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QUARTERLY INSURANCE COVERAGE NEWSLETTER: NEW YORK

A quarterly newsletter from L'Abbate, Balkan, Colavita & Contini, L.L.P. Volume VI · Issue II · Second Quarter 2013

CASES OF INTEREST BY TOPIC

DUTY TO DEFEND

K2 Inv. Grp., LLC v. American Guarantee & Liability Ins. Co., 2013 WL 2475869 (June 11, 2013). K2 Group, LLC provided loans secured by mortgages to Goldan, LLC; however, Goldan failed to record the mortgages or repay the loans. Consequently, K2 Group commenced a lawsuit against Goldan and its two principals, Mark Goldman and Jeffrey Daniels (an attorney). Although the lawsuit primarily sought payment on the loans, a claim for legal malpractice was also asserted against Daniels and, as such, he notified his malpractice carrier, American Guarantee and Liability Insurance Company, of the same. American Guarantee refused to provide "either defense or indemnity coverage" based upon its belief that the allegations against Daniels were "not based on the rendering or failing to render legal services for others." After issuance of the disclaimer, K2 Group made a settlement demand on Daniels for $450,000—significantly less than the $2 million limit of the American Guarantee policy. Daniels forwarded the settlement demand to American Guarantee; however, it was rejected on the same grounds as cited in the disclaimer. Daniels ultimately failed to appear in the lawsuit and K2 Group obtained a default judgment in excess of the policy limits. The judgment was entered only as to the legal malpractice claim; the other claims against Daniels were discontinued. Daniels subsequently assigned his rights against American Guarantee to K2 Group and K2 Group commenced an action for, *inter alia*, breach of contract under the policy. American Guarantee thereafter moved for summary judgment seeking the dismissal of the Complaint, relying on policy exclusions pertaining to "insured status" and "business enterprise." K2 Group cross-moved for summary judgment asserting that as American Guarantee breached its duty to defend Daniels, it was bound up to the $2 million limit of its policy and required to pay the resulting judgment against him.

The Court of Appeals (New York's highest court) stated that the underlying lawsuit against Daniels unmistakably plead a claim for legal malpractice and while American Guarantee had every right to be skeptical of the same as being "groundless, false or baseless…meritless or not covered"—that was not sufficient to escape the duty to defend. In relying on its decision in *Lang v. Hanover Ins. Co.*, 3 N.Y.3d 350 (2003), the Court of Appeals stated that "when an insurer has breached its duty to defend and is called upon to indemnify its insured for a judgment entered against it, the insurer may not assert in its defense grounds that would have defeated the underlying claim against the insured." The Court further held that "an insurance company that has disclaimed its duty to defend 'may litigate only the validity of the disclaimer.' If the disclaimer is found bad, the insurance company must indemnify its insured for the resulting judgment, even if policy exclusions would otherwise have negated the duty to indemnify." The Court reasoned that the foregoing would incentivize insurers to defend the cases that they are bound by law to defend, and thus to give insureds the full benefit of their bargain. The Court did note, however, that there may be an exception to the rule, if for example, public policy would prevent an insurer from indemnifying a judgment for intentional wrongdoing, but there were no such public policy arguments available to American Guarantee in this case. Finally, it was suggested by the Court that insurers in similar situations should have the coverage dispute resolved by way of a declaratory judgment action.

State Farm Fire & Cas. Co. v. Joseph M., 2013 WL 1896996 (2d Dept. May 8, 2013). Joseph M. was allegedly insured under a homeowner's insurance policy issued by State Farm Fire & Casualty Company to his parents. The policy provided personal liability coverage for claims made against an insured for damages because of bodily injury caused by an "occurrence", which was defined as "an accident…which result[ed] in…bodily injury." The underlying lawsuit was commenced against Joseph M. alleging that he sexually assaulted the plaintiff resulting in bodily injury. Joseph M. sought a defense and indemnification and, in response, State Farm commenced a declaratory judgment action for a finding that there was no obligation to provide a defense or indemnity relative to the underlying action. The Second Department stated that the bodily injuries allegedly sustained were inherently caused by the alleged sexual assault which could not be construed as an accident within the definition of an

"occurrence" under the policy. The Court further indicated that Joseph M. could not "exalt form over substance by labeling the [underlying] action as one to recover damages for negligence." Accordingly, the Second Department found that State Farm had no duty to defend or indemnify Joseph M. in connection with the underlying action.

Seneca Ins. Co., Inc. v. Cimran Co., Inc., 2013 WL 1405231 (1st Dept. Apr. 9, 2013). On October 12, 2009, while construction was underway to add three additional floors to Cimran Co., Inc.'s one-story building in Flushing, Queens, an employee of the subcontractor handling the framing fell and sustained injuries. The employee subsequently commenced a personal injury action against Cimran. While the Complaint in the personal injury action merely stated that the employee fell at "the construction site," the Bill of Particulars added that the incident took place "while the [employee] was working on the fourth floor on top of the steel framing of the fourth floor side and/or edge." Cimran had provided notice to Seneca Insurance Company, Inc., which had issued a Commercial General Liability policy to Cimran. After accepting the defense, Seneca subsequently commenced a declaratory judgment action, seeking, *inter alia*, a declaration that it had no duty to defend Cimran in the underlying action because the alleged accident did not take place at the "Designated Premises" covered by the policy; specifically, the insured premises, designated as a 10,000-square-foot, one-story building. Seneca asserted that the alleged accident occurred on the three story addition, which was under construction and materially altered the "Designated Premises." Both Seneca and Cimran moved for summary judgment. Based on the fact that the insured premises was described in Cimran's insurance application as a one-story building that housed two commercial tenants, the First Department stated that as the policy was explicitly issued in reliance on the representations made in the insurance application, there could be no dispute that the purchased coverage was limited to the one-story building. The Court reasoned that as the policy only provided coverage for injuries arising out of the insured building—namely the first floor, the Seneca policy did not provide coverage for the structure that existed during the construction of the three additional floors. As such, the First Department held that Seneca had no duty to defend or indemnify Cimran relative to the underlying action.

APPLICABILITY OF EXCLUSIONS

Dreyer v. New York Central Mut. Fire Ins. Co., 2013 WL 1810851 (2d Dept. May 1, 2013). Edmund Schwartz commenced a personal injury action against Walter and Patricia Dreyer in connection with an incident in which a vehicle driven by Walter, and owned by Patricia, was rear-ended by a vehicle driven by Schwartz. Immediately after the collision, when Schwartz stopped and exited his vehicle, Walter allegedly intentionally drove his vehicle into Schwartz, verbally accosted him, and left the scene. In a separate criminal prosecution, Walter was charged with assault and leaving the scene of an accident involving a personal injury, and ultimately pled guilty to disorderly conduct and leaving the scene. In the underlying personal injury action, Schwartz asserted a cause of action for negligence against the Dreyers and intentional tort causes of action against Walter. The Dreyers notified their insurer, New York Central Mutual Fire Insurance Company, which disclaimed coverage for any injuries caused by the intentional acts of Walter under an exclusion in the personal Auto policy. In response, the Dreyers commenced a declaratory judgment action against New York Central to provide a defense and indemnity in the underlying action. At the conclusion of the trial in the underlying action, only the negligence cause of action was submitted to the jury and the jury found against Walter. As such, the Dreyers moved for summary judgment on indemnification of the jury award against Walter. The Second Department found that although the Dreyers established their prima facie entitlement to judgment as a matter of law for indemnification, in opposition, New York Central submitted evidence from the criminal prosecution and the underlying action, including Schwartz' deposition testimony, which raised a triable issue of fact as to whether the loss fell within the policy exclusion for bodily injury "intentionally" caused by the insured. Further, the Court noted that the intentional tort causes of action were not submitted to the jury in the underlying action and, thus, there had been no adjudication of the facts relevant to the applicability of the policy exclusion. As such, the Second Department overturned the trial court's finding that New York Central was obligated to indemnify the Dreyers based upon the remaining issues of fact.

RSUI Indem. Co. v. RCG Group (USA), 2013 WL 2460634 (2d Cir. June 10, 2013). On or about March 21, 2007, East 51st Street Development Company, the owner of a property in Manhattan entered into an agreement with RCG Group Reliance Construction, Inc. for the initial construction work of a high-rise development. Pursuant to the terms of the construction agreement, in addition to procuring primary liability insurance, RCG also procured excess liability insurance from RSUI Indemnity Company which named East 51st Street as an additional insured.

The RSUI Policy contained an endorsement entitled: "Exclusion – Residential Work" precluding coverage for the construction of a "residential project." "Residential project" included "mixed-use buildings", defined as "structures and improvements thereto, which contain both residential units and commercial space." On March 15, 2008, a tower crane at the property collapsed, killing seven people, injuring dozens more, and causing extensive property damage. RCG and East 51st Street notified RSUI of the accident and RSUI disclaimed coverage. RSUI then commenced a declaratory judgment action against RCG and East 51st Street, seeking a declaration of its rights and responsibilities arising out of the crane collapse. RSUI subsequently filed a Motion for Summary Judgment for an order that coverage was precluded under the Residential Work Exclusion. In its decision, the United States Court of Appeals for the Second Circuit found that at the time of the accident, the building was intended to contain a large number of residential units, in addition to commercial and community space. The Court was unpersuaded by RCG's and East 51st Street's arguments that the contemplated community space removed the building from the Policy's definition of a "mixed-use building." In this regard, the Second Circuit stated "that the plain meaning of the word 'contain' implies the actual presence of a specified substance or quantity within something…[and i]t does not, however, signal that the specified substances are the exclusive content." Thus, the Court held that the Residential Property Exclusion applied and RSUI had no duty to indemnify RCG or East 51st Street in connection with the crane collapse.

Silverman Neu, LLP v. Admiral Ins. Co., 2013 WL 1248629 (E.D.N.Y. Mar. 28, 2013). Silverman Neu, LLP, as successor to Chipentine, Neu & Silverman, LLC ("CNS"), commenced a declaratory judgment action against its professional liability insurer, Admiral Insurance Company, for a defense and indemnity in an underlying class action lawsuit. The underlying action was initiated by class representatives claiming that CNS was involved in shielding certain of its clients' allegedly wrongful debt management practices from the public. Specifically, it was alleged that CNS was aware that its clients had engaged in unlawful acts from audits performed and the preparation of relevant tax forms. Admiral argued, *inter alia*, that coverage for the claims was barred pursuant to the policy's Wrongful Act Exclusion, which precluded coverage for "any liability based in whole or in part on any knowingly wrongful, dishonest, fraudulent, criminal or malicious act committed by or at the direction of any 'Insured' in the course of providing 'professional services.'" Although it was undisputed that the underlying action contained allegations of knowing and intentional wrongful conduct, CNS countered that some of the allegations were negligence based. The United States District Court for the Eastern District of New York stated that as CNS essentially conceded that at least some of the allegations in the Complaint were based on knowing and intentional conduct which was sufficient (based on the plain language of the Wrongful Acts Exclusion) to exclude coverage under the Admiral policy.

TRIGGER OF COVERAGE

I.J. White Corp. v. Columbia Cas. Co., 105 A.D.3d 531, 964 N.Y.S.2d 21 (1st Dept. Apr. 16, 2013). Hill Country Bakery, LLC made and distributed frozen baked goods. In 2006, Hill Country purchased a spiral freezer system from I.J. White Corp.; however, it was alleged that the freezer system never operated properly. In 2010, Hill Country commenced an action against I.J. White alleging that for eight months it was unable to use a $21 million facility constructed specifically to house the equipment. Moreover, Hill Country alleged that it expended an additional $1.9 million to render the equipment operable. I.J. White tendered its defense and indemnification to its Commercial General Liability insurer, Columbia Casualty Company. The Columbia policy defined "property damage" as "[p]hysical injury to tangible property, including all resulting loss of use of property" and "loss of use of tangible property that is not physically injured." The First Department reiterated New York's well-settled principle that Commercial General Liability policies do not insure against faulty workmanship, but instead against the damage caused by faulty workmanship to something other than the work product itself. As such, it was found that Hill Country's loss of use of the facility specifically built to house the freezer was covered under the policy as "property damage" was defined to include "[l]oss of use of tangible property that is not physically injured."

LATE NOTICE

B & A Demolition & Removal v. Markel Ins. Co., 2013 WL 1686635 (E.D.N.Y. Apr. 18, 2013). On April 13, 2009, Parabit Realty, LLC and Parabit Systems, Inc., the owners of a building located in Roosevelt, New York, commenced an action against B & A Demolition and Removal, Inc., among others, alleging that it damaged their building during the construction of an adjacent structure. Approximately seven months later, on November 17, 2009, B & A provided notice to its insurer, Markel Insurance Company, LLC. On December 2, 2009, Markel disclaimed coverage to B & A on late notice grounds. In turn, B & A commenced a declaratory judgment action against Markel. Specifically, B & A contended that the changes to Insurance Law § 3420(a) governed the subject policy and, thus, Markel must demonstrate prejudice in order to disclaim coverage on the basis of late notice. The United States District Court for the Eastern District of New York noted that the determination as to whether Markel must demonstrate prejudice depended entirely on when its policy was "issued or delivered" as the changes to § 3420(a) apply only to policies that were issued or delivered on or after January 17, 2009. In this regard, the policy was bound by Markel and effective on October 13, 2008. The binder was then released by Markel to Gremesco Corporation, the wholesale broker, and on December 1, 2008, Markel transmitted a copy of the policy to Gremesco via e-mail. Gremesco subsequently forwarded a copy of the policy to The Halland Companies, the retail broker. Although Gremesco claimed that a copy of the policy was sent to Halland on December 1, 2008, Halland maintained that it did not receive the same until February 18, 2009. In making its determination, the Court noted that compliance with the condition of delivery of an insurance policy calls for a legal delivery, but not in all cases for an actual or manual delivery. It was further stated that a policy is not considered to be "delivered" at the time the binder is issued as it is not equivalent to the issuance of the actual policy. Moreover, the Court reiterated the well settled rule that under New York law, insurance brokers are generally deemed to be the agent of the insured and not the insurer. As such, the Court held that Gremesco was an agent of B & A with regard to the "delivery" of the policy. Thus, as the "delivery" took place when Gremesco received the policy from Markel on December 1, 2008, the Court found that the policy was not governed by the changes to § 3420(a) and, therefore, Markel did not have to demonstrate prejudice to disclaim coverage on late notice grounds.

Ortiz v. Fage USA Corp., 2013 WL 1319398 (2d Dept. Apr. 3, 2013). Fage USA Corp. commenced a declaratory judgment action against Utica Mutual Insurance Company, which had issued an umbrella policy, seeking a declaration that Utica, which denied coverage, was obligated to provide a defense and indemnity in an underlying personal injury action arising out of a motor vehicle accident that occurred on March 25, 2007. The umbrella policy required Fage to inform Utica of an occurrence or suit as soon as practicable. However, Fage did not provide Utica with notice until more than two and one half years after the accident and more than two years after the underlying action was commenced. Fage's only excuse was that the delay was due to the fact that its counsel was unaware of the existence of the umbrella policy until October 2009 and, upon the discovery of the same, notice was immediately provided. In finding that Fage did not establish its prima facie entitlement to judgment as a matter of law, the Second Department held that when an insurance policy requires notice of an occurrence as soon as practicable, it must be given within a reasonable time in view of all the circumstances and, absent a valid excuse, the failure to satisfy the notice requirement vitiates coverage as long as the policy was issued prior to January 17, 2009 (the date after which New York Insurance Law §3420(a) was changed to require a showing of prejudice). The Second Department held that Fage's counsel lack of awareness of the umbrella policy until October 2009 was not a valid excuse for the failure to provide Utica with timely notice; therefore, Utica was not obligated to defend or indemnify Fage under the umbrella policy.

EXCESS INSURANCE/DROP DOWN

Ali v. Federal Ins. Co., 2013 WL 2396046 (2d Cir. June 4, 2013). Former directors and officers of Commodore International Limited, a computer technology company which ceased operations and filed for bankruptcy in 1994, had purchased primary and several layers of excess directors and officers insurance coverage designed to protect them from potential liability. Since that time, Reliance Insurance Company and the Home Insurance Company, two of the insurers, had ceased operations and liquidated their assets. Federal Insurance Company ("FIC"), the still-operational provider of the second and fifth level excess insurance policies, anticipating that the directors and officers would seek coverage for a lawsuit pending against them in the Supreme Court of the Commonwealth of the Bahamas, filed for declaratory relief. Specifically, FIC sought a declaration that it was not

required to "drop down" to cover liability that would have otherwise been covered by Reliance and Home. The FIC policies provide, in relevant part, that excess liability coverage "shall attach only after all…'Underlying Insurance' has been exhausted by payment of claim(s)" and that "exhaustion" of the underlying insurance occurs "solely as a result of the payment of losses thereunder." The directors and officers then filed a counterclaim against FIC seeking a declaration that FIC's coverage obligations are triggered once the total amount of the defense and/or indemnity obligations exceed the limits of any insurance policies underlying their respective policies, regardless of whether such amounts have actually been paid by those underlying insurance companies. The United States Court of Appeals for the Second Circuit held that the express language of the relevant contract terms "establishes a clear condition precedent to the attachment of the Excess Policies," by "expressly stat[ing] that coverage does not attach until there is payment of the underlying losses." The Court stated that because the plain language of the contracts specifies that the coverage obligation is not triggered until payments reach the respective attachment points, the District Court properly denied the request of the directors and officers for a declaration that coverage obligations were triggered.

RESCISSION/REFORMATION

Meah v. A. Aleem Constr. Inc., 105 A.D.3d 1017 (2d Dept. Apr. 24, 2013). On August 18, 2005, Saleh Ahmed Meah, was working for Liberty Contracting & Home Improvement, a subcontractor at a job site owned by Garden of Eden Associates, L.P. at which A. Aleem Construction, Inc. was the general contractor. While Meah was performing his work, he was allegedly cut by a saw and sustained injuries. Meah then commenced a personal injury action against Aleem and Garden of Eden. Aleem, in turn, commenced an action against Rutgers Casualty Insurance Company, Liberty's insurer, seeking, *inter alia*, a declaration that Rutgers was obligated to defend and indemnify Aleem as an additional insured. Rutgers cross-moved for summary judgment against Aleem seeking rescission of the policy. The Second Department stated that to establish the right to rescind an insurance policy, an insurer must show that its insured made a material misrepresentation of fact when securing the policy and that material misrepresentations if proven would void the policy *ab initio*. The Court found that Rutgers established, *prima facie*, that Liberty made material misrepresentations in its application for the subject insurance policy by representing that it would perform no roofing work during the period of coverage and that it would perform no work at heights above two stories. It was undisputed that Liberty's employees were performing work on a roof six stories above ground. Rutgers established that these representations were material by demonstrating, through its underwriting guidelines and past practices, among other things, that had it been properly advised as to the type of work performed by Liberty, it would not have issued the subject policy. As such, the Second Department held that the Rutgers policy was void *ab initio* and, accordingly, Aleem was not entitled to additional insured coverage as there was no valid existing policy.

NUMBER OF OCCURRENCES

Roman Catholic Diocese of Brooklyn v. Nat'l Union Fire Ins. Co. of Pittsburgh, PA, 2013 WL 1875302 (Ct. of App. May 7, 2013). In November 2003, Jeanne M. N.-L., individually and as mother and natural guardian of Alexandra L., a minor, commenced a civil action against the Roman Catholic Diocese of Brooklyn and one of its priests. The Complaint alleged that the priest sexually abused Alexandra on several occasions between August 10, 1996 and May 2002, and that the molestation took place in several locations. In August 2007, the Diocese settled the action for $2 million and "additional consideration." The Diocese, which had procured three consecutive one-year Commercial General Liability insurance policies from National Union Fire Insurance Company of Pittsburgh, Pennsylvania for the periods 1995-1996, 1996-1997, and 1997-1998, sought coverage under those policies. National Union asserted, in part, that the "policies have $750,000 policy limits over a $250,000 self-insured retention" and that the SIRs needed to be satisfied. In January 2009, the Diocese commenced a declaratory judgment action against National Union for indemnification of the $2 million settlement and defense costs. National Union subsequently moved for partial summary judgment seeking an order that the incidents of sexual abuse in the underlying action constituted separate occurrences in each of the implicated policies, and, thus, the Diocese was required to exhaust a separate $250,000 self-insured retention for each occurrence. In a plurality opinion, the Court of Appeals noted that under New York law, absent policy language indicating an intent to aggregate separate incidents into a single occurrence, the unfortunate event test should be applied to determine how occurrences are categorized for insurance coverage purposes, and that the same requires consideration of "whether there is a close temporal and spatial relationship between the incidents giving rise to injury or loss, and whether the incidents can be viewed as part of the

same causal continuum, without intervening agents or factors." The Court stated that here, nothing in the language of the policies nor in the definition of "occurrence" evinced an intent to aggregate the incidents of sexual abuse into a single occurrence. As such, in applying the unfortunate event test, the Court found that the incidents of sexual abuse which spanned a six-year period and transpired in multiple locations lacked the requisite temporal and spatial closeness to join the incidents. Accordingly, the Court of Appeals held that the Diocese was required to exhaust a separate self-insured retention for each occurrence that transpired within an implicated policy from which coverage was sought.

ADVERTISING INJURY

CGS Industries, Inc. v. Charter Oak Fire Ins. Co., 2013 WL 2476998 (2d Cir. June 11, 2013). On December 23, 2009, Five Four Clothing, Inc. sued Wal-Mart Stores, Inc. for trademark infringement based on CGS Industries, Inc.'s use of Five Four's distinctive rear pocket stitching design on jeans supplied to Wal-Mart. CGS was subsequently added as a defendant in that action and sought a defense and indemnification from Charter Oak Fire Insurance Company pursuant to its liability insurance policy. Charter refused, asserting that the claims in the action were not covered by the policy and, thereafter, CGS eventually settled with Five Four. The Charter policy provided, in relevant part, that Charter "will pay those sums that [CGS] becomes legally obligated to pay as damages because of 'advertising injury'…to which this insurance applies." "Advertising injury" is defined as injury arising out of the "[i]nfringement of copyright, title or slogan." CGS then commenced an action against Charter for breach of its duty to defend CGS against Five Four's lawsuit and both parties moved for summary judgment. Specifically, Charter argued, among other things, that it had no duty to defend or indemnify CGS because the stitching on the pocket was not a "title" used in advertising and, therefore, the underlying action did not allege an infringement of title. The Court of Appeals for the Second Circuit noted that as "title" was not defined in the policy and as neither New York state courts nor industry usage provided insight as to the meaning of the term, it had to look to federal case law to ascertain its meaning in the context of infringement. The Court found that based upon the majority of federal courts addressing this issue, "title" means the name or appellation of a product and does not cover design elements such as pocket stitching that may serve as a trademark designating the origin of a product. As such, the Court stated that it had no difficulty in concluding that the stitching on the jeans could not fairly be called the name or appellation of that pair of jeans and, thus, was not a title in the context of infringement. Nevertheless, the Court indicated while the duty to indemnify had clearly not been triggered, if there was any residual uncertainty as to whether "title" was unambiguous, then Charter still had a duty to defend. In this regard, while the vast majority of federal courts have unambiguously defined "title" to mean a word or phrase, a handful had defined it in a way that could arguably include a design or symbol similar to the pocket stitching at issue here. Accordingly, the Court found that that "these cases created enough legal uncertainty around the meaning of 'title' to 'give[] rise to (an at least temporary) duty to defend…until the uncertainty surrounding the term was resolved.'" Therefore, while there was not sufficient ambiguity to invoke the *contra proferentem* presumption that would trigger a duty to indemnify, there was nonetheless, at the time of the filing of the underlying action, sufficient uncertainty about the scope of coverage to trigger Charter's duty to defend.

HOMEOWNERS' INSURANCE

James P. McGowan v. Great Northern Ins. Co., 2013 WL 1317095 (2d Dept. Apr. 3, 2013). In January 2004, a pipe burst in a guest house on property that James McGowan owned in East Norwich, New York. As a result, McGowan filed a claim with his homeowners' insurer, Great Northern Insurance Company, which reimbursed him for the cost of the repair. In December 2006, McGowan learned that an odor emanating from the guest house, which was initially detected during the fall of 2006, was caused by mold. McGowan subsequently filed a claim with Great Northern, but the claim was denied. In 2008, McGowan commenced an action against Great Northern to recover for losses caused by mold contamination and for mold remediation expenses. The case proceeded to trial and a jury attributed the mold contamination to the pipe burst in 2004 and awarded McGowan compensatory damages. Great Northern appealed the trial court's decision, arguing that the action was time-barred by the limitations period contained in the policy which provided that an action had to be commenced two years "after the loss occurs". The Second Department found that the policy's limitations period was ambiguous as it lacked specificity as to the event insured against and did not include precise phrases such as "date of loss" or "after inception of the loss" and, thus, the provision was construed against its drafter, Great Northern. In this regard, the Court held that the two-year period did

not begin to run when the pipe burst in January 2004, but in 2007, as it was at that time when all the facts necessary to the cause of action accrued, entitling McGowan to seek relief in court.

MISCELLANEOUS

J.P. Morgan Securities, Inc. v. Vigilant Ins. Co., 2013 WL 2475864 (Ct. of App. June 11, 2013). In 2003, the SEC, among others, undertook an investigation of Bear Stearns & Co., Inc. and Bear Stearns Securities Corp. for allegedly facilitating late trading and deceptive market timing on behalf of certain customers (predominately large hedge funds) in the purchase and sale of shares in mutual funds. During the course of the investigation, the SEC notified Bear Stearns of its intention to commence a civil proceeding for violating federal securities laws and to seek injunctive relief and sanctions. Bear Stearns disputed the proposed charges asserting, *inter alia*, that it did not share in the profits or benefits from the late trading. Nevertheless, Bear Stearns made a formal offer of settlement in November 2005 and agreed to pay $160 million as "disgorgement" and $90 million as a civil penalty. Bear Stearns then sought indemnification for the $160 million disgorgement payment, among other things, from its insurers—Vigilant Insurance Company, which issued primary professional liability coverage, and six excess carriers. The insurers, however, disclaimed coverage and Bear Stearns commenced a breach of contract and declaratory judgment action which the insurers moved to dismiss. The Court of Appeals noted that although it had not considered the issue, other courts have held that the risk of being ordered to return ill-gotten gains—disgorgement—is not insurable as the return of improperly acquired funds does not constitute a "loss" or "damages" within the meaning of insurance policies and public policy prohibits an insured from receiving indemnification for its own illicit gains. While Bear Stearns did not disagree with those principles, it asserted that they did not prohibit coverage as the bulk of the disgorgement payment—approximately $140 million—represented the improper profits acquired by third-party hedge fund customers, not revenue that Bear Stearns itself pocketed. The Court of Appeals stated that, contrary to the insurers' position, the SEC order did not establish that the $160 million disgorgement payment was predicated on sums that Bear Stearns improperly earned as a result of its securities violations. Rather, the SEC order recited that Bear Stearns' misconduct enabled its "customers to generate hundreds of millions of dollars in profits." As such, the Court found that the documentary evidence did not decisively repudiate Bear Stearns' allegation that the SEC disgorgement payment amount was calculated in large measure on the profits of others. Accordingly, the Court of Appeals held that the insurers were not entitled to dismissal of its coverage claim premised on the nature of the SEC disgorgement payment.

RECENT INSURANCE REGULATIONS AND BILLS

On February 25, 2013, the New York State Department of Financial Services adopted an amendment to 11 NYCRR 216 (Unfair Claims Settlement Practices and Claim Cost Control Measures) which requires mandatory Mediation relative to disputes or contests relative to the outcome of a Hurricane Sandy claim if requested by the insured.

The New York Assembly also recently passed several insurance bills in the wake of Hurricane Sandy. (It should be noted, however, that these bills need to be approved by the Senate and signed by the Governor before they are enacted as law.)

The Assembly approved A. 7455-A which relates to anti-concurrent causation clauses and specifies that where there is both excluded flood damage and covered damage (such as wind damage), the insurer will be required to pay for the covered portion of the damage.

The Assembly also passed A. 5870, which would create a private right of action for violation of N.Y. Ins. Law § 2601 (an unfair clam settlement practice statute), available when insurers and individuals disagree on whether there is coverage for property damage in areas where the Governor has declared a disaster. Under this bill, punitive damages and attorneys' fees are potentially available to policyholders whose claims are unfairly handled by their insurers.

Other bills that were approved include: (i) A. 5570 which would expedite the handling of litigation relative to insurance claims arising out of disasters. Specifically, it mandates that the Court hold a preliminary conference within thirty days after the Request for Judicial Intervention is filed, and that discovery be completed sixty days from the date of the preliminary conference. This bill also requires a mandatory settlement conference to be held fourteen days after the Note of Issue has been filed relative to insurance claims for property damage in a county where the Governor has declared a state of emergency; (ii) A. 1092A which provides insurers with fifteen business days to make a determination as to whether to accept or deny a disaster related claim. (An insurer could, however, grant itself one extension of fifteen business days by notifying the insured in writing as to why the additional time is needed); (iii) A. 2729 which seeks to standardize disclosure requirements with respect to triggers of windstorm deductibles in homeowners' insurance and mandates that the insurers explain how deductibles work; (iv) A. 7453 would require the New York Insurance Superintendent to provide standardized definitions for common terms in personal lines policies; (v) A. 1093 would create a task force to examine insurers' responses to disasters, assess how those responses could be improved, and determine whether policyholders and communities have adequate insurance coverage they can rely on in the event of a disaster; (vi) A. 7452A would amend Insurance Law § 3426(a) to prevent insurers from denying business interruption coverage for a covered peril solely because it is caused, in part, by an excluded peril; (vii) A. 7454 requires insurers which issue personal lines and commercial lines insurance policies to provide copies of the same to policyholders prior to their purchase of insurance and allow policyholders sufficient time to review them; and (viii) A. 2287A which would create a homeowners' bill of rights to educate consumers about coverage and limitations for losses caused by catastrophic events.

LBC&C's INSURANCE INDUSTRY PRACTICE GROUP

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