Simpson Thacher

Insurance Law Alert

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The District of Columbia Circuit Court ruled that reinsurers and reinsurance intermediaries were not directly liable to the original insured. *Vantage Commodities Financial Services I, LLC v. Assured Risk Transfer PCC, LLC*, 2022 WL 1193996 (D.C. Cir. Apr. 22, 2022). (Click here for full article)

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"[Simpson Thacher is] able to handle both direct insurance and reinsurance matters with equal flair, and also adept at handling the most complex of disputes regarding insurers' business practices. Often called on in cases involving potentially significant exposure."

–Chambers USA 2021

State And Federal Appellate Courts Continue To Rule In Insurers' Favor In Suits Seeking Coverage For Pandemic-Related Business Losses

In recent weeks, several state and federal appellate courts have continued the trend of dismissing policyholder suits seeking coverage for economic losses incurred in the wake of government orders relating to COVID-19. (Click here for full article)

Seventh Circuit Rules That Policyholder's Suit Against Property Insurer Is Time Barred

The Seventh Circuit dismissed a suit against a property insurer, ruling that the policyholder's failure to bring a legal action within two years of the date of damage was fatal to its coverage claim. *Legend's Creek Homeowners Assoc., Inc. v. Travelers Indem. Co. of Am.*, 2022 WL 1467456 (7th Cir. May 10, 2022). (Click here for full article)

Coverage Alert:

California Appellate Court Rules That Intentional Acts That Cause Unintended Harm Are Not Covered Occurrences Under Property Policy

A California appellate court ruled that a homeowner was not entitled to coverage under a property policy for losses stemming from the intentional removal of trees based on her mistaken belief that the trees were located on her property. *Ghukasian v. Aegis Security Ins. Co.*, 2022 WL 1421511 (Cal. Ct. App. Apr. 14, 2022).

The policyholder hired a contractor to remove trees that she mistakenly believed to be on her own property. Her neighbors sued, alleging trespass and negligence. The insurer denied coverage on the ground that the underlying suit alleged only intentional conduct. In the ensuing litigation, a trial court granted the insurer's summary judgment motion, finding no allegations of a covered "occurrence," and alternatively that several policy exclusions barred coverage.

The appellate court affirmed, explaining that the tree removal and land leveling were intentional actions, regardless of the policyholder's mistaken beliefs about property boundaries. The court rejected the policyholder's contention that *Liberty Surplus Ins. Corp. v. Ledesma & Meyer Construction Co.*, 5 Cal. 5th 216 (2018), in which the California Supreme Court held that a negligent hiring suit stemming from an employee's molestation of a third party may allege a covered occurrence, was controlling. The court explained that in *Liberty Surplus*, the causal chain that led to injury began with the employer's alleged negligent act of hiring the employee, whereas here, the immediate cause of damage was the policyholder's intentional action of tree removal. In addition, the court emphasized that *Liberty Surplus* "contain[ed] no language indicating it intended to overrule prior caselaw holding that intentional acts are not 'accidents' merely because the insured did not intend to cause injury." Finally, the court deemed it irrelevant that the underlying suit alleged a cause of action sounding in negligence, noting that the insurer's duty to defend turns on the facts alleged in the underlying complaint, not the labels of the causes of action.

Reinsurance Alert:

District Of Columbia Circuit Court Dismisses Original Insured's Claims Against Reinsurers And Intermediaries

The District of Columbia Circuit Court ruled that reinsurers and reinsurance intermediaries were not directly liable to the original insured. *Vantage Commodities Financial Services I, LLC v. Assured Risk Transfer PCC, LLC*, 2022 WL 1193996 (D.C. Cir. Apr. 22, 2022).

Vantage entered into a loan agreement extending credit to an energy company. In order to mitigate the risk of loan default, Vantage hired Equifin Risk Solutions to create Assured Risk Transfer ("ART"), a special purpose "captive" insurance entity backed by reinsurance. In turn, Equifin retained Willis Towers to assist in the management of ART. Equifin secured reinsurance from several carriers to reinsure ART for a portion of insurance issued to Vantage. When the energy company defaulted on the loan, Vantage submitted a claim to ART. ART disputed the claim and an arbitration panel ultimately found in Vantage's favor. ART had insufficient funds to pay the arbitration award. The reinsurers notified ART that any future claims would be denied because ART had failed to comply with certain notice and proof of loss requirements in the reinsurance agreements. Thereafter, Vantage sued ART, the reinsurers and Willis Towers, alleging negligence, breach of contract, promissory estoppel, unjust enrichment and professional negligence. The district court dismissed the suit and the appellate court affirmed.

The appellate court held that as to the claims against the reinsurers, Vantage failed to plead facts sufficient to establish a direct contractual relationship. The court acknowledged that in certain circumstances, a reinsurer may become directly liable to the original insured, but concluded this case did not present such a scenario. In particular, the court held that there was no implied contract because Vantage never dealt directly with the reinsurers. Similarly, the promissory estoppel and unjust enrichment claims failed because both depended on the existence of an agency relationship between the reinsurers and either ART or Willis Towers, which was not established by the allegations or factual record.

With respect to the professional negligence claims against Willis Towers, the court held that the "economic loss doctrine" bars such claims where, as here, the claimant seeks to recover purely economic losses. The court rejected Vantage's assertion that there was a "special relationship" between the parties that would create an exception to the economic loss doctrine. The court noted that Willis Towers had minimal contact with Vantage, "nothing approaching the 'close' or 'intimate' nexus" needed to trigger the exception. The court also ruled that the negligent misrepresentation claims were without merit, citing the lack of false representations or reasonable reliance.

Assignment Alert:

South Carolina Supreme Court Rules That Post-Loss Assignment Of Insurance Rights Is Valid Notwithstanding Lack Of Insurer Consent

Reversing an appellate court decision, the South Carolina Supreme Court ruled that the operative "loss" for insurance coverage purposes is determined by the date of occurrence, rather than the time of judgment or settlement, and that a post-loss assignment of insurance rights was valid even without insurer consent. *PCS Nitrogen, Inc. v. Continental Cas. Co.*, 2022 WL 1101704 (S.C. Apr. 13, 2022).

From 1966 to 1972, Columbia Nitrogen Corporation ("Old CNC") operated fertilizer plants in Charleston. During that time frame, Old CNC was insured under policies issued by Continental. In 1986, Old CNC entered into an acquisition agreement which sold most of its assets to CNC Corp. ("New CNC"). In addition to the assets, New CNC assumed some of Old CNC's liabilities related to the "acquired business." The agreement also included a document titled "Assignment of Insurance Benefits," which stated that Old CNC "has agreed to sell, convey, transfer, and assign . . . all of [its] rights, proceeds and other benefits to and under all of [its] policies." New CNC later changed its name and merged with PCS Nitrogen. In 2013, PCS Nitrogen was found liable for environmental remediation as a corporate successor to Old CNC. PCS Nitrogen sought coverage under Old CNC's policies, which Continental denied. A South Carolina trial court granted the insurer's summary judgment motion, and the appellate court affirmed.

As discussed in our January 2020 Alert, the appellate court ruled that the policies were not assigned to New CNC because Old CNC did not obtain the consent from the insurers required by the policies and South Carolina law. The court further held that the assignment was invalid as a post-loss assignment because there were no vested claims from prior actions against Old CNC at the time of assignment. The policies specified that coverage was not available "until the amount of the insured's obligation to pay shall have been finally determined by judgment . . . or by written agreement." Under this language, and because no actions had been filed against Old CNC prior to the asset sale, the court held that no losses had occurred and no vested claims existed. The court explained that although the operative occurrences (*i.e.*, contamination) may have occurred during the policy period, the insured loss (*i.e.*, the insured's obligation to pay a sum of money) did not occur prior to the assignment.

Last month, the South Carolina Supreme Court reversed, adopting the "post-loss exception" and holding that insurer consent is not required for an assignment of insurance benefits made after a "loss" has occurred. As a preliminary matter, the court concluded that under third-party policies, the operative "loss" arises at the time of the occurrence, not when judgment is issued against the insured. Further, the court ruled that in the present case, any loss occurred before Old

CNC executed the assignment in 1986 and therefore that the assignment was valid.

The court remanded the matter for a determination of several other coverage issues, including whether the discharge of contaminants constitutes a covered "occurrence" in the first instance, whether a pollution exclusion bars coverage, or whether PCS engaged in any post-loss conduct that would operate to void coverage.

Several other state supreme courts have addressed this issue. The highest courts of California and New Jersey have applied a post-loss exception to factual scenarios similar to the one presented here. However, the State Supreme Courts of Hawaii and Oregon have held that post-loss assignments are not valid without insurer consent.

COVID-19 Alerts:

Two State Supreme Courts Rule That COVID-19-Related Business Losses Do Not Allege Physical Loss Or Damage

The highest courts in Iowa and Massachusetts have ruled that pandemic-related business losses are not covered by all risk property policies, concluding that allegations relating to the COVID-19 virus do not allege physical loss or damage.

In *Verveine Corp. v. Stratmore Ins. Co.*, 2022 WL 1180061 (Mass. Apr. 21, 2022), the Supreme Judicial Court of Massachusetts ruled that losses incurred by restaurants in the wake of government shutdown orders were not covered by all risk property policies because there was no "direct physical loss of or damage to" property. In so ruling, the court emphasized that the relevant inquiry is "not whether the virus is physical, but rather if it has direct physical effect *on property* that can be fairly characterized as 'loss or damage.'" (Emphasis in original). Noting that every federal appellate court in the nation has required some "distinct, demonstrable, physical alteration of the property," the court concluded that no such loss or damage is alleged in the context of COVID-19-related business losses stemming from government restrictions.

Further, the court held that allegations of viral "presence" do not amount to physical loss or damage, stating: "Evanescent presence of a harmful airborne substance that will quickly dissipate on its own, or surface-level contamination that can be removed by simple cleaning, does not physically alter or affect property." Having reached this conclusion, the court also held that civil authority coverage was unavailable because there was no damage to properties located nearby to the insured premises.

Finally, the court rejected the policyholder's contention that the inclusion of a virus exclusion in one policy but not in others created "a clear negative implication" that the policies without the exclusion were intended to cover COVID-19-related claims.

In *Wakonda Club v. Selective Ins. Co. of Am.*, 2022 WL 1194012 (Iowa Apr. 22, 2022), the Iowa Supreme Court granted an all-risk property insurer's motion for summary judgment, finding that losses suffered as a result of government closure orders were not covered by Business Income and Extra Expense provisions. Addressing this matter of first impression under Iowa law, the court held that a policyholder's loss of use of its property, without more, cannot satisfy the policy's "direct physical loss of" property requirement. Because the policyholder disavowed any knowledge that the COVID-19 virus was present at its premises, the court held there was no potential physical element that could implicate coverage.

The court rejected the policyholder's assertion that coverage was available pursuant to Iowa's reasonable expectations doctrine, which turns on an ordinary layperson's understanding of policy coverage, regardless of ambiguity. The court explained that even if a layperson would not understand the difference between "loss" and "damage," the "physical"

requirement "defeats any expectation that the policy provided coverage for any business interruption untethered from a physical loss of the property."

On the same day that *Wakonda Club* was decided, the Iowa Supreme Court also dismissed a policyholder's complaint in *Jesse's Embers, LLC v. Western Agricultural Ins. Co.*, 2022 WL 1194006 (Iowa Apr. 22, 2022). There, the court rejected a claim for business interruption coverage for the same reasons set forth in *Wakonda Club*, and also upheld the insurer's denial of coverage under a civil authority policy provision. The court reasoned that the government orders were not issued in response to physical loss or damage to nearby property, but rather in order to reduce the spread of the virus.

State And Federal Appellate Courts Continue To Rule In Insurers' Favor In Suits Seeking Coverage For Pandemic-Related Business Losses

In recent weeks, several state and federal appellate courts have continued the trend of dismissing policyholder suits seeking coverage for economic losses incurred in the wake of government orders relating to COVID-19.

State appellate courts in Florida, Illinois and Michigan have recently affirmed the dismissal of policyholders' claims for business losses incurred in the wake of the pandemic and its related government shutdown orders.

In *Commodore, Inc. v. Certain Underwriters at Lloyd's London*, 2022 WL 1481776 (Fla. Dist. Ct. App. May 11, 2022), a Florida appellate court upheld the dismissal of a restaurant's coverage suit against its commercial property insurer. The court emphasized the necessity of a "tangible" loss in order to satisfy the policy's "direct physical loss of or damage to" property requirement, rejecting the restaurant's contention that its inability to use its property for its intended purpose was sufficient to trigger coverage. Like many other courts across jurisdictions, the *Commodore* court also noted that the policy's "period of restoration" provision further supported its conclusion that loss of use alone cannot constitute loss or damage to property under the policy.

Two appellate courts in Illinois also rejected claims for COVID-19-related coverage. In *GPIF Crescent Court Hotel LLC v. Zurich Am. Ins. Co.*, No. 1-21-1335 (Ill. Ct. App. May 20, 2022), the court held that a hotel's implementation of plexiglass barriers, sanitizer stations and other elements were insufficient to satisfy the physical loss requirement, and in *Firebirds International, LLC v. Zurich Am. Ins. Co.*, No. 2020 CH 05360 (Ill. Ct. App. May 20, 2022), the court ruled that a contamination exclusion unambiguously barred coverage for the COVID-19-related business loss claims.

Michigan appellate courts have likewise concluded that business losses arising out of the COVID-19 virus itself or the related government orders do not give rise to coverage under business interruption or civil authority policy provisions. *See Massage Bliss, Inc. v. Farm Bureau General Ins. Co. of Michigan*, 2022 WL 1591925 (Mich. Ct. App. May 19, 2022); *Three Won Three, Corp. v. Property-Owners Ins. Co.*, 2022 WL 1594828 (Mich. Ct. App. May 19, 2022).

Employing similar reasoning, federal appellate courts in the Sixth, Eighth and Eleventh Circuits have also upheld dismissals of COVID-19-related coverage suits. *See Renaissance/The Park, LLC v. Cincinnati Ins. Co.*, 2022 WL 1596257 (6th Cir. May 20, 2022) (Kentucky law); *Glen R. Edwards, Inc. v. Travelers Cas. Ins.*, 2022 WL 1510818 (8th Cir. May 13, 2022) (Missouri law); *SA Palm Beach, LLC v. Certain Underwriters at Lloyd's London*, 2022 WL 1421414 (11th Cir. May 5, 2022) (Florida law).

Suit Limitation Clause Alert:

Seventh Circuit Rules That Policyholder's Suit Against Property Insurer Is Time Barred

The Seventh Circuit dismissed a suit against a property insurer, ruling that the policyholder's failure to bring a legal action within two years of the date of damage was fatal to its coverage claim. *Legend's Creek Homeowners Assoc., Inc. v. Travelers Indem. Co. of Am.*, 2022 WL 1467456 (7th Cir. May 10, 2022).

In 2016, Legend's Creek, a homeowners' association, filed a claim with Travelers for hail and wind damage that had occurred in May 2016. During the following two-year period, the public adjuster retained by Legend's Creek and Travelers worked together to evaluate the scope and cost of covered damages. During that time frame, Travelers issued three payments totaling more than $900,000. In 2018, less than three weeks before the contractual deadline to bring a legal action, the adjuster made an additional demand for payment in order to replace non-damaged exterior sides of the building so that they would match the newly repaired side.

When Travelers refused, Legend's Creek sued, alleging bad faith and breach of contract. An Indiana district court granted Travelers' summary judgment motion and the Seventh Circuit affirmed.

The Seventh Circuit noted that Indiana law recognizes a few limited exceptions to contractual suit deadlines, but concluded that none applied here. In particular, the court rejected Legend's Creek's assertion that compliance with the suit provision was impossible where, as here, the claim investigation takes more than two years. The court reasoned that Legend's Creek "points to no term in the policy that it did not or could not have abided by within the two-year window." In addition, the court rejected the contention that ongoing cooperation during the two-year period excused the suit limitation deadline, stating: "Though Legend's Creek may not have had a reason to litigate in that period, that doesn't render the policy requirements incomprehensible or its obligations impossible." The court also rejected Legend's Creek's argument that Travelers was obligated to provide notice of its intent to rely on the policy's suit limitation clause, noting the absence of legal support for that contention. Finally, the court held that Travelers did not waive its right to rely on the suit limitations provision by continuing to negotiate with the public adjuster.

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