of the policy as a whole. In particular, the court reasoned that another, more broadly-worded sexual misconduct exclusion (relating to Board Directors and Trustees) mitigated in favor of finding ambiguity because that exclusion contained more expansive exclusionary language (*e.g.*, "arising out of or in any way involving, directly or indirectly, any alleged sexual misconduct"). The court emphasized that "arising out of" is not inherently ambiguous under Massachusetts law. It also cautioned that its holding "is confined to this case where the ambiguity question is close to begin with and where another sexual-misconduct exclusion is worded more broadly."

Defending Insurer May Sue Insured's Appointed Counsel For Malpractice, Says South Carolina Supreme Court

Answering a certified question, the South Carolina Supreme Court ruled that an insurer may bring a direct malpractice action against counsel hired to represent its insured. *Sentry Select Ins. Co. v. Maybank Law Firm, LLC*, 2018 WL 2423694 (S.C. May 30, 2018).

An insurer hired attorney Roy Maybank to defend its insured in a personal injury suit. When Maybank failed to timely answer requests to admit, the insurer settled the suit for an amount larger than originally anticipated based on the likelihood of an adverse ruling. It then sued Maybank alleging malpractice.

The South Carolina Supreme Court ruled that the insurer's malpractice action was viable, notwithstanding the absence of an attorney-client relationship between counsel and the insurer. The court explained that although counsel owes a fiduciary duty only to the insured, the "unique position" of the insurer in this context mitigates in favor of allowing a malpractice claim. In so ruling, the court emphasized that appointed counsel owes no separate duty to the insurer and that South Carolina does not recognize a "dual attorney-client relationship."

The court limited its holding in several important respects. First, an insurer may recover for counsel's breach of his duty only where the insurer proves by clear and convincing evidence that the breach proximately caused damage to the insurer. Second, there can be no liability if the interests of the client "are the slightest bit inconsistent with the insurer's interests." Potential inconsistencies are to be evaluated on a case-by-case basis.

As the court noted, the majority of states that have considered this issue have similarly allowed an insurer to pursue a malpractice claim against appointed counsel.

Number Of Occurrence Alerts:

Arizona Appellate Court Rules That Injuries Caused By Several Independent Acts Are A Single Occurrence

An Arizona appellate court ruled that under applicable policy language an accident caused by several independent acts is a single occurrence. *Cincinnati Indem. Co. v. Southwestern Line Constructors Joint Apprenticeship & Training Program*, 2018 WL 2440627 (Ariz. App. May 31, 2018).

Two workers were injured when a utility pole broke while they were working on it. They sued the construction company and ultimately reached a settlement for the limits of the company's liability policy. The policy contained a $1 million per-occurrence limit and a $2 million aggregate limit. The insurer sought a declaration that the employees' injuries arose from a single occurrence and its obligation was therefore capped by the $1 million limit. An Arizona trial court agreed, and the appellate court affirmed.

The policy defined "occurrence" as "an accident, including continuous or repeated exposure to substantially the same general harmful conditions." The appellate court ruled that there was only one occurrence because the injuries resulted from a single accident (*i.e.*, the collapse of the utility pole). The employees argued that under Arizona law, the number of occurrences is determined by the number of allegedly negligent acts, and that here, at least five separate acts of negligence caused the pole to break, including the use of wooden poles, the failure to perform inspections and the lack of secondary support or supervision. The court rejected this assertion, explaining that a "negligent act" analysis is appropriate only where policy language defines "occurrence" in relation to incidents, acts or omissions that result in injury. Where, as here, occurrence is defined as an "accident" (rather than the precipitating cause of the accident), the number of antecedent negligent acts is irrelevant.

Louisiana Appellate Court Rules That Multiple-Impact Collision Was A Single Occurrence

A Louisiana appellate court ruled that a multiple-impact collision that injured several individuals was a single occurrence for insurance coverage purposes. *Lloyd's Syndicate 1861 v. Darwin National Assurance Co.*, 2018 WL 2327719 (La. Ct. App. May 23, 2018).

The coverage dispute arose out of an automobile accident that spanned a nearly one mile distance from initial to final impact. During the course of the incident, the insured driver struck four different vehicles at a high rate of speed, resulting in numerous injuries. The parties disputed whether the incident constituted one occurrence or multiple occurrences under Louisiana law. A trial court ruled that the accident was a single occurrence, subject to a single policy limit under the driver's policy. The appellate court affirmed.

Addressing this matter of first impression under Louisiana law, the appellate court applied a causation test under which "an insured tortfeasor will be limited to a single policy limit for a single accident in situations where all of the successive impacts are the result of the same cause as the initial impact" unless there are "new and distinct, intervening cause[s]." The court expressly rejected a "time and space" test under which accidents separated by time and space are considered multiple occurrences. However, the court noted that factors relating to time and space are not irrelevant to the causation test; rather, a court may consider a time lapse or spatial range in evaluating whether injuries are the result of a single occurance or multiple occurrences. Applying this framework to the factual record, the court concluded that the successive collisions were the result of a single cause without any intervening acts of negligence between impacts.

Professional Services Alert:

Ninth Circuit Enforces "Professional Services" Exclusion With Respect To *Qui Tam* Claim

The Ninth Circuit ruled that a professional services exclusion in a directors and officers liability policy bars coverage for a *qui tam* action against an insured company. *HotChalk, Inc. v. Scottsdale Ins. Co.*, 2018 WL 2473474 (9th Cir. June 4, 2018).

HotChalk, a company that provides online marketing and technology services to universities, was sued by former employees in a *qui tam* action. The suit alleged that HotChalk violated federal regulations concerning the enrollment of students who received federal financial aid, causing both the students and universities with which HotChalk partnered to submit false claims to the government. Scottsdale Insurance denied coverage and refused to defend the suit based on the policy's professional services exclusion. In ensuing litigation, a California district court granted Scottsdale's summary

judgment motion. The Ninth Circuit affirmed, ruling that the allegations in the *qui tam* suit against HotChalk "arose out of" the rendering of professional services because they involved HotChalk's professional services of recruiting students and providing support services to the universities.

D&O Alert:

Director Acting In Multiple Capacities Not Entitled To D&O Coverage, Says North Dakota Court

Addressing a matter of first impression under North Dakota law, a North Dakota federal district court ruled that a director is not entitled to coverage under a directors and officers policy because he was not alleged to have acted solely in his capacity as a director. *Security National Ins. Co. v. H.O.M.E., Inc.*, 2018 WL 2325406 (D.N.D. May 18, 2018).

Lauris Molbert, president and CEO of H.O.M.E., sued his siblings in connection with a stock purchase agreement. The siblings alleged several counterclaims against Molbert, including breach of fiduciary duty and violation of state statutory law. Security National, H.O.M.E.'s D&O insurer, denied coverage for the counterclaims. In ensuing coverage litigation, the court granted Security National's summary judgment motion, finding no coverage under the policy.

The court ruled that the siblings' counterclaims were not covered because the allegations did not assert that Molbert was acting "solely in [his] capacity as director" as required by the policy. The court reasoned that the counterclaims "inextricably intertwine" Molbert's role as lawyer with his role as director because they allege that his legal work directly facilitated the breach of duties that he owed the company as director. The court rejected Molbert's assertion that he acted solely in his capacity as director with respect to at least some claims (*i.e.*, the statutory claims that apply only to directors and officers), finding that the counterclaims "not only allege[] he simultaneously acted in noncovered capacities during all relevant times but also that these capacities aided the breach of his fiduciary duties as director and officer."

Alternatively, the court ruled that even if there was ambiguity with respect to coverage under the policy, the counterclaims would nonetheless be excluded under the insured vs. insured exclusion because the siblings were "insureds" under the policy. The court rejected H.O.M.E.'s contention that the exclusion ought not apply because the underlying litigation did not raise concerns about collusion among insureds.

Arbitration Alert:

Second Circuit Reverses District Court's Vacatur Of Reinsurance Arbitration Award Based On Arbitrator Partiality

Our April 2017 Alert reported on a New York federal district court decision vacating an arbitration award in a reinsurance dispute based on an arbitrator's failure to disclose his relationship with a party to the dispute. *Certain Underwriting Members at Lloyd's of London v. Insurance Co. of the Americas*, 2017 WL 5508781 (S.D.N.Y. Mar. 31, 2017). This month, the Second Circuit vacated the decision, finding that the district court applied an incorrect standard for evaluating the partiality of a party-appointed arbitrator. *Certain Underwriting Members of Lloyds of London v. State of Florida, Dep't of Fin. Svs., as Receiver for Ins. Co. of the Americas*, 2018 WL 2727492 (2d Cir. June 7, 2018).

ICA entered into reinsurance treaties with certain Lloyd's Underwriters. When a dispute over a reinsurance claim arose, ICA demanded arbitration and designated Alex Campos as its arbitrator. Each arbitration panel member made affirmative disclosures regarding their relationships with the parties and individuals involved in the dispute. Campos indicated that he had no personal relationship with any party or any

business relationship with ICA. At the end of arbitration, the panel issued an award in ICA's favor. The Underwriters moved to vacate the award based on Campos' evident partiality. The district court granted the motion, concluding that the Underwriters had established evident partiality by clear and convincing evidence based on Campos' failure to disclose his extensive business relationships with ICA and individuals associated with ICA.

The Second Circuit disagreed, holding that a party seeking to vacate an award under the Federal Arbitration Act must sustain a high burden to prove evident partiality on the part of a party-appointed arbitrator. Noting that party-appointed arbitrators are "expected to espouse the view or perspective of the appointing party," the court held that evident partiality in this context requires a heightened showing that the relationship violates the contractual requirement of disinterestedness, or it prejudicially affects the award. As the court noted, several other circuit courts have concluded that the disclosure requirements for neutral arbitrators/umpires do not extend to party-appointed arbitrators.

The Second Circuit remanded the matter for a determination as to whether the Underwriters have shown by clear and convincing evidence that Campos' omissions violated the contractual requirement of "disinterestedness" or had a prejudicial impact on the award.

Statute Of Limitations Alerts:

Massachusetts Court Rules That Unfair Practices Claim Accrues At Last Settlement Activity, Not Adverse Judgment

A Massachusetts federal district court ruled that a statutory claim against an insurer for unfair and deceptive business practices accrues no later than the date of the last alleged settlement misconduct. *Hong v. Northland Ins. Co.*, 2018 WL 2435196 (D. Mass. May 30, 2018).

In November 2017, Hong sued his insurer for unfair and deceptive practices under Massachusetts statutory law (Mass. Gen. Laws ch. 93A, § 9). The complaint alleged that in September 2013, the insurer withdrew a $4,000 settlement offer and that in November 2013, a trial verdict was entered against the insurer in the amount of nearly $60,000. The insurer argued that the statutory claim was time-barred under the applicable four-year statute of limitations. The court agreed.

The court held that the claim accrued no later than September 2013, the last date of settlement activity. The court stated: "The injury alleged here is the failure to offer a reasonable settlement under the circumstances. This was fully known as of September 24, 2013 when the defendant insurer rescinded its $4,000 offer." The court rejected Hong's assertion that the claim did not accrue until the adverse judgment was entered against the insurer, noting that the statute of limitations begins when actionable injury or harm occurs, which in this case, was the rescinding of the settlement offer.

Colorado Supreme Court Finds That Claim For Unreasonable Benefits Delay Or Denial Is Not Subject To One-Year Limitations Period

Answering a certified question, the Colorado Supreme Court ruled that a statutory claim for the unreasonable delay or denial of insurance benefits is not subject to the one-year statute of limitations applicable to actions brought under any penal statute. *Rooftop Restoration, Inc. v. American Family Mutual Ins. Co.*, 2018 WL 2407591 (Colo. May 29, 2018).

A contractor, as assignee of benefits under a homeowners' policy, alleged several causes of action against an insurer, including a statutory claim based on the unreasonable delay or denial of policy benefits. *See* Section

10-3-1116, C.R.S. (2017). The insurer argued that the claim was time-barred under the one-year statute of limitations set forth in section 13-80-103(1)(d), C.R.S. (2017), which applies to "all actions for any penalty or forfeiture of any penal statutes." The court disagreed, finding that the denial of insurance benefits statute was not "penal" under Colorado law.

The court declined to apply the three-part test previously adopted by the Colorado Supreme Court in evaluating the "penal" nature of a statute. *See Kruse v. McKenna*, 178 P.3d 1198 (Colo. 2008). The court stated that "if the legislature even implicitly indicates that a statute is not penal for the purposes of identifying the correct statute of limitations, then our judicially created test must yield to the intent of the legislature." The court inferred that the legislature did not intend to make section 10-3-1116 penal based on an accrual statute, 13-80-108, which provides that a cause of action for penalties accrues "when the determination of overpayment or delinquency for which such penalties are assessed is no longer subject to appeal."

The court did not specify the applicable statute of limitations and remanded the matter for further proceedings.

Simpson Thacher News Alerts

Simpson Thacher has been honored by the *New York Law Journal* as its 2018 Litigation Department of the Year in the category of Insurance. The publication selected Simpson Thacher based on client feedback, impressive victories and involvement in important insurance and reinsurance-related litigation.

Legal 500 has ranked Simpson Thacher as a leading law firm in the United States. The Firm was recognized in 44 practice areas, including in the field of Insurance: Advice to Insurers.

Mary Beth Forshaw was named "Best in Insurance and Reinsurance" at the *Euromoney* Legal Media Group Americas Women in Business Law Awards 2018.

Deborah Stein recently spoke at the Practising Law Institute's "Insurance Coverage Litigation – Insurer and Policyholder Perspectives" webinar about litigation strategies and best practices in insurance matters.

Elisa Alcabes spoke at the New York State Bar Association's Insurance Coverage Update: A Glimpse Forward and A Glance Back CLE last month in New York City. Elisa participated on a panel titled "Excess Coverage: Umbrella v. Follow-Form, Obligations between Primary and Excess; Reporting to Excess; Claims in Excess of Limits; and Burning Limits," which discussed excess and umbrella insurance coverage issues and recent noteworthy decisions.

Simpson Thacher

Simpson Thacher has been an international leader in the practice of insurance and reinsurance law for more than a quarter of a century. Our insurance litigation team practices worldwide.

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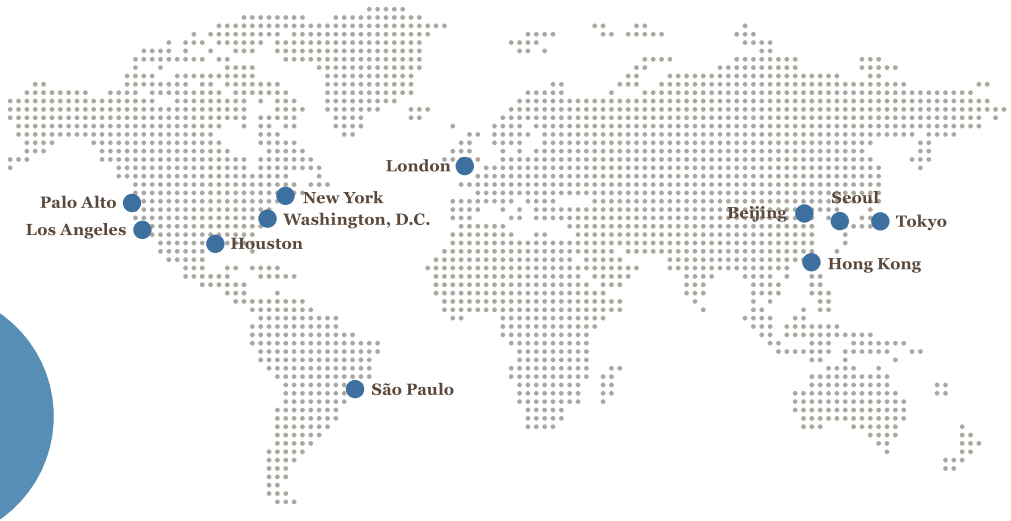

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