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Insurance Law Alert

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***– Chambers USA* 2020 (quoting a client)**

Insurer's Failure To Reference Specific Exclusion In Reservation Of Rights Rendered It Deficient, Says Pennsylvania Court

Reversing a lower court, the Superior Court of Pennsylvania ruled that an insurer's reservation of rights was deficient because it failed to reference a specific exclusion that would have precluded coverage. *Selective Way Ins. Co. v. MAK Services, Inc.*, 2020 WL 1973964 (Pa. Super. Ct. Apr. 24, 2020). (Click here for full article)

Ohio Supreme Court Rejects "All Sums" Allocation For Discrete Injury Claims

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The Pennsylvania Supreme Court ruled that an insurer was obligated to defend a personal injury suit arising out of a shooting that occurred in the midst of a murder-suicide, reasoning that the policyholder did not necessarily expect or intend to cause the resulting bystander injuries. *Erie Ins. Exch. v. Moore*, 2020 WL 1932642 (Pa. Apr. 22, 2020). (Click here for full article)

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The New York Court of Appeals ruled that an arbitration panel acted within the bounds of its authority in reconsidering a "Partial Final Award" in an arbitration proceeding. *American Int'l Specialty Lines Ins. Co. v. Allied Capital Corp.*, 2020 WL 2066743 (N.Y. Apr. 30, 2020). (Click here for full article)

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Reinsurance Alert:

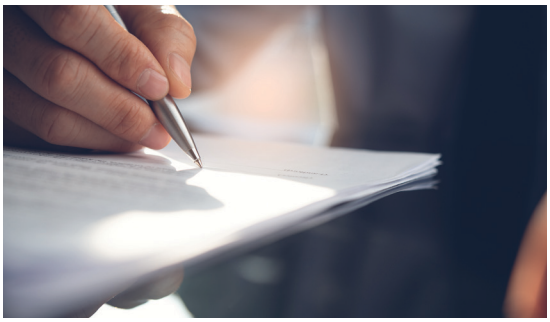
Reversing Jury Verdict, Second Circuit Rules That Reinsurer's Refusal To Indemnify Settlement Was Not Breach Of Contract

The Second Circuit reversed a jury verdict and ruled that a reinsurer did not breach its obligations under reinsurance contracts by refusing to indemnify a ceding insurer's settlement. *Utica Mut. Ins. Co. v. Fireman's Fund Ins. Co.*, 2020 WL 2047431 (2d Cir. Apr. 28, 2020).

Fireman's Fund issued several reinsurance contracts to Utica, each reinsuring umbrella policies that Utica had issued to Goulds Pump, Inc. The reinsurance certificates stated that Fireman's Fund's liability followed Utica's liability pursuant to the umbrella policies. The umbrella policies, in turn, provided that Utica was liable "for the ultimate net loss resulting from any one occurrence in excess of . . . the amounts of the applicable limits of liability of the underlying insurance as stated in the Schedule of Underlying Insurance Policies." The underlying insurance for Utica's umbrella policies were primary policies that Utica had also issued to Goulds.

Utica and Goulds disputed the extent of coverage available for asbestos bodily injury claims brought against Goulds, including whether Goulds' primary policies included aggregate limits for bodily injury claims. Utica and Goulds ultimately stipulated that each primary policy contained an aggregate limit for bodily injury claims that had been exhausted and that Utica's umbrella policies would therefore provide coverage. Thereafter, Utica sought to recover reinsurance from Fireman's Fund in the amounts that Utica had paid out under the umbrella policies. In doing so, Utica relied upon a "follow the settlements" clause in the reinsurance contracts, arguing that it bound the reinsurer to all good faith, reasonable settlements within the terms of the policies, including Utica's settlement-related stipulation as to the exhaustion of the primary policies. Fireman's Fund denied liability, arguing that the umbrella policies were not triggered until the bodily injury losses exceeded any limits specified in the underlying schedules, which had not occurred. That matter proceeded to a trial, in which a jury issued judgment in Utica's favor.

The Second Circuit reversed the verdict, ruling as a matter of law that Fireman's Fund had no obligation to pay for losses that were not covered by the umbrella policies. The court explained that the umbrella policies only covered losses that exceeded the limits stated in the schedules of underlying insurance. In referencing the primary policies underlying Utica's umbrella policies, those schedules did not list any aggregate limits applicable to bodily injury claims (and instead only provided aggregate limits for property damage claims). On this basis, the court found that Fireman's Fund had no contractual duty to pay for the bodily injury losses. The court rejected Utica's contention that the schedules did not need to list aggregate limits for bodily injury claims because they included per-occurrence limits, finding that assertion unsupported by case law or principles of policy interpretation.



In addition, the court rejected Utica's argument that Fireman's Fund was nevertheless obligated by the follow the settlements clauses to accept Utica's interpretation of when the umbrella policies were required to respond to claims, as set forth in the underlying settlement with Goulds. The court explained that follow the settlements does not override the terms of the reinsurance policies. Where such terms expressly limit coverage, follow the settlements cannot be used to vacate those limitations. The court stated: "a reinsurer cannot be held accountable for an allocation that is contrary to the express language of the reinsurance policy." The court further noted that although follow the settlements prohibits *de novo* review of a cedent's settlement and allocation decisions, it does not insulate a cedent from application of unambiguous policy terms.

Reservation Of Rights Alert:

Insurer's Failure To Reference Specific Exclusion In Reservation Of Rights Rendered It Deficient, Says Pennsylvania Court

Reversing a lower court, the Superior Court of Pennsylvania ruled that an insurer's reservation of rights ("ROR") was deficient because it failed to reference a specific exclusion that would have precluded coverage. *Selective Way Ins. Co. v. MAK Services, Inc.*, 2020 WL 1973964 (Pa. Super. Ct. Apr. 24, 2020).

Selective Way issued a liability policy to MAK Services, a snow removal company. When MAK was named as a defendant in a personal injury suit, Selective Way agreed to defend pursuant to an ROR. The ROR did not reference an exclusion that barred coverage for all injuries arising out of snow or ice removal. Approximately eighteen months after assuming MAK's defense, Selective Way sought a declaration that it owed no duty to defend or indemnify based on the snow and ice removal exclusion. A Pennsylvania trial court granted Selective Way's summary judgment motion, rejecting MAK's assertion that the insurer was estopped from raising the exclusion. The appellate court reversed.

The appellate court ruled that Selective Way's ROR had failed to preserve the snow and ice removal exclusion. The ROR stated that the underlying claims were "potentially covered" and that Selective Way generally reserved all rights under applicable law and all issues "that may become relevant as this matter continues to develop." Deeming this language insufficient to preclude estoppel, the court stated:

> While the language in Selective Way's letter may have sufficiently apprised MAK Services that future exigencies might affect coverage, it provided no notice whatsoever of the existing coverage issue appearing on the face of the Policy, *i.e.*, the snow and ice removal exclusion. Any complete review of the Policy would have immediately revealed the existence of this exclusion. Such a revelation which would have vitiated any obligation that Selective Way had to defend or indemnify MAK Services with equal speed. Instead, the boilerplate language relied upon by Selective Way obfuscated this absolute defense to coverage, and caused MAK Services to reach the reasonable conclusion there was no pressing need to secure back-up counsel.

Based on the length of the delay, the court also concluded that prejudice to MAK could fairly be presumed. Importantly, the court noted that Pennsylvania law does not require an insurer to list every potential defense in an ROR, but that "some level of specificity is necessary."

Allocation Alert:

Ohio Supreme Court Rejects "All Sums" Allocation For Discrete Injury Claims

The Supreme Court of Ohio held that damage for which liability was sought that occurred at a discernible time should be allocated to specific policy periods based on actual damage. *Lubrizol Advanced Materials, Inc. v. Nat'l Union Fire Ins. Co. of Pittsburgh, Pa*, 2020 WL 1943212 (Ohio Apr. 23, 2020). In doing so, the court rejected application of "all sums" or pro rata approaches to allocation.

Between 2001 and 2008, Lubrizol sold allegedly defective resin that was used in plumbing materials and resulted in property damage. Lubrizol argued that under Ohio law, each of its insurance policies issued between 2001 and 2008 was subject to "joint and several liability," such that Lubrizol could recover for the resin claims under the

policy of its choice. In contrast, National Union claimed that "all sums" allocation was inappropriate in light of policy language requiring the Insurer to pay "those sums" that Lubrizol was obligated to pay. National Union also argued that Ohio precedent applying "all sums" allocation was inapposite because those cases involved continuous and indivisible harm or damage, whereas the resin claims involved discrete harm that triggered coverage at individual, discernable points in time.

The court declined to "engage in a hypertechnical grammar analysis to determine whether the phrase 'those sums' is always more limited than 'all sums' and would always lead to a different allocation." The court also left open the possibility that Lubrizol could establish that the harm was progressive and continuous. Nonetheless, the court concluded that "all sums" allocation under which Lubrizol could select the policy under which it would receive coverage was unwarranted because the timing of damage was "known or knowable," based on production and sale dates and dates of damage. The court explained that under this scenario, the operative policy language requires injury or damage "during the policy period." The court therefore concluded that coverage is determined by reference to specific policy periods during which actual damage occurred.

Duty To Defend Alerts:

Pennsylvania Supreme Court Rules That Insurer Must Defend Personal Injury Suit Arising Out Of Shooting During Murder-Suicide

Previous Alerts have discussed decisions that address whether injuries or damage caused by gun shootings give rise to insurance coverage. *See* March 2020 Alert; April 2018 Alert. Last month, the Pennsylvania Supreme Court ruled that an insurer was obligated to defend a personal injury suit arising out of a shooting that occurred in the midst of a murder-suicide, reasoning that the policyholder did not necessarily expect or intend to cause the resulting bystander injuries. *Erie Ins. Exch. v. Moore*, 2020 WL 1932642 (Pa. Apr. 22, 2020).

The coverage dispute arose out of a murder-suicide. A former husband broke into the home of his ex-wife and shot and killed her. Before the former husband took his own life, the boyfriend of the ex-wife arrived on the scene. A fight ensued between the two men, during which the former husband's gun was fired several times. The boyfriend was seriously injured and sued the former husband's estate. The estate sought coverage from Erie under homeowners' and catastrophe policies, both of which defined "occurrence" as "an accident" and which excluded injury or damage "expected or intended by anyone we protect," including injury "different than what was expected or intended" in "degree, kind or quality."

A trial court granted Erie's summary judgment motion, ruling that the insurer had no duty to defend because the injuries could not be deemed "accidental" and were the result of deliberate conduct. An intermediate court reversed, noting that "not all injuries from gun violence are intentional" and finding that the underlying allegations "fairly portray a situation in which injury may have been inflicted unintentionally." The Supreme Court affirmed.

The Pennsylvania Supreme Court reasoned that the complaint, taken as true and liberally construed, alleged an accidental shooting as to the boyfriend. The complaint alleged that there was a sudden struggle between the men, in which the former husband was acting "crazy" and "incoherent." Further, the complaint asserted that he "negligently, carelessly and recklessly caused the weapon to be fired." The court rejected the contention that the allegations of negligence were "artful pleading" designed to invoke insurance coverage. The court distinguished cases involving conduct that was clearly intentional (even if couched in allegations of negligence) and caused unintended injuries, and which did not trigger an insurer's defense obligations. Here, the court explained, the initial conduct itself was allegedly accidental and/or negligent.

Texas Supreme Court Adopts Fraud Exception To Eight-Corners Rule

The Supreme Court of Texas adopted an exception to the eight-corners rule, ruling that courts may consider extrinsic evidence regarding whether the insured colluded with a third party in order to secure coverage that would otherwise not exist. *Loya Ins. Co. v. Avalos*, 2020 WL 2089752 (Tex. May 1, 2020).

Loya issued an automobile policy to Karla Guevara that expressly excluded coverage for her husband, Rodolfo Flores. An accident occurred while Flores was driving the car, but all parties involved agreed to tell the responding police officer and insurer that Guevara had been driving. When the misrepresentation was discovered, Loya refused to defend a suit brought against Guevara. A trial court ruled in Loya's favor, but an appellate court reversed, ruling that Loya's duty to defend derived solely from the face of the relevant policy and the complaint, which alleged that Guevara was driving at the time of the accident. The Texas Supreme Court reversed, endorsing a new exception to the eight-corners rule.

The Texas Supreme Court ruled that in determining an insurer's duty to defend, courts may consider extrinsic evidence regarding collusion to make false statements for the purpose of obtaining insurance coverage. In addition, the court held that an insurer, when confronted with undisputed evidence of collusion or fraud, need not file a declaratory judgment action before withdrawing its defense. However, if an insurer terminates its defense and it is subsequently determined that there was no collusion, an insurer risks "substantial liability" in terms of damages or attorneys' fees.

Number Of Occurrences Alert:

California Court Rules That Faulty Construction Suit Arose Out Of Multiple Occurrences

A California federal district court ruled that a construction defect lawsuit arose out of three separate occurrences, requiring the policyholder's payment of three deductibles and rejecting the assertion that the claims arose out of a single negligent supervision occurrence. *Liberty Mut. Fire Ins. Co. v. Bosa Dev. Cal. II, Inc.*, 2020 WL 1864645 (S.D. Ca. Apr. 13, 2020).

Bosa, the developer of a condominium project, was named as a defendant in a lawsuit alleging various construction defects. Liberty Mutual defended Bosa and ultimately paid the $4 million aggregate limit to settle the claims. However, Liberty argued that Bosa was responsible for the payment of multiple deductibles, based on its assertion that the lawsuit arose out of several distinct occurrences. In response, Bosa contended that its allegedly negligent supervision of the project constituted one occurrence, triggering only a single $500,000 deductible payment.

Applying California's cause-oriented test for determining the number of occurrences, the court concluded that there were three occurrences, arising out of three discrete events that caused damage: (1) the allegedly defective installation of exterior concrete structures; (2) the allegedly defective installation of interior plumbing and HVAC systems; and (3) the allegedly negligent selection of materials. The court explained that this conclusion was supported by the fact that different subcontractors worked on each of these distinct areas of the project, and that each "occurrence" resulted in a qualitatively different type of damage. Rejecting Bosa's single-occurrence assertion based on negligent supervision, the court stated that "such an interpretation would mean that there would never be more than a single occurrence in the course of a single construction project, no matter how disparate the harms."

Arbitration Alert:

Arbitration Panel Did Not Exceed Authority By Reconsidering Initial Determination, Says New York Court Of Appeals

Last year, a New York appellate court vacated an arbitration award issued in an insurance dispute on the basis that the arbitration panel exceeded its authority when it reconsidered a final liability award it had previously rendered. *American Int'l Specialty Lines Ins. Co. v. Allied Capital Corp.*, 2018 WL 5285241 (N.Y. App. Div. 1st Dep't Oct. 25, 2018). *See* November 2018 Alert. Last month, the New York Court of Appeals reversed, ruling that the panel acted within the bounds of its authority in reconsidering the "Partial Final Award." *American Int'l Specialty Lines Ins. Co. v. Allied Capital Corp.*, 2020 WL 2066743 (N.Y. Apr. 30, 2020).

Allied sought defense and indemnity from American International Specialty Lines Insurance Company ("AISLIC") for an underlying False Claims Act suit that it had settled for approximately $10 million. When AISLIC denied coverage, Allied filed for arbitration. During the arbitration proceeding, the arbitration panel issued a determination as to AISLIC's liability but stated that a separate hearing would be held as to the amount of defenses costs, if any, to which Allied was entitled. In its "Partial Final Award," the arbitration panel held that the $10 million settlement payment was not covered, but that Allied was entitled to reimbursement of defense costs.

Thereafter, but prior to the evidentiary hearing on the amount of expenses, the panel issued a "Corrected Partial Final Award," which deviated from the original Partial Final Award by holding that the underlying settlement was a covered loss. After conducting an evidentiary hearing regarding the amount of covered defense costs, the panel issued a Final Award awarding Allied more than $11 million in damages and interest. A New York trial court denied AISLIC's motion to vacate the Corrected Partial Final Award and the Final Award. The appellate court reversed, ruling that the arbitration panel exceeded its authority when it reconsidered the Partial Final Award. The appellate court explained that under the doctrine of *functus officio*, an arbitrator may not entertain an application to change a final award, except to correct a deficiency of form or miscalculation.

Reversing the appellate court, the New York Court of Appeals held that the *functus officio* doctrine was inapplicable because no final award had been issued. The court explained that even assuming that parties to an arbitration can agree to the issuance of a partial final award resolving some, but not all, of the disputed issues, no such agreement was reached here. Although counsel had suggested a separate proceeding to determine the amount of defense costs, if recoverable, AISLIC did not consent to bifurcation of the proceedings and "neither the parties nor the arbitrators ever discussed or otherwise demonstrated any mutual understanding regarding whether the proposed severance of the calculation of defense costs would result in a final partial award." The court held that absent such express, mutual agreement, there was no final award which would trigger application of the *functus officio* doctrine.

STB News Alerts:

Bryce Friedman and Nick Goldin authored an article titled, "Leveraging Cyber Insurance To Mitigate the Economic Impact of Cyber Incidents," which was published by *New York Law Journal* this month. The article provides an overview of the types of insurance policies that might cover cyber incidents and highlights some of the issues that are likely to arise surrounding cyber-related insurance coverage.

Simpson Thacher has once again been ranked among the leading law firms in the United States in *Chambers USA* 2020. The Firm or its lawyers were recognized in 55 practice categories, with a total of 27 firm rankings in the top two bands, including Band 1 rankings for Insurance: Dispute Resolution in the U.S. and New York. In addition, the Firm's attorneys received a total of 94 recognitions as leaders in their respective fields of practice.

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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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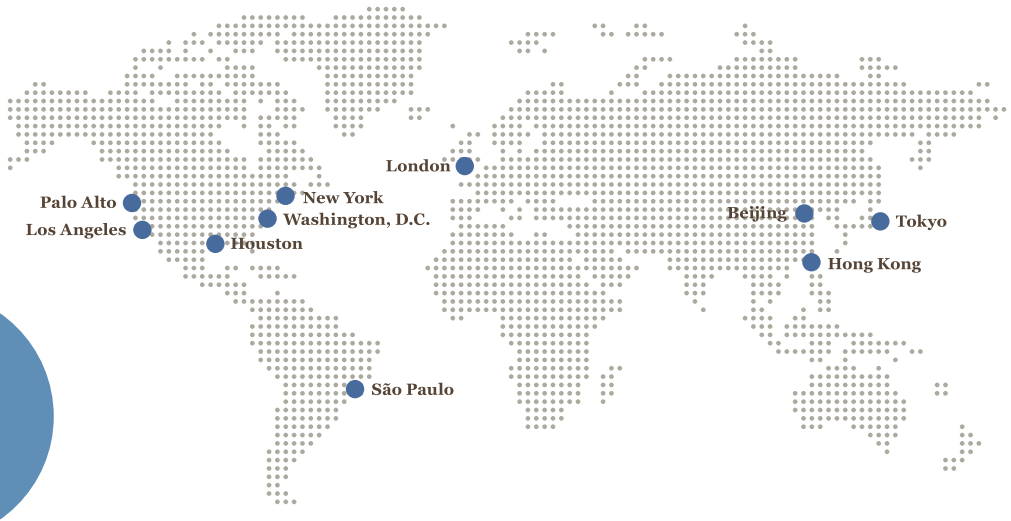

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