dri™ The Voice of the Defense Bar

Covered Events

The newsletter of the Insurance Law Committee

8/7/2018

2018 Issue 7

Committee Leadership

Chair
Matthew S. Foy
Gordon Rees Scully Mansukhani LLP
San Francisco, CA

Vice Chair
F. Lane Finch, Jr.
Swift Currie McGhee & Hiers LLP
Birmingham, AL

Editor-in-Chief
Tiffany M. Brown
Meagher & Geer PLLP
Minneapolis, MN

Editor
Rob Friedman
Harman Claytor Corrigan & Wellman PC
Richmond, VA

Click here to view entire Leadership

In This Issue

Featured Articles

Recent Cases of Interest

Leadership Notes

Note from the Editor

By Tiffany Brown

It's officially summer, but it's been hot for a while! And, while I know summer keeps us all busy enjoying vacations, beaches, parks, and everting else outdoors, I hope you find time to read the July edition of *Covered Events*.

Your Insurance Law Committee is also keeping busy. Currently, we are preparing for the DRI Annual Meeting, which takes place October 17–21, at the San Francisco Marriott Marquis Hotel. September is the perfect time to visit the San Francisco, a world-class city with abundant charm and atmosphere. The Annual Meeting is designed to provide attendees with opportunities to engage, learn, connect, and grow. And each day of the Annual Meeting will be jam-packed with spectacular keynote speakers, cutting-edge CLE presentations, and plenty of networking events.

Things get started for the ILC on the first day of the Annual Meeting—Wednesday—when it co-presents "Sexual Harassment Claims in the #MeToo Era" with the Labor and Employment Law Committee. This is a CLE event that will address the handling of sexual harassment claims from the perspective of a well-known employment plaintiffs' attorney, a defense attorney, and a coverage attorney. Topics discussed will include what effect media coverage has had on the value of settlements, how employers have adapted in this environment, and what role EPLI coverage plays in this litigation. Following this CLE event is the Annual Meeting's official Welcome Reception.

Another a not-to-be-missed event is the Networking Reception at The Village on Thursday evening. The Village is a place unlike anywhere in the city—a little offbeat, infused with charm, and coursing with energy in the heart of Downtown San Francisco. Here, you can join your friends and colleagues, and enjoy an evening with a high-tech vibe of fun—experiencing interactive games, virtual reality activities, and music—all while dining on tasty cuisine and sharing great conversation.

We look forward to seeing you in San Francisco. If you haven't already registered, you may view the brochure and register to attend this year's Annual Meeting at: https://www.dri.org/education-cle/annual-meeting

Finally, please mark your calendars for ILC's Insurance Coverage and Practice Symposium, November 29–30 at the Sheraton New York Times Square Hotel in New York. Brochures will be mailed soon!

In the meantime, grab your favorite cold beverage and keep cool while reading Covered Events to stay up to date on important insurance coverage-related decisions across the nation. Enjoy summer!

Tiffany Brown is a partner in the Minneapolis office of Meagher & Geer, P.L.L.P., where she focuses her practice on commercial litigation, with particular emphasis on insurance coverage disputes involving commercial, professional and personal lines of insurance, including breach of contract, declaratory judgments, and bad faith actions. Tiffany's practice also includes E&O liability defense. She has previous experience representing insurance companies in cases involving arson and other insurance fraud.

Personal Lines - Home and Auto Subcommittee

By Laurie Barbe and Keith Marxkors

Bill Graden had shoes so big that it now takes two of us to run the Personal Lines Subcommittee following his retirement, but we are honored to do so and up to the challenge. If your practice includes defending personal auto and homeowners insureds and insurers, including coverage work, come one come all and share your experiences and knowledge. We don't try to solve worldly problems, but we do generate some good discussion with members representing numerous jurisdictions, and hopefully provide some takeaways for you to ponder and use in your own practices. Recent topics include the award of attorney fees, punitive

damages, medical protective orders, and adjusters named as parties to defeat diversity.

We currently have 162 members and would love to hear from you if you or someone you know would like to be included on our Subcommittee distribution list (peer, firm associate, assistant, client, etc.). Our Subcommittee meets quarterly by phone, contributes written articles to DRI publications (including the Featured Article in today's Covered Events), contributes to the Insurance Law Committee's Community Posts, and helps generate topics for ILC seminars. Let us know if you would like to join our party by contacting Laurie Barbe (Laurie.Barbe@Steptoe-Johnson.com) or Keith Marxkors (keith.marxkors.bqf5@statefarm.com).

Laurie Barbe is a member of Steptoe & Johnson PLLC in Morgantown, West Virginia. Keith Marxkors is claim counsel with State Farm in Bloomington, Illinois. They are co-chairs of the Personal Lines – Home and Auto Subcommittee.

Advertising Injury and Personal Injury SLG

By Daniel I. Graham, Jr.

When personal and advertising injury coverage was first introduced, the internet did not exist, there were no personal computers, and only a limited number of businesses had access to facsimile communication over hard-wire telephone lines. Since that time, however, privacy, data security, and intellectual property claims have supplanted centuries-old risks of bodily injury and property damage as a focus of risk managers and underwriters. Given the potential exposures, insurance law practitioners will want to be mindful of how courts have construed personal and advertising injury coverage in the context of these twenty-first century claims.

The Advertising Injury and Personal Injury subcommittee offers its members numerous opportunities to share their insight and experience on personal and advertising injury matters. We author featured articles in the ILC's *Covered Events* newsletter, post on recent legal developments on the ILC's Community page, and speak at DRI Insurance Law seminars. If you are interested in Coverage B topics, and are looking for opportunities to get involved with DRI, I invite you to contact me at dgraham@nicolaidesllp.com for more information. And if our subcommittee isn't for you, please know that the ILC offers its members plenty of other SLGs where they can learn, contribute, and participate. Join us!

Daniel I. Graham, Jr., a founding partner of Nicolaides Fink Thorpe Michaelides Sullivan LLP in Chicago, assists his insurance company clients in both appreciating and navigating the complex coverage issues intellectual property infringement and unfair business practice claims present. He has represented his clients' interests before state and federal courts nationwide, at both the trial and appellate level, and in doing so, helped law addressing the scope of insurance coverage in the context of emerging technology-related coverage issues. Mr. Graham chairs the Advertising Injury and Personal Injury Specialized Litigation Group.

Featured Articles

Agency Theory in Actions Against Co-operative Businesses: Considerations and Case Law

By Danielle N. Malaty

A Winnebago County trial court sitting in Illinois' 4th Appellate District recently granted a cooperative business' motion for summary judgment in a propane explosion case. *Maychszak v. True Value Company*, 15 L 259 (2018). The propane tank exploded, causing the Plaintiff serious bodily harm and permanent disfigurement. Codefendant had allowed the tank to fall into disrepair, along with his trailer, to which the tank was attached. The co-op did not sell the tank to the store, as the store was free to purchase its merchandise from vendors of its choice.

Prior to the explosion, the member store had serviced Codefendant's propane tank pursuant to a "Propane Gas Supply Agreement," to which the cop-op was not a party. The co-op did not manufacture or sell the tank, nor did it service or provide propane for the tank. Plaintiff filed a negligence suit against the member store, but named the co-op as a defendant solely under an agency theory. Specifically, plaintiff alleged that the co-op was liable because the member store was acting as its actual/apparent agent at the time the member store serviced codefendant's tank, and since the member store's alleged negligence caused the tank to explode, the co-op was vicariously liable for plaintiff's resulting injury.

It is important to note the significance of plaintiff's failure to allege direct negligence against the co-op. The Court recognized this in its opinion and echoed the Appellate and Supreme Court of Illinois in holding that actual and/or apparent agency cannot serve as separate and distinct, stand-alone legal theories of recovery and cannot serve as the basis for recovery. *Wilson v. Edward Hosp.*, 2012 IL 112989, 981 N.E.2d 971 (2012).

Critical Characteristics of Co-ops

In an action against a co-op, a plaintiff is put in a precarious position, such that it is nearly impossible to allege any direct negligence against the co-op who has no involvement with the member on a day to day basis. While control over day-to-day operations is nearly codified within the bylaws of a franchise and immediately noticeable upon entering any of its stores, the same cannot be said in the context of a co-op. A plaintiff filing suit against a co-op must typically resort to allegations "by and through" the member and purported agent, who carries the name of an entity, to which it does not answer, at the front of their stores. If a plaintiff cannot produce facts that demonstrate a right to control the manner in which a member accomplishes tasks on a day-to-day basis, there can be no finding of actual agency as a matter of law. *Tansey v. Robinson*, 24 Ill. App. 2d 227, 164 N.E. 2d 272 (1960).

Retailers, restaurants and hotels with well-known, recognizable logos sometimes opt for alternative business structures rather than franchises in order to shield themselves from being held vicariously liable for the tortious conduct of their member stores. A co-op is often named in a lawsuit alongside the member for having the deepest pockets, despite the fact that its only involvement with the member may include discounts on bulk purchases and the obvious benefit of displaying their reputable, recognizable logo on their storefront for purposes of increasing marketability and business development. As distinguished from a franchise structure, co-ops allow their independently owned and operated members to carry products from vendors of their choosing, while not necessarily obligating them to keep a certain amount of their own in stock. So the question then turns to who is in control, and to what degree.

A few notable co-operative business organizations include Ace Hardware, True Value, Best Western, United Western Grocers, and Certified Grocers. It is important to be cognizant of the attention that these household names draw when discussing vicarious liability. If someone is injured during their stay at a Best Western, can liability be imposed on any parent company? Does Ace control the day-to-day activities of the hardware store where plaintiff purchased his defective product? Did the plaintiff rely to his detriment on that bright, shiny sign carrying the logo of Certified Grocers when he walked through its doors? A close look at case law involving these specific co-ops can provide ample guidance on the facts that should be sought from the inception of a suit to rebut allegations of actual and apparent agency.

Summary Judgment Granted on Plaintiff's Actual Agency Claims

The Winnebago trial court considered several questions of law under the theory of agency, both actual and apparent. On the issue of actual agency, the court relied heavily on the absence of control over the retailer's day-to-day activities. In citing *Salisbury v. Chapman Realty and Oliveira-Brooks v. Re/Max Int'l, Inc.*, the Winnebago trial court found that the plaintiff's attempts to establish actual agency based exclusively on the Cooperative Agreement fell flat. 124 Ill App. 3d 1057, 465 N.E.2d 127 (1984); 372 Ill App. 3d 127, 865 N.E.2d 252 (2007).

Co-ops typically have an agreement set in place that defines the parameters of their relationship with a member, and in this case, its terms and conditions were dissected by both of the parties. While the co-op drew the trial court's attention to terms that required its members to identify themselves conspicuously as independent contractors, plaintiff selected anecdotal terms that exhibited minimal amounts of control that only spoke to the general purpose of the store. Notably, plaintiff could not reconcile certain terms that further allowed the member store to utilize the logos of other distributors from whom they purchased products in their inventory.

Plaintiff attempted to draw the court's attention to certain guidelines contained in the agreement for the store's layout (which was limited to one display in the member store), the luxury of having been given the right to use its logo, and a requirement to utilize the co-op as its primary supplier. Plaintiff further argued that the co-op exercised control over the retailer because the agreement instructed the retailer to adhere to the co-op's high standards of honesty, integrity, fair dealing and ethical conduct in how it dealt with its patrons. The Court held that these instructions only served to demonstrate an interest in protecting the co-op's reputation and goodwill, but did not demonstrate control over the store itself. In so ruling, the Court perceived the member store as though it were merely a licensee, rather than an agent.

Further, the Court rejected plaintiff's agency theory because the member agreement never outlined any control over the day-to-day business activities or gave any mandate whatsoever as to how it should operate. The retailer was free to make its own decision when it came to merchandise, and was further free to manage its employees in any way it saw fit. The co-op never exerted any control over the layout of the store and never retained the right to hire or terminate member store personnel, nor was it involved in its hiring process. In addition to these operative facts, the member agreement was supported by testimonial admissions by member employees, including store managers, confirming that the co-op never interacted with them directly, never trained them, and that the co-op was just another brand that they happened to carry.

While the member agreement spoke to some degree of training available to its members, the Winnebago trial court considered it relevant to its decision that any such training only consisted of optional seminars on best business practices. In ruling on the motion, the Court held that plaintiff was unable to prove actual agency without adducing facts that demonstrate an exertion of control over the day-to-day operations of an alleged agent. *Anderson v. Boy Scouts of America, Inc.*, 226 Ill App. 3d 440, 589 N.E.2d 892 (1992).

A decision from the Pennsylvania Courts provided the Winnebago trial court with ample guidance as to how the doctrine of vicarious liability should be applied to an action against a co-op, as this issue has not been heavily litigated in Illinois. *Myszkowski v. Penn Stroud Hotel*, 430 Pa. Super. 315, 634 A.2d 622 (1993). As previously mentioned, Best Western is one of those "big name" companies that operates under the protective business model of a co-operative organization. In *Myszkowski*, *Id.*, a plaintiff filed suit against Best Western under a theory of actual agency, further arguing that, based on a member agreement, Best Western retained the right to take away use of its trade name, while lacking control over the everyday business activities. *Id.* The Court focused on what Best Western lacked in granting its motion for summary judgment: direct, supervisory control.

The trial court further considered a case against a real estate entity with much better facts than those at present. That entity actually had training requirements for its purported agent's employees and even reserved the right to inspect its accounts on a regular basis. Salisbury, Id. Nevertheless, because the entity had no control over the day-to-day activities of the purported agent, the court found no actual agency. Moreover, the trial court considered precedent set forth in a suit against Certified Grocers, another recognizable co-op, wherein the court granted a motion for a directed verdict based upon the fact that it exercised zero day-to-day control over its member store, did not have the power to hire or fire employees, and could only withdraw its permission to use its name and terminate the grocery stores membership for a violation of its rules. *Yassin v. Certified Grocers of Illinois, Inc.*, 150 Ill App. 3d 1052, 502 N.E.2d 315 (1986).

In comparing the facts in both *Yassin*, *Id.*, and *Myszkowski*, *Id.*, the trial court recognized that the co-op retained

the same minimal level control in reserving the power to take away the store's right to use its logo, which the Court deemed insufficient as evidence of actual agency. The big takeaway from the Court's position on actual agency is that the absence of any facts that would demonstrate *direct, supervisory powers* over the method and manner in which the store accomplishes everyday tasks is fatal to a plaintiff's claim.

Summary Judgment Granted on Plaintiff's Apparent Agency

The Winnebago trial court also found the plaintiff's apparent agency claims against the co-op infirm as well. In reaching its decision, the trial court first emphasized that the Plaintiff needed to show facts satisfying the three factors of an apparent agency relationship between the co-op and the member store in order to survive summary judgment; (1) That the co-op held the member store out as its agent at the time Plaintiff was injured; (2) Plaintiff could reasonably believe that an agency relationship existed between the two entities; and (3) The Plaintiff relied on that agency relationship to his detriment. *Oliveira-Brooks v. Re/Max International, Inc.*, *Id*.

In finding that the Plaintiff failed to show facts satisfying the third factor, the trial court reasoned that the Plaintiff did not show evidence that he relied on the member store's apparent authority to act on behalf of the co-op at the time the member store serviced codefendant's propane tank leading to Plaintiff's injury. In reaching this conclusion, the trial court first recited the fact that neither the co-op nor Plaintiff was a party to the Propane Gas Supply Agreement between the member store–which serviced the tank.

Next, the trial court found the co-op's right to summary judgment was clear and free from doubt as to Plaintiff's apparent agency theory since the Plaintiff could not have possibly known that the member store was acting on behalf of the co-op in servicing the propane tank, since the co-op was not a party to Propane Service Agreement. In essence, the trial court concluded that summary judgment was due based on the two agreements at issue, the causes of action as pled in the complaint, and the co-op's ability to take advantage of the Plaintiff's failure to present facts supporting the elements of his claim, while at the same time showcasing case law favorable to the co-op's position.

The Court cited to a decision in a case against Re/Max, a co-op, wherein the plaintiff was unable to demonstrate apparent agency. In that case, plaintiff unsuccessfully relied on a number of facts to demonstrate apparent agency. For example, the purported agent mentioned the name of Re/Max to his clients to grow his business and increase his credibility; wore a pendant with the Re/Max logo; and even had the Re/Max logo affixed to his vehicle. *Id*. The most probative aspect to the *Re/Max* decision is the testimony of plaintiff's son. Specifically, he testified that he recommended Re/Max to his mother as a good company, and further, that she relied on his recommendation to her detriment. *Id*. On the other hand, plaintiff herself did not provide any such testimony. *Id*. The court concluded that Plaintiff had failed to adduce evidence to demonstrate *her own reasonable reliance* on an apparent agency relationship between the purported agent and the co-op. *Id*.

The trial court cited to the *Re/Max* decision in considering plaintiff's attempt to satisfy the requirements it set forth, as the facts were almost synonymous. Plaintiff attempted to rely on the testimony of the codefendant that purchased the propane tank, and since plaintiff himself could not have reasonably concluded that an agency relationship existed, plaintiff submitted to the court *codefendant's state of mind*, rather than his own, to satisfy court's test for apparent agency. Plaintiff's proof of an apparent agency relationship rested on codefendant's admission that he thought the store and the co-op were one in the same when he purchased the propane tank. The Court nevertheless rejected this argument in holding that any "reasonable conclusion" that an agency relationship exists must be made by the injured party who relied on it to his detriment. In so holding, the Court held that it was *plaintiff's* state of mind that was determinative—not that of a third party. *O'Banner v. McDonald's Corp.*, 173 Ill. 2d 208, 670 N.E.2d 632 (1996). Reliance of another cannot be imputed on an injured party in order to establish apparent agency. Other than codefendant, plaintiff could not point to any testimony that comported with codefendant's speculation.

Plaintiff was unable to demonstrate that he himself relied in any way whatsoever on the apparent authority of the store. In fact, the evidence adduced demonstrated that plaintiff was quite familiar with the layout of where the explosion occurred, in addition to the subject trailer and tank, as he had worked as a public safety officer for several years prior to the explosion. Moreover, it was within plaintiff's job description to address propane leaks or address a potential hazard observable by scent or sound. Plaintiff's state of mind carried the day in the Court's determination that apparent agency could not be proved, as no facts were adduced that could demonstrate *his own* reasonable conclusion that agency existed, or that *he himself* detrimentally relied on such a relationship.

Practical Advice for Handling Co-op Cases

When defending a co-op against allegations of actual and apparent agency, the first line of defense is to sit down and talk with your client about their business structure and make sure they understand the nature of the allegations. It is important to understand your co-op's business structure so that you can identify the intent behind the actual agreement in place with respect to its members. Furthermore, it is important to better understand the actual relationship your client has with its members, as well as the members' perception of the co-op. This is how you become fluent in the interplay between the parties involved in a multiparty lawsuit involving your client.

After you have taken these initial steps, you can move on to the second line of defense that occurs during discovery. First, it is important that the protections necessary to defend against these allegations are included and enumerated in the agreement. By having a conversation with your client about their relationship with the co-op, you can identify potential witnesses who may be called by the plaintiff to testify. Once you've identified those individuals, have conversations with them. Identify whether they will testify within the confines of the member agreement, as your motion for summary judgment may very well hinge on what they say under oath.

In addition to preparing for testimony provided by representatives of your co-op, you can begin to prepare for plaintiff's own testimony and any witnesses they may call to support plaintiff's theory. Elicit testimony from the plaintiff wherein they themselves commit to the allegations of actual and apparent agency as their only theory of liability against the co-op, knowing that those allegations are insufficient as a standalone cause of action. Go into plaintiff's discovery deposition knowing that they will not be able to make the leap of claiming they reasonably relied on apparent authority to their detriment, and further knowing that they may not entirely understand the nature of the allegations.

Defending a co-op requires a shrewd understanding of your client's contractual rights of control over their members. Armed with that understanding, take the complaint at face value and attack the cause of action pled at the summary judgment stage rather than providing plaintiff with a roadmap of your defense strategy by highlighting those deficiencies early in the case. Finally, reduce the complexities in a case, where the roles of the defendants risk being confused, down to simple and practical terms which showcase to the court that a plaintiff could not have reasonably relied on an agency relationship to his detriment.

Trends in Other Jurisdictions

The Winnebago Trial Court relied on the Pennsylvania Courts in ruling on this motion due to the lack of litigation involving co-operative business organizations and the narrow distinctions that the Courts must draw between these organizations and a prototypical franchise. While Illinois lacks substantial authority with respect to these distinct entities, other states are creating precedent for imposing vicarious liability on a co-op. In *Murphy v. Holiday Inns, Inc.*, the Supreme Court of Virginia determined that a mere franchise agreement did not make the franchisee an agent of the franchisor. There must exist some control of, or right to control, the methods or details of doing the work. 219 S.E.2d 874 (Va. 1975).

A Maryland Court grappled with a similar fact pattern in *Wood v. Shell Oil Co.*, 495 So. 2d 1034 (Ala. 1986). In *Wood*, *Id.*, the Court noted several factors that are also found in this case. Pursuant to a lease, Parker Shell had purchased gasoline and other products from Shell Oil and had retailed these products to the general public. The employees of Parker Shell received all their compensation and benefits from Parker Shell, and Parker Shell had exclusive authority for hiring and firing them. Parker Shell was not obligated to accept advertising material from Shell Oil; it determined for itself what products, if any, it wished to purchase from Shell Oil and in what quantities; it was free to purchase and sell products of suppliers other than Shell Oil; and it determined the retail price to be charged for the sale of its products. Further, by deposition, the dealer testified that Shell Oil did not interfere in the daily operation of the station and did not inspect the service station's premises for safety. No evidence was adduced that Shell Oil retained any right or control over the manner in which Parker Shell performed in order to meet the requirements of the lease and dealer agreement. Although the lease and the dealer agreement specified what Parker Shell must do in order to conform to the terms of these contracts, and gave Shell Oil the right to approve certain aspects of Parker Shell's operation, in no way did Shell Oil determine how Parker Shell was to achieve compliance with those terms.

The Courts in North Carolina have followed the trend of other jurisdictions in finding that a principal's vicarious liability for the torts of his agent depends on the degree of control retained by the principal over the details of the work *as it is being performed*. The controlling principal is that vicarious liability arises from the right of supervision

and control. *Vaughn v. North Carolina Dept. of Human Resources*, 252 S.E.2d 792 (N.C. 1979). South Carolina Courts have also followed suit in finding that liability depends upon the existence of an agency relationship, which is determined by the nature and extent of control and supervision retained and exercised by the franchisor over the methods or details of conducting the day-to-day operation. *Fernander v. Thigpen*, 293 S.E.2d 424 (S.C. 1982).

Similarly in Michigan, Defendant contended that, while it owned the land where a restaurant was located, it did not actually occupy or control a restaurant's premises, and thus was not a "possessor" liable for the plaintiff's injuries. *Little v. Howard Johnson Co.*, 455 N.W.2d 390 (Mich. 1990). Plaintiff contended that the mere fact that defendant owned the land on which the restaurant was situated created a question existed regarding defendant's direct liability. The Court disagreed in finding that title ownership of the premises is not determinative and thus fails to create an issue of material fact. The Court concluded that it is the possessor or occupier of land, not necessarily the titleholder, who owes a duty to invitees regarding the condition of the land.

The Georgia Courts took a strong position against the determinativeness of a written document establishing a franchisor/franchisee relationship. *Washington Road Properties v. Home Ins. Co.*, 145 Ga. App. 782, 784, 245 S.E.2d 15 (1978). In *Washington*, the fact that a contract was labeled a franchise agreement was not necessarily controlling, and the Courts must look to the contents to determine the character of the relationship created. *Id.*

Conclusion

Walking into any fast food chain or coffee store, it becomes readily apparent that someone is in charge of how things are organized and how tasks are performed, ranging from how the napkins are arranged, to the methods in which safety policies and procedures are implemented. Because of this apparent relationship to a parent organization, companies are often held liable for the tortious conduct of its franchisees, even though they played no contributory role in an alleged breach of duty. Organizing as a co-op rather than a franchise substantially limits a company's exposure to risk while still cultivating a profitable business structure. A company can find it much easier to separate itself from the tortious conduct of an alleged agent, over which they may have absolutely no control and for conduct which they should not be held liable.

It will be interesting to see how this business structure is treated by the courts in the coming years. However, at present, co-op defense is still in its formative years. This decision is a reminder of how much facts matter. By understanding your company's business structure, reading the agreement between the company and its members, and adducing the right testimony during discovery regarding the company's right of control over a securing agent, a zealous defense attorney can successfully defend a co-op, even in the absence of substantial legal precedent.

Danielle N. Malaty is an associate of Kopka Pinkus Dolin pc in Chicago, where she concentrates her practice on premises liability, product liability, employment law, municipal/public entity, construction, commercial transportation, contract breach, professional liability, and general insurance defense. Her clients include retailers, restaurants, property management companies, hardware stores, product manufacturers, cooperative business organizations, grocery stores, shopping centers, general contractors, sub-contractors, police departments, municipalities, and trucking/transportation entities.

I Know What You Mean

Recent Decisions Construing "Personal and Advertising Injury" Coverage for False Advertising and Deceptive Trade Practice Claims

By Thomas W. Arvanitis

Rapid developments in technology and the regulatory environment have spawned significant changes in the breadth and complexity of claims liability insurers face. In this ever-evolving landscape, it is vital for insurance law practitioners to be aware of how courts are defining the contours of "personal advertising injury" coverage in the context of both traditional and 21st century claims, because these claims are often high-stakes, "bet the company" exposures. Business disputes between aggressive competitors that spare no expense give rise not only to potentially massive damage awards, but skyrocketing litigation costs. Faced with these new and significant exposures, insureds are looking to their "personal and advertising injury" coverage more than ever for a defense and indemnity. And this is particularly true where an insured faces false advertising and deceptive trade practice claims.

But under what circumstances will these claims implicate the "personal and advertising injury" coverage? And when? This article will discuss a couple of recent decisions that illustrate the different approaches courts have taken in evaluating an insurer's obligations under the "personal and advertising injury" coverage in the context of false advertising and deceptive trade practice claims.

Recent Decisions Assessing the Application of the Disparagement Offense in the Context of False Advertisement Claims

For an insurer's duty to defend a lawsuit to exist under the "personal and advertising injury" liability coverage, the insured must establish (among other things) that the lawsuit at least potentially seeks damages that are within the scope of one of the enumerated "personal and advertising injury" offenses. Oftentimes, these offenses include injury arising out of oral or written publication of material, in any manner, of material that slanders or libels a person or organization or disparages a person's or organization's goods, products or services ("disparagement offense").

To potentially implicate the disparagement offense, the insured must allegedly: (1) publish material, either in writing or orally, (2) that disparages the claimant's goods, products, or services. To constitute "disparagement," the statement must be made about a competitor's goods; it must be untrue or misleading; and it must be made to influence or tend to influence the public not to buy those goods or services. *Pekin Ins. Co. v. Phelan*, 799 N.E.2d 523, 526 (Ill. App. Ct. 2003).

Over the past several years, there has been a steady rise in the number of cases addressing coverage under the disparagement offense, despite no express claim against the insured for slander, libel, or disparagement. These cases often emanate from disputes in which the insured is alleged to have falsely advertised its products, infringed a competitor's intellectual property, or made "knock-offs" or inferior versions of the competitor's products. The question becomes whether these allegations involve a statement that implicitly references the competitor and, if so, whether the statement says something false or derogatory. If so, some courts have found a potential claim for implied disparagement sufficient to trigger an insurer's duty to defend.

For example, in *Jar Laboratories, LLC v. Great American E&S Insurance Co.*, 945 F. Supp. 2d 937 (N.D. Ill. 2013), the insured was sued for false advertising based on statements it made about its over-the-counter pharmaceutical product, LidoPatch, that allegedly caused the distributor of a competing prescription product, Lidoderm, to suffer damaged goodwill and lost profits. The insured's false advertising allegedly included statements that its product would provide the same benefits as the "prescription brand" and had the "same active ingredient as leading prescription patch." Although the insured never mentioned Lidoderm by name, the court found that its statements were clear references to the insured's competing product. Because the insured implicitly equated the competitor's product with the insured's allegedly inferior product, the court found the underlying complaint alleged a potential claim for implied disparagement, triggering a duty to defend.

That is not to say that false advertisement claims necessarily involve implied disparagement for purposes of "personal and advertising injury" coverage, however.

Take *Albion Engineering Co. v. Hartford Fire Insurance Co.*, No. 1:17-cv-3569, 2018 WL 1469046 (D.N.J. Mar. 26, 2018) (New Jersey law), in which the insured was sued by a competitor for falsely advertising its caulking guns as made in the U.S.A., when they were actually made in Taiwan. The competitor alleged that it distinguished its competing caulking guns based on their manufacture in the United States, and that the insured's false advertising resulted in lost sales and damage to the competitor's reputation.

In analyzing whether the disparagement offense was triggered, the *Albion* court found that an action for product disparagement or trade libel requires: (1) a publication; (2) with malice; (3) of false allegations concerning the plaintiff's property or product; and (4) special damages. The insured's alleged false representation that its products were made in the U.S.A. contained no statement that referenced the claimant, explicitly or implicitly. The court therefore concluded that the underlying complaint failed to allege a potential claim under the disparagement offense.

Albion is in line with other recent decisions finding that an insured's false statements about its own products, which do not necessarily refer to and derogate a competitor's product or clearly imply the inferiority of the competitor's product, do not give rise to a potential claim for disparagement by implication, and thus do not implicate the disparagement offense. *See*, *e.g.*, *Vitamin Health, Inc. v. Hartford Cas. Ins. Co.*, 685 Fed. App'x 477 (6th Cir. 2017) (Michigan law); *Charter Oak Ins. Co. v. Maglio Fresh Foods*, 629 Fed. App'x 239 (3d Cir. 2015) (Pennsylvania law).

Even when an insured is alleged to have made a false statement that expressly references the claimant, there may be no coverage under the disparagement offense absent a claim for damage to the claimant's reputation. For example, in *Cincinnati Insurance Co. v. Zaycon Foods, LLC*, No. 2:17-cv-140, 2018 WL 847247 (E.D. Wash. Feb. 13, 2018) (Washington law), the insured, Zaycon Foods LLC, faced claims for violations of securities laws, fraud, negligent misrepresentation, breach of fiduciary duty, and others related to the ouster of Zaycon's CEO. Zaycon argued there was a duty to defend allegations that it falsely represented the former CEO's position on a deal to obtain votes from Zaycon members for his removal. The court found that, under Washington law, defamation is concerned with compensating the injured party for damage to reputation. Although Zaycon allegedly made a false statement about the claimant, nowhere was it alleged that the claimant suffered reputational harm, or that the claimant sought damages for any such injury. Therefore, the court found the insurer did not have a duty to defend under the disparagement offense.

Recent Decisions Construing Policy Exclusions in the Context of False Advertisement and Deceptive Trade Practice Claims

Even if a lawsuit's false advertisement or deceptive trade practice allegations can be construed as potentially seeking damages that implicate the disparagement offense, exclusions applicable to Coverage B. could limit or possibly exclude coverage with respect to such damages.

For example, in *Scott, Blane, and Darren Recovery, LLC v. Auto-Owners Insurance Company*, No. 17-12945, 2018 WL 1611256 (11th Cir. April 3, 2018) (unpublished), the Eleventh Circuit, applying Florida law, found the "quality of goods" exclusion precluded a duty to defend allegations that the insured falsely advertised the quality of its tuna meat.

The insured, Anova Food, Inc., advertised that it preserved its sashimi-grade tuna using a natural wood smoking process, without the use of additives or chemicals. King Tuna, Anova's competitor, alleged the insured was actually using synthetic carbon monoxide to give its tuna the bright red color favored by consumers. King Tuna also alleged that Anova falsely advertised its tuna meat as "superior to its competitor's offerings" based on its wood chip smoking process. King Tuna filed two suits against Anova for false advertising under the Lanham Act and unfair trade practices.

Anova's insurer, Auto-Owners Insurance Co., declined a duty to defend. After incurring over $3.5 million to defeat King Tuna's claims, Anova sued Auto-Owners for breach of contract and bad faith. Anova sought coverage under the disparagement offense.

The district court found the disparagement offense was not triggered because Anova's statements were directed generally to its competition, not specifically to King Tuna, and therefore did not support a claim for express or implied disparagement.

After a detailed summary of the parties' positions, the Eleventh Circuit declined to rule on the issue. The court found that, even if King Tuna alleged a potential claim for implied disparagement, coverage was nevertheless precluded by the exclusion for "advertising injury" arising out of the "failure of the insured's goods, products or services to conform with advertised quality or performance." The Eleventh Circuit reasoned that the underlying lawsuits

accused Anova of misrepresenting the nature, characteristics and qualities of its tuna products by claiming they were prepared in a manner different from Anova's actual methods of preparation. The court therefore concluded the suits "arose from the alleged failure of Anova's products to conform to their advertised quality," and were excluded from coverage.

The Scott decision is a reminder of the key role the "quality of goods" exclusion may play in limiting coverage for potential claims of implied disparagement, particularly when the insured's advertised claims of superiority are based solely on false statements concerning the quality of its own goods, products or services.

In contrast, the recent decision captioned *West Bend Mutual Ins. Co. v. Ixthus Medical Supply, Inc., et al.*, No. 2017AP909, 2018 WL 1583124 (Wis. Ct. App. Mar. 28, 2018) (unpublished), illustrates the reluctance courts exercise in applying policy exclusions predicated on an insured's intentional conduct. In *West Bend*, the Wisconsin Court of Appeals found West Bend had a duty to defend its insured against allegations of willful misconduct and fraud, because the underlying complaint included causes of action that did not require proof of intentional wrongdoing.

The insured, Ixthus Medical Supply, was sued by Abbott Laboratories for deceptive business practices, unfair competition, trademark and trade dress infringement, and fraud. Abbott sold blood-glucose test strips for international use that did not comply with U.S. regulations, and were cheaper than their domestic counterpart. Abbott alleged that Ixthus illegally conspired to pass off Abbott's test strips as domestic test strips that qualified for Medicare and Medicaid reimbursement. Ixthus then allegedly falsified rebate claims submitted to Abbott. Ixthus allegedly knew its diversion of the test strips was illegal, and constituted criminal mail, wire, and insurance fraud.

West Bend denied a duty to defend based, in part, on the exclusion for "personal and advertising injury" "caused by or at the direction of the insured with the knowledge that the act would violate the rights of another and would inflict 'personal and advertising injury.'" The trial court agreed with West Bend, finding the exclusion applied because the underlying complaint alleged only willful misconduct by Ixthus.

The insurer's victory, however, was short-lived. On appeal, Ixthus and Abbott successfully argued that, regardless of whether a complaint alleges a policyholder knowingly committed a wrongful act, an insurer has a duty to defend if the policyholder could face liability without a showing of intentional conduct. Abbott's complaint included strict liability claims for trademark dilution and deceptive trade practices under the Lanham Act and New York law. Because Ixthus could face liability under these causes of action regardless of its intent, the court found Ixthus faced potential liability for which the exclusion would not apply.

West Bend argued on appeal that, because the duty to defend is determined by the facts alleged rather than the theories of liability, coverage for Abbott's lawsuit was excluded because the complaint alleged only a fraudulent, criminal scheme. The West Bend court was not persuaded by the argument. It noted that, although some of the counts included allegations of intentional misconduct, others did not. The court also rejected West Bend's argument that the exclusion nevertheless applied because each count incorporated by reference the allegations of willful misconduct and criminal fraud set forth in the body of the complaint.

The *West Bend* decision thus serves as a reminder of the challenges insurers face in some jurisdictions when relying on Coverage B's intent-based exclusions to deny a duty to defend.

Conclusion

This article, which expresses the opinions of the author and does not necessarily reflect the views of Nicolaides Fink Thorpe Michaelides Sullivan LLP or its clients, demonstrates the different approaches courts have recently taken in construing the circumstances in which a false advertisement or deceptive trade practice claim may implicate a liability policy's "personal and advertising injury" coverage. Each claim requires a fact-specific inquiry, to be sure. Even so, given the potential exposure that "personal and advertising injury" claims present, insurance law practitioners will want to be mindful of the ever-evolving, developments in case law construing the scope of "personal and advertising injury" coverage in the context of false advertisement and deceptive trade practice claims.

Thomas W. Arvanitis is a partner of Nicolaides Fink Thorne Michaelides Sullivan LLP in Chicago, where he focuses his practice in insurance coverage counseling and litigation. He has significant experience advising insurers on coverage issues with respect to personal and advertising injury coverage, including intellectual property claims, privacy claims, defamation claims, false imprisonment and malicious prosecution claims. *The author would like to thank associates Meaghan Sweeney and Emily Steinberg for their assistance in the development of this article.*

First Circuit

Sexual Assault Exclusions/"Arising Out Of" (MA)

In a case that we argued for AIG back in February, the First Circuit ruled last week in *AIG Property Cas. Co. v. Cosby*, No. 17-1505 (1st Cir. June 7, 2018), that a Massachusetts District Court was correct in ruling that a sexual abuse exclusion in AIG's homeowner's policy did not unambiguously precluded numerous suits by women who claim that Cosby defamed them in denying their allegations of rape and sexual assault. The court did not reach the issue of whether the coverage triggering allegations of sexual assault "arose out of" the original incidents of assault, holding instead merely that the exclusion in AIG's homeowner's policy was ambiguous with respect to such claims because the umbrella policy issued to Cosby had different language in a separate sexual assault exclusion for "Limited Charitable Trustees and Directors Liability."

Michael Aylward
Morrison Mahoney
Boston, MA

Second Circuit

Choice of Law/Contestability of Life Insurance Policy (NY)

***AEI Life LLC v. Lincoln Benefit Life Co.*, No 17-224, --- F.3d ---, 2018 WL 2746589 (2d Cir. June 8, 2018)**

The U.S. Court of Appeals for the Second Circuit held that 1) a clause in a life insurance policy stating that the policy "is subject to the laws of the state where the application was signed" was not a choice-of-law provision, and 2) under New York law, the policy was incontestable for fraud because the challenge was brought later than the two-year contestability period. Lincoln Benefit Life Company (Lincoln) issued the policy in 2008, insuring the life of Gabriela Fischer, a New York resident. The policy was sold a few times, ultimately to AEI Life LLC (AEI). When Lincoln discovered what it believed to be fraudulent acts in the application for the policy, it tried to invalidate the policy. Lincoln argued that New Jersey law applied because it believed the application was signed in New Jersey, and a clause in the policy (called a "conformity" clause by the court) stated that the policy "is subject to the laws of the state where the application was signed." Importantly, New Jersey law allows for a life insurance policy to be contested even after the two-year contestability period expires. The appellate court found that this clause was not a choice-of-law provision "because it does not reflect the parties' intent to select the law of a specified state." The appellate court applied New York's conflicts law and found that the "center of gravity" of the transaction was in New York—the policyholder and her son were domiciled in New York, and the broker solicited the business in New York. Under New York law, Lincoln was barred from contesting the policy after the two-year contestability period. The appellate court also rejected Lincoln's substantive challenges to the validity of the policy because the incontestability law did not allow for such exceptions.

Charles W. Browning
Elaine M. Pohl
Patrick E. Winters
Plunkett Cooney
Bloomfield Hills, MI

Two-Year Suit Limitation (NY)

***Classic Laundry and Linen Corp. v. Travelers Casualty Ins. Co.,* June 26, 2018**

Classic Laundry and Linen Corp ("Classic") purchased a policy from Travelers which provided coverage for damage to Classic's business personal property and any business income loss or incurred extra expense resulting from any covered loss. The policy's suit limitation provision stated that "no one may bring a legal action against [Travelers] under this Coverage form unless … the action is brought within 2 years after the date on which the direct physical loss or damage occurred."

On May 1, 2013, there was a fire at Classic's business premises. Travelers paid the business property damage claim, but denied coverage for business income and incurred expenses. The basis for the denial was, in part, Classic's failure to timely return an executed sworn statement providing for and detailing its losses. Classic then sued Travelers on that claim in an action on March 3, 2016.

The Second Circuit found the suit limitation clause to be unambiguous. As above, no one could bring action against the carrier under the coverage provided unless that action was brought within two years after the "date on which the direct physical loss or damage occurred." (emphasis supplied by the Court). New York precedent has repeatedly

held that this refers to the date on which the physical loss, casualty, or accident took place, not the day on which the insured's claim accrued. This means that the clock starts running from the occurrence, whether that be the accident at issue or fire at a property. While the business income loss might actually take place after that time, the suit limitation clause is clear. Moreover, not only did the court find the clause unambiguous, they also found it reasonable and therefore clearly enforceable. Classic's claim for further coverage was therefore barred.

Agnes A. Wilewicz
Hurwitz & Fine, P.C.
Buffalo, NY

Third Circuit

Arbitration Clauses (NJ)

The Third Circuit has ruled that a former ACE Vice President's suit against the insurer for allegedly discharging him after he protested the destruction of materials in violation of "litigation hold" notices must be arbitrated. In granting ACE's motion to compel arbitration, the Third Circuit ruled in Ace American Ins. Co. v. Guerriero, No. 17-2893 (3rd Cir. June 20, 2018) that Guerriero had, in fact, signed an "arbitration agreement" on his first day of employment which stated that he would "submit any employment-related legal claims to final and binding neutral third-party arbitration …"

Michael Aylward
Morrison Mahoney
Boston, MA

Faulty Workmanship Exclusion (NJ)

***Lenick Constr., Inc. v. Selective Way Ins. Co.*, June 6, 2018**

US Court of Appeals Holds Insurer had no Duty to Defend or Indemnify its Insured in Underlying Action Where Insured's Own Faulty Workmanship was the Only Legal Theory Under Which the Insured Could be Held Liable This declaratory-judgment action arises out of an underlying construction defects action involving the construction of a condominium development. A number of entities, collectively referred to as Westrum, were hired as the general contractor for the 92-unit development, and it subcontracted with Lenick Construction, Inc. ("Lenick") to perform rough and finish carpentry and to install paneling, windows, and doors provided by the developer. Upon completion of the project, it was discovered that some units experienced water infiltration, leaks, and cracked drywall.

In the underlying action, the Villas at Packer Park Condominium Association sued Westrum alleging contract and warranty claims. Westrum impleaded Lenick (and others), asserting claims for breach of contract and indemnification.

Soon after being named as a defendant, Lenick notified its insurer, Selective Way Insurance Company ("Selective") of the claims, claiming that the commercial general liability (CGL) policy in effect when the defects were discovered entitled Lenick to defense and indemnification. Selective initially denied Lenick's request, but eventually agreed to defend Lenick, subject to a reservation of rights.

In response to Selective's reservation of rights, Lenick commenced a declaratory-judgment action seeking a declaration that Selective was obliged to defend and indemnify Lenick. After removal to federal court, the parties filed cross-motions for summary judgment regarding Selective's duty to defend. Selective also sought summary judgment on its duty to indemnify. The District Court concluded that the allegations against Lenick were not covered under its CGL policy. As such, the District Court held that Selective had no duty to defend or indemnify Lenick. Thereafter, Lenick filed an appeal.

In determining whether a duty to defend existed, the Court of Appeals first reviewed the policy language to determine when it provides coverage, and then examined the underlying complaint against the insured to determine whether the allegations triggered coverage.

The Selective policy at issue insured against bodily injury and property damage caused by an "occurrence," which was defined as "an accident, including continuous or repeated exposure to substantially the same general harmful conditions." Lenick argued that the pleadings established occurrences under Pennsylvania law in three ways: (1) the damage occurred to areas of the property on which Lenick did not work, (2) the damage was caused by work performed by other subcontractors, and (3) the damage was caused by defects in the materials that Lenick used rather than by its own faulty workmanship. In response, Selective argued that Lenick's liability arises from its own faulty workmanship, which is not covered as an occurrence under the policy.

Lenick acknowledged that under Pennsylvania law, there is no occurrence when the complaint alleges only property damage from poor workmanship to the work product itself. However, Lenick pointed out that the various complaints identified leaks, water infiltration, and cracked drywall,

which were unrelated to Lenick's work. Lenick argued that, if presented with this question, the Pennsylvania Supreme Court would find that "consequential damages beyond the work itself are "occurrences' under CGL policies." The Court of Appeals disagreed and noted prior case law holding that damages that are a reasonably foreseeable result of the faulty workmanship are not covered, even when such damage occurs to areas outside the work provided by the insured. The Court further noted that as the Pennsylvania Supreme Court has not subsequently issued a contrary opinion, the case law referenced by the Court still controls.

With regard to Lenick's second argument, the Court of Appeals disregarded the affidavits Lenick relied on and looked only at the allegations against Lenick in the underlying complaints. The Court noted and agreed with the District Court's findings that although the various complaints asserted that others may be liable for the property damage, they did not allege that Lenick should be held liable for the faulty products or poor workmanship of others and that Lenick's own faulty workmanship was the only legal theory under which Lenick, as opposed to other contractors or subcontractors, could be found liable.

Lastly, the Court of Appeals held that Lenick's argument that the property damage was caused by defects in the materials provided to it by the developer lacked support in the underlying pleadings. The Court noted that Lenick pointed only to extrinsic evidence to support this argument. Because the underlying pleadings did not contain allegations sufficient to support a claim that the windows, doors, and/or panels used by Lenick "actively malfunctioned, directly and proximately causing" the property damage to the project, the Court found that such an argument fails. Accordingly, the Court affirmed the District Court's decision holding that Selective had no duty to defend or indemnify Lenick relative to the underlying action.

Brian F. Mark
Hurwitz & Fine, P.C.
Buffalo, NY

Fifth Circuit

Equitable Lien Doctrine (TX)

***Sierra Equip., Inc. v. Lexington Ins. Co.*, No. 17-10076, --- Fed. Appx ---, 2018 WL 2222695 (5th Cir. May 15, 2018)**

The U.S. Court of Appeals for the Fifth Circuit held that Sierra Equipment Inc. (Sierra) lacked standing to sue Lexington Insurance Co. (Lexington) as Sierra was not identified in any loss payable clause in the property insurance policy that Lexington issued to LWL Management Inc. (LWL). Sierra had leased equipment to LWL under a lease agreement that required "LWL to insure the leased equipment, deliver a copy of the insurance policy to Sierra, and obtain a policy in form, in terms, in amount, and with insurance carriers reasonably satisfactory to Sierra." The agreement did not "require that the policy list Sierra as an additional insured or contain a loss payable clause listing Sierra."

After discovering that the equipment LWL had leased was lost, damaged or destroyed, Sierra initiated suit against Lexington seeking recovery under the policy. Lexington, however, argued that Sierra lacked standing to maintain such a suit. The appellate court first recognized that an "insurance policy is a personal contract between the insurer and the insured named in the policy and a stranger to the policy may not ordinarily maintain a suit on it." The appellate court also recognized that the equitable lien doctrine represented an exception, applying "in such instances as those where a mortgagor or lessee is charged with the duty of procuring such a policy with loss payable to the mortgagee or lessor."

Sierra argued its lease agreement with LWL qualified as such an agreement, especially as "LWL was required to deliver the insurance policy to Sierra and obtain a policy in terms satisfactory to Sierra." The appellate court ultimately disagreed, finding that "the agreement between Sierra and LWL did not require that LWL obtain insurance with a loss payable clause to Sierra … [a]nd the Lexington policy does not contain such a clause[,]" such that "Sierra, who was not a party to the insurance policy, does not have standing to sue Lexington."

Charles W. Browning
Elaine M. Pohl
Patrick E. Winters
Plunkett Cooney
Bloomfield Hills, MI

Eighth Circuit

Business Income Coverage (AR)

***Welspun Pipes Inc. v. Liberty Mutual Fire Ins. Co.*, No. 17-1470, --- F.3d ---, 2018 WL 2376479 (8th Cir. May 25, 2018)**

The U.S. Court of Appeals for the Eighth Circuit held that Liberty Mutual Fire Insurance Company (Liberty Mutual) need not provide coverage for expenses incurred by

Welspun Pipes Inc. (Welspun) when it moved production overseas following a fire at its Little Rock plant. The Liberty Mutual policy covered loss of income, as well as certain expenses incurred to mitigate the loss of income, during a time period defined in the policy. Welspun sought coverage for business income as well as more than $13 million in expenses associated with moving production to India in order to comply with contract deadlines. The appellate court agreed with the district court's finding that these expenses were not covered because they were not "necessary" costs (as defined in the policy) that mitigated Welspun's lost income amounts that would need to be covered by Liberty Mutual. The appellate court noted that Welspun's reading of the policy would actually increase Liberty Mutual's obligation to an amount higher than if the insured had not mitigated the loss at all – an outcome that was specifically made impermissible by the policy.

Charles W. Browning
Elaine M. Pohl
Patrick E. Winters
Plunkett Cooney
Bloomfield Hills, MI

Ninth Circuit

D&O/"Professional Services" Exclusion (CA)

The US Court of Appeals for the 9th Circuit has ruled in ***Hotchalk, Inc. v. Scottsdale Ins. Co.***, No.: 16-17287 (9th Cir. June 4, 2018) that qui tam claims against a vendor of online educational technology in which the claimants alleged that Hotchalk had violated federal regulations concerning the involvement of students who received financial aid are subject to an exclusion for a "professional services" under Scottsdale's Directors and Officers policy. In an unpublished opinion, the Ninth Circuit affirmed the California District Court's declaration that services that Hotchalk provided to universities, including its recruitment services, are "professional services" subject to this exclusion.

Michael Aylward
Morrison Mahoney
Boston, MA

Limits of Liability (AZ)

In an Arizona dispute between and excess insurer and a primary insurer concerning the available primary limits for an individual who was seriously injured in the insured's parking garage, the Ninth Circuit has ruled in ***Scottsdale Ins. Co. v. Hudson Specialty Ins. Co.***, No. 17-15875 (9th Cir. June 18, 2018)(unpublished) that Hudson only owed $1 million, rejecting Scottsdale's argument that the primary policy owed both the $1 million general liability limit and a separate $1 million in coverage pursuant to a "claims made" Parking Errors and Omissions endorsement.

Michael Aylward
Morrison Mahoney
Boston, MA

Bad Faith (WA)

***Bridgham-Morrison v. National General Assurance Company*, June 22, 2018**

Insurer did not Act in Bad Faith by Failing to Intuit Plaintiff's Damages After an automobile accident, NGAC paid Plaintiff the policy maximum under her personal injury protection (PIP) policy, and the motorist who struck Plaintiff's vehicle paid his insurance policy maximum. Plaintiff then sought to recover additional damages under her underinsured motorist (UIM) policy. In fall 2013, after offsetting for money already received under the PIP policy and from the motorist's insurer, NGAC offered Plaintiff an additional $20,000 to settle her claim. In total, the insurance payments covered Plaintiff's then-documented economic damages and gave an additional sum for non-economic damages based on internal NGAC estimates. Plaintiff rejected this offer and negotiations stalled and no settlement was reached.

Plaintiff hired a new attorney in late 2013, and between December 2013 and October 2014, Plaintiff's new attorney sent many letters demanding a payment higher than the $20,000 that NGAC had previously offered. Those letters gave little to no explanation for why a higher payment would be appropriate, and they did not document a justification for additional payments. In early 2014 an NGAC claims adjuster had some questions about causation and asked Plaintiff for additional employment and medical documentation. Despite repeated requests, Plaintiff refused to turn over these documents until April 2015, on the eve of litigation. Eventually, but only after litigation started, NGAC tendered the policy maximum.

Plaintiff argued that NGAC's investigation was unreasonable because it did not include certain categories of economic and non-economic damages. Most of these claimed damages were never mentioned by Plaintiff before litigation, and they were not included in Plaintiff's initial demands. Plaintiff contended that NGAC had a duty to investigate these damages whether or not she ever claimed them.

This argument was rejected by the Court. NGAC granted coverage for all documented economic damages, and

estimated non-economic damages based on the records Plaintiff provided. In early communications with NGAC, Plaintiff's counsel represented that Plaintiff had largely recovered from her injuries and was able to get back to work after her second shoulder surgery. In such

circumstances, NGAC could reasonably have concluded that the information given before NGAC's settlement offer was all that was necessary to evaluate the claim. That NGAC may not have covered some categories of damages did not make their investigation unreasonable, especially where Plaintiff was represented by counsel, those damages were never claimed by Plaintiff, and Plaintiff refused to turn over medical and employment documents requested by NGAC.

The Court declined to hold that Washington law imposes a duty on an insurer to intuit what a plaintiff's damages might be. While Plaintiff claimed that the valuation of her non-economic damages was too low, disagreement about the amount of damages based on available evidence cannot ground a claim for failure to investigate.

Plaintiff also argued that NGAC's settlement offers were unreasonable because NGAC offered less than was ultimately recovered, and because NGAC forced Plaintiff into litigation to recover what she was owed under the policy. A disparity between an offer and the amount ultimately recovered does not, on its own, give a basis for a claim of bad faith—the plaintiff must show something more.

Plaintiff contended that NGAC had two different internal estimates of damages for her shoulder injury, and that NGAC's initial offer was based on the lower estimate. This, she claimed, supported her contention that the offer was unreasonably low. However, the Court noted that assessing non-economic damages is hardly scientific. An internal disagreement within NGAC about the amount of non-economic damages does not show that the second estimate on which the offer was based was unreasonable.

Plaintiff also argued that violations of Washington state insurance regulations are per se IFCA violations and per se good faith violations, and that there were material disputes of fact as to whether NGAC violated some of the regulations. However, the Washington Supreme Court has held that merely violating a regulation is not a per se violation of the IFCA. A court must still assess whether the insurer acted unreasonably. Based on the record presented, no reasonable juror could conclude that NGAC acted unreasonably.

Brian D. Barnas
Hurwitz & Fine, P.C.
Buffalo, NY

Tenth Circuit

Professional Liability (CO)

***Evanston Ins. Co. v. Law Office of Michael P. Medved, P.C.*, No. 16-1464, --- F.3d ---, 2018 WL 2306871 (10th Cir. May 22, 2018)**

Evanston Insurance Co. filed suit against foreclosure attorney, Michael Medved (Medved), and his solo practice, alleging that its professional services liability policy did not extend coverage to a suit based on the firm's alleged overbilling practices. Medved represented lenders and investors, and although he billed them directly, the cost of his services was reportedly passed on to property owners. The U.S. District Court for the District of Colorado granted Evanston's motion for summary judgment, and the U.S. Court of Appeals for the Tenth Circuit affirmed, ruling that, under Colorado law, Evanston had no duty to defend Medved or his solo practice from a homeowner class action or an investigation by the state attorney general. The courts reasoned that the policy only covered "professional services," defined as "those services performed by [Medved] for others ... as a lawyer," and that billing did not fall within that definition. The record was clear, and Medved acknowledged under oath, that the class action and attorney general's allegations all arose from improper billing practices, not professional services. Medved, nonetheless, argued that his policy covered billing-related suits because it promised coverage for damages "by reason of" professional services. The appellate court disagreed, holding that "by reason of" is much more limited than "arising out of" and is not expansive enough to encompass billing matters.

Charles W. Browning
Elaine M. Pohl
Patrick E. Winters
Plunkett Cooney
Bloomfield Hills, MI

Eleventh Circuit

Declaratory Relief/Diversity Jurisdiction (GA)

The Eleventh Circuit has ruled that a Georgia District Court should not have entered a ruling declaring the rights and

obligations of primary and excess insurers for a large explosion at the Imperial Sugar plant that killed dozens of workers. In ***St. Paul Fire & Marine Ins. Co. v. National Union Fire Ins. Co. of Pittsburgh, PA***, No. 16-12015 (11th Cir. May 29, 2018), the Court of Appeals found that the interests of St. Paul and one of the defendant insurers (AGLIC) were identical and that AGLIC should therefore have been realigned as a party plaintiff, which would have defeated diversity jurisdiction because AGLIC and the AIG defendants are all New York corporations.

Michael Aylward
Morrison Mahoney
Boston, MA

Alabama

Agents/Failure to Procure/Limitations Periods

The Alabama Supreme Court has ruled that Alabama's two year statute of limitations for claims against agents and brokers for failing to procure insurance ran from the date that a claim was filed against the insured and the carrier denied coverage in such a manner as to alert them to the shortfall in the coverage that they might otherwise have expected but for the agent's alleged negligence. In ***Beddingfield v. Mullins Ins. Co.***, No. 1170143 (Ala. June 15, 2018), the court rejected the insureds' argument that the limitations period did not begin to run until such time as a judgment entered against them exceeding the amount of the available limits of coverage. However, the court also ruled that the insureds' allegation of "wanton" conduct could go forward in light of its ruling in Ex Parte Capstone Building Corporation (Ala. 2011) that litigants who brought claims based on allegedly wanton conduct had an additional two years after June 3, 2011 to do so. The Supreme Court also rejected the agent's argument that the insureds had not suffered any damages because the defense of the claims were paid for by the Alabama Insurance Guarantee Association and were ultimately settled within the available policy limits. The court found that the insureds had, in fact, provided proof of actual damages including attorney's fees and business losses due to this problem.

Michael Aylward
Morrison Mahoney
Boston, MA

Arizona

Duty to Defend/Contractual Liability Exclusion

The Arizona Supreme Court has ruled that an exclusion for liability arising "under any contractual agreement" did not relieve an insurer of its obligation to defend a builder against a claim for negligent excavation brought by the home buyer, In ***Teufel v. American Family Mutual Insurance Co.***, No. 17-0190 (Ariz. June 14, 2018), the state Supreme Court ruled that the exclusion did not apply because the underlying lawsuit contained an allegation of negligence arising from a common law duty to construct the home as a reasonable builder would and was not based solely upon the contract between the builder and buyer. The court ruled that in such circumstances, the insured's tort obligations arose independently of any contractual duties and therefore fell outside the scope of this exclusion.

Michael Aylward
Morrison Mahoney
Boston, MA

California

Arbitration

The Court of Appeal has ruled in ***Nielsen Contracting, Inc. v. Applied Underwriters, Inc.***, D072393 (Cal. App. May 3, 2018) that an insured's argument that the worker's compensation policies that it was sold were fraudulent was for a court to decide rather by an arbitrator pursuant to an arbitration clause in the agreement.

Michael Aylward
Morrison Mahoney
Boston, MA

"Occurrence"/Negligent Supervision

Liberty Surplus Ins. Corp. v. Ledesma & Meyer Constr. Co., Inc.*, No. S236765, --- P.3d ---, 2018 WL 2470975 (Cal. June 4, 2018)*

A student brought an action against a contractor for a school district, Ledesma & Meyer Construction Company (L&M), alleging negligent hiring, retention and supervision of L&M's employee, who allegedly sexually abused the student while working on a construction project at the student's middle school. L&M's insurer, Liberty Surplus Insurance Corp. (Liberty), brought a declaratory judgment action in federal court, contending it had no obligation to defend or indemnify L&M. The district court granted summary judgment in Liberty's favor, and L&M appealed.

The U. S. Court of Appeals for the Ninth Circuit certified to the California Supreme Court the question of whether a suit against an employer for the negligent hiring, retention and supervision of an employee who intentionally injured a third party alleges an "occurrence" under a CGL policy. The California Supreme Court held in the affirmative, determining that the intentional conduct of a contractor's employee does not preclude potential coverage of an employer's independent tort liability for injury deliberately caused by its employee under a CGL policy that covered bodily injury caused by an "occurrence," which was defined as an "accident."

The Supreme Court reasoned that because Liberty promised to indemnify L&M for all sums which L&M shall become obligated to pay for damages because of bodily injury, coverage necessarily turned on whether the claimant's damages resulted, under tort law, from covered causes: "Causation is established … if the defendant's conduct is a 'substantial factor' in bringing about the plaintiff's injury." While the alleged molestation was the act directly responsible for the claimant's injury, L&M's negligence in hiring, retaining and supervising him was an indirect cause, and "a finder of fact could conclude that the causal connection between L&M's alleged negligence and the injury inflicted by [its employee] was close enough to justify the imposition of liability on L&M." The Supreme Court further determined that even though L&M's hiring, retention and supervision of its employee may have been "deliberate," and, thus, not an "accident," the molestation could be considered an additional, unexpected, independent and unforeseen happening that resulted in the damage. The Supreme Court reiterated that the public policy against insurance for one's own intentional misconduct does not extend to bar liability coverage for others whose mere negligence contributed in some way to the harm.

Charles W. Browning
Elaine M. Pohl
Patrick E. Winters
Plunkett Cooney
Bloomfield Hills, MI

Colorado

Bad Faith/Statute of Limitations

Rooftop Restoration, Inc. v. American Family Mutual Insurance, **2018 CO 44 (Colo. May 29, 2018)**

Denish and Betty Jo Chastain held an insurance policy issued by the defendant, American Family. On August 30, 2013, the Chastains submitted a claim to American Family for hail damage to their roof. American Family inspected the Chastains' home and on September 3, 2013, estimated that the cost to repair the hail damage was less than the policy's $1000 deductible. The Chastains disagreed with American Family's estimate and subsequently assigned their claim against American Family to their contractor, the plaintiff in this case, Rooftop.

On May 13, 2014, Rooftop sent American Family an estimate which indicated that the cost to repair the hail damage was approximately $70,000. On May 28, 2014, American Family re-inspected the Chastains' home and increased its estimate of the covered damage to approximately $4000. American Family sent the Chastains a payment for approximately $3000-$4000 less their $1000 deductible—on May 30, 2014.

More than one year later, on September 11, 2015, Rooftop filed a complaint against American Family in Denver District Court asserting two claims for relief: (1) breach of contract; and (2) unreasonable delay or denial of insurance benefits under section 10-3-1116(1). American Family removed the case to federal district court and moved for partial summary judgment, arguing that Rooftop's statutory claim for unreasonable delay or denial of insurance benefits under section 10-3-1116(1) was barred by the one-year statute of limitations provided in section 13-80-103(1)(d).

The one-year statute of limitations in section 13-80-103(1)(d) applies to "[a]ll actions for any penalty or forfeiture of any penal statutes." In this instance, after consulting an intimately related provision of state law, the court concluded that the legislature did not intend for the one-year statute of limitations found in section 13-80-103(1)(d) to apply to section 10-3-1116(1).

The Colorado Supreme Court paid particular attention to the interplay between the one-year statute of limitations, section 13-80-103(1)(d), and the accrual statute, section 13-80-108. The accrual statute provides that a cause of action for penalties shall be deemed to accrue when the determination of overpayment or delinquency for which such penalties are assessed is no longer subject to appeal. A cause of action under section 10-3-1116(1), however, never leads to a determination of overpayment or delinquency. Thus, if such a claim is deemed a cause of action for penalties in the meaning of section 13-80-108(9), the claim would never accrue, and the statute of limitations would be rendered meaningless. Consequently, it appears that the legislature considered a defining feature of a cause of action for penalties to be a determination of either

overpayment or delinquency and that defining feature is conspicuously absent from a cause of action under section 10-3-1116(1), where an insured must only file a complaint alleging that an insurer delayed or denied the payment of insurance benefits without a reasonable basis.

Accordingly, the court held that the one-year statute of limitations found in section 13-80-103(1)(d) does not apply to a cause of action brought pursuant to section 10-3-1116(1).

Brian Barnas
Hurwitz & Fine, P.C.
Buffalo, NY

Connecticut

First Party/Crumbling Foundation Claims

In an opinion that may have significant consequences for the future of crumbling foundation coverage claims in Connecticut, a federal district court judge announced in Vera v. Liberty Mutual Fire Insurance, No. 16 72 (D. Conn. June 15, 2018) that he was asking the Connecticut Supreme Court to amplify its analysis of older "collapse" language in Beach to clarify "what constitutes a "substantial impairment of structural integrity" for purposes of applying the "collapse provision" of a homeowner's insurance policy. However, Judge Chatigny declined to also certify a question with respect to the meaning of "foundation, noting the significant number of Connecticut rulings in which courts have declared this language to be ambiguous.

Michael Aylward
Morrison Mahoney
Boston, MA

Long-Arm Jurisdiction

The Connecticut Supreme Court has ruled that a Connecticut court had jurisdiction over a local citizen's §38(a)-321 reach and apply action against the insurer of a New York motorist, Despite the fact that the policy at issue was issued in New York and that Kingstone had no jurisdictional contacts with Connecticut, the Supreme Court ruled in *Samelko v. Kingstone Ins. Co.*, SC 199 64 (Conn. June 12, 2018) that Connecticut's judiciary had jurisdiction over Kingstone in light of "Territory" provisions in the policy requiring as a precondition to coverage that "the accidental loss must occur within the designated coverage territory of the United States of America." In light of this Territory provision, the Supreme Court ruled that it was foreseeable to Kingstone that it would be called upon to provide a defense to claims arising in the courts of Connecticut.

Michael Aylward
Morrison Mahoney
Boston, MA

Property Insurance/"Collapse"

In contrast to several recent federal district court rulings that have upheld "collapse" provisions in homeowners' policies that require "sudden and accidental" losses in order to trigger coverage, Judge Eginton has ruled in *Maki v. Allstate Ins. Co.*, [https://protect-us.mimecast.com/s/2Cbk-C4xklxiBGqk7hBvUP2?domain=t.e2ma.net] No. 17-1219 (D. Conn. June 22, 2018) that he could not "preclude the possibility that previously undetectable, structurally devastating cracks that appear in a home's foundation without notice can constitute the sudden collapse of a building structure, in this case caused by hidden decay and defective materials used in construction" and that homeowners should not have to wait for their home to fall to the ground to be eligible for "collapse" coverage. The District Court took note of the fact that another federal judge has recently asked the Connecticut Supreme Court to determine what "substantial impairment of structural integrity" means in a case of this sort. Accordingly, the court denied Allstate's motion to dismiss without prejudice pending the Supreme Court's answer to the certified question in the *Karas* case.

Michael Aylward
Morrison Mahoney
Boston, MA

Stipulated Judgments/"Reach and Apply" Actions

A federal district court has ruled that an accident victim could not pursued bad faith claims against the liability insurers of the truck that struck her lacked standing to do so. Although Section 38a-321 gives tort claimants the right to pursue "reach and apply" actions against a defendant's liability insurers "upon the recovery of any final judgment," Judge Eginton ruled in *Salinas v. HDI-Gerling America Ins. Co.*, No. 17-1755 (D. Conn. June 7, 2018) that no final judgment had entered in this case because the judge in the underlying tort proceedings denied the plaintiff's motion for entry of the stipulated judgment that she had negotiated with the defendant/insured truck driver.

Michael Aylward
Morrison Mahoney
Boston, MA

First Party/Bad Faith

A federal court that a business owner could not recover bad faith damages against its property insurer for providing it with inadequate temporary air conditioners after construction debris clogged its original HVAC system. In granting Sentinel's motion to dismiss the bad faith claims **under New York law**, Judge Merer ruled in *Quinn Fable Advertising, Inc. v. Sentinel Ins. Co.*, No. 17-1795 (D. Conn. May 2018) that there an insured sues for breach of contract and breach of the implied covenant of good faith and fair dealing based on the same set of fact the implied covenant claim is redundant and should be dismissed. The court also agreed to dismiss the insured's claim for punitive damages in the absence of any suggestion that the insurer acted with an intent to harm the general public.

Michael Aylward
Morrison Mahoney
Boston, MA

Illinois

Auto/UM/"Phantom Vehicles"

On remand from a 2015 Appellate Court ruling declaring that UM coverage requires evidence of an accident involving physical contact with another car, the Illinois Appellate Court has ruled in *Cincinnati Insurance Company v. Pritchett*, [https://protect-us.mimecast.com/s/p8jhC5ylmyHZO2NWc2PT7U?domain=t.e2ma.net]2018 IL App. (3rd) 170577 (IL. App. Ct. June 12, 2018) that the driver of the insurance trailer truck was not entitled to UM coverage in the absence of any evidence with respect to an unidentified "phantom" vehicle that caused the driver to swerve into the curb and lose control of his vehicle. The appellate court rejected the driver's argument that all that was required was evidence of a second vehicle in the vicinity of the insured vehicle at the time of the accident or that this was probably an issue for arbitration and should not have been decided by the trial court. For instance, the appellate court ruled that the trial court's determination that a second vehicle did not cause the insurance accident, was not against a manifest weight of the evidence.

Michael Aylward
Morrison Mahoney
Boston, MA

E&O/Intentional Acts

The Appellate Court has ruled an attorney's willful breach of trust in distributing the assets of a client's Estate were not covered under his professional liability policy in light of a policy exclusion for claims "arising out of any criminal, dishonest, fraudulent or intentional act or omission." In *Illinois State Bar Mut. Ins. Assoc. v. Leighton Legal Group LLC,* 2018 IL App (1st) 170458 (Ill. App. Ct. May 22, 2018), the First District pointed to phrases in the underlying complaint "such as mislead, conceal, scheme, deceive, intentionally, or willfully" are the paradigm of intentional conduct and the antithesis of negligent actions" and not merely the result of professional negligence.

Michael Aylward
Morrison Mahoney
Boston, MA

Asbestos/"Horizontal Exhaustion"/Excess/SIRs

The Appellate Court has ruled that the principle of "horizontal exhaustion" that the Illinois Supreme Court articulated a decade ago in Kajima requires payment of all primary policies before umbrella insurance policies are triggered. In *Lamorak Ins.. Co. v. Kone, Inc.*, 2018 IL App (1st) 163998 (Ill. App. May 15, 2018), the First District ruled that CGL policies issued by Lamorak did not become "excess" insurance merely because they featured self-insured retentions and not deductibles.

Michael Aylward
Morrison Mahoney
Boston, MA

Insurer Insolvencies

The Appellate Court has ruled in *In Re Liquidation of Lumbermens Ins. Co.*, 2018 IL App (1st) 1170966 (Ill. App. Ct. June 1, 2018) that the state Director of insurance has sustained a lower court's declaration that California Insurance Guarantee Association cannot be order to reimburse itself for general administrative costs from funds held in a special deposit. The First District declared that California law prohibited CIGA from using special deposits to pay for general administrative expenses.

Michael Aylward
Morrison Mahoney
Boston, MA

Indiana

Auto/UM

The Indiana Supreme Court has ruled that a trial court erred in ordering an auto insurer to provide UM coverage to a homeowner's who was struck by an uninsured vehicle while he was mowing his lawn. Whereas lower courts had found ambiguity in the policy's UM/UIM coverage for "Others We Protect," the Supreme Court ruled in *Erie Ind. Co. v. Harris*, [https://protect-us.mimecast.com/s/bVXyC68mn-8SrxqwGsxyjbp?domain=t.e2ma.net]No. 18S-CT-114 (Ind. June 18, 2018) that this language was unambiguous and did not extend coverage to a scheduled driver who was not injured while using a covered vehicle.

Michael Aylward
Morrison Mahoney
Boston, MA

Iowa

Loss Causation/Appraisal

***Walnut Creek Townhome Assoc. v. Depositors Insurance Co.*, June 1, 2018, 16-0121 (Iowa 2018)**

The Supreme Court of Iowa ruled the trial court erred in disregarding an appraisal award's determination of the amount of the insured's loss for roof shingles damaged by a hailstorm. The Supreme Court held that appraisers may determine the factual cause of damage to insured property to ascertain the amount of the loss, and that the appraisal panel's determination of damage causation issues is binding on the parties.

The decision did reiterate that "[C]overage questions are for the court." The case has been remanded for adjudication of coverage exclusions.

The appraisal held to be binding on the parties only considered the extent of hail damage to the shingles. The appraisal did not address the extent of pre-existing shingle damage/defect, which would be excluded from coverage through the insurance policy's anti-concurrent cause provision. That issue remains to be decided at the district court on remand.

The section of the Supreme Court of Iowa's opinion labeled "Analysis" provides an overview of the insurance policy provision and case law applying the standard policy language. Notably, the appraisal provision in the Iowa Code is based upon the 1943 New York Standard Fire Policy adopted in most states. The decision recites that the only states that have not adopted the New York Standard Fire Policy are Massachusetts, New Hampshire, Minnesota, and Texas.

The Supreme Court of Iowa noted "courts across the country are divided as to whether, in determining the „amount of loss' pursuant to appraisal provisions like the one here, appraisers may consider questions of causation." The court determined that although "some" courts (citing decisions from Illinois, Alabama, and Mississippi) view causation questions as off-limits for appraiser because determining causation is within the exclusive purview of the courts, the "better-reasoned cases" recognize appraisers necessarily address causation when determining the amount of loss from an insured event. Perhaps not surprisingly, two of the three so-called "better-reasoned cases" were decided by courts in Texas and Minnesota, states which have not adopted the New York Standard Fire Policy.

Eric T. Boron
Hurwitz & Fine, P.C.
Buffalo, NY

Massachusetts

First Party/"Innocent Co-Insureds"

In *Shepperson v. Metro. Prop. & Cas. Ins. Co.*, No. 16-12116-DPW (D. Mass. May 22, 2018), the court held that M.G.L. c. 175 §99 assures property damage coverage for an innocent named insured when her unnamed co-insured son intentionally set the insured premises on fire. The court further concluded that insured "will have great difficulty" proving that Metropolitan engaged in bad faith and that Metropolitan's position, "while erroneous, was not unreasonable or implausible."

Shepperson claimed that as an innocent insured, she is entitled to property coverage regardless of whether the fire that damaged her house was intentionally caused by her son. The court determined that Shepperson's son was an unnamed coinsured and also a resident of the premises. According to the court, by its plain terms, the policy excluded coverage. Shepperson's son was a resident of the premises "under any current and common sense definition of that term." Therefore, the court concluded that "in the absence of some supervening legal principles, the policy by its terms would provide no coverage" for Shepperson.

However, the court further concluded that such an exclusion is barred under Massachusetts law. The court predicted that the SJC would conclude that M.G.L. c. 175,

§99 provides coverage for innocent co-insureds under the present circumstances. The court held that "[o]nce the illegal exclusion is excised from the policy, Ms. Shepperson is entitled to coverage" because she was innocent of involvement in the fire which caused the injury for which she seeks damages.

The court also held that Shepperson "will have great difficulty" proving that Metropolitan engaged in bad faith and that Metropolitan's position, "while erroneous, was not unreasonable or implausible." Metropolitan argued that "[t]he very existence of the legal debate [Ms.] Shepperson asked this Honorable Court to join militates in favor of dismissal of her c. 93A, §9 claim." The court opined that "Metropolitan's argument appears persuasive at this point in the litigation." The court further held that nothing in the record suggests Shepperson will be able to prove her claim of emotional distress.

Suzanne Young Whitehead
Zelle McDonough & Cohen
Boston, Massachusetts

Bad Faith/Statute of Limitations

In *Hong v. Northland Ins. Co.*, No. 18-10440-DPW (D. Mass. May 30, 2018), the court held that four year statute of limitations barred claimant's bad faith claim against insurer; and further that the limitations period began no later than the date of the insurer's last alleged settlement misconduct, the date on which the insurer rescinded its final offer of settlement. *Hong v. Northland Ins. Co.*, No. 18-10440-DPW (D. Mass. May 30, 2018).

Hong alleged that Northland engaged in bad faith when it withdrew its $4,000 settlement offer shortly before trial. Applying M.G.L. c. 260 §5A, which states that the statute of limitations for filing an unfair settlement practices lawsuit is four years, the court held that Hong's claims were barred by the SOL.

The court discussed that accrual of a claim under c. 93A "typically occurs at the time injury results from the assertedly unfair or deceptive acts" and "when the plaintiff knew or should have known of appreciable harm" caused by the alleged conduct. According to the court, Hong "fail[ed] to recognize that the injury or harm alleged here was appreciable no later than when the defendant insurer rescinded its settlement offer altogether." Hong's alleged injury was the insured's alleged failure to offer a reasonable settlement, which was fully known when Northland rescinded its $4,000 offer. Consequently, the court held that the four year SOL barred Hong's bad faith claims.

Note however, that the court discussed that Northland's $4,000 settlement offer "was an offer, it bears noting, that itself was some $10,000 less than the plaintiff's claimed medical bills as of that date. The plaintiff prevailed at trial two months later and obtained a verdict resulting in a judgment of $59,713.60."

Suzanne Young Whitehead
Zelle McDonough & Cohen
Boston, Massachusetts

Bad Faith/Settlement

***Matckie v. Great Divide Ins. Co.*, No. 12-1627-G (June 11, 2018) (Ullmann, J.).**

The Superior Court allowed Great Divide's motion for summary judgment on plaintiff's c. 93A claim. The court held that Great Divide's settlement offer was "entirely reasonable. Further, the court held that liability was unclear until the jury returned its verdict, at which point Great Divide made prompt payment.

The underlying claim involved a slip-and-fall accident in June 2010 causing serious injury to Pamela Matckie at Gillette Stadium during the Great American Food Festival. Matckie sent Great Divide a demand letter in February 2012. Great Divide initially offered $160,000 to settle, then increased its offer to $175,000 in June 2012. Matckie sued Great Divide, the insurer of Kraft Group, NPS and Team Ops, alleging Great Divide violated c. 93A. The court allowed Great Divide's motion to sever and stay plaintiff's c. 93A claim.

On May 18, 2016, the jury returned negligence verdicts against NPS, Team Ops, and Uncle Al's, and awarded damages of $450,000. The court entered judgment in the amount of $670,298.40, which included four years of statutory prejudgment interest. Great Divide paid its insureds' two-thirds share of the judgment, totaling $447,089.03.

The court discussed that "[a]lthough reasonableness of settlement negotiations and offers is often a question of fact for the jury, summary judgment in favor of an insurer may be granted where liability was unclear, and the insurer promptly paid after it became clear." The court determined that liability was unclear until the jury returned its verdict, at which time Great Divide promptly paid its insureds' share of the judgment. Further, the court concluded that Great Divide's June 2012 settlement offer of $175,000 was "entirely reasonable." Consequently, the court held that "there is no disputed issue of material fact as to Great Divide's good-faith approach to settlement, and no need for a trial."

The court utilized a two-step analysis in determining that Great Divide made a reasonable settlement offer. First, the court determined that based on the trial evidence, Matckie's damages award of $450,000 was reasonable and "quite favorable" to Matckie. Secondly, the court discussed that if the jury had accepted Matckie's position before and throughout the trial that all five defendants were liable, Great Divide's liability for its two insureds "would have been almost exactly what Great Divide had offered" Matckie four years earlier. The court noted that Great Divide's payment to Matckie was significantly greater than $180,000 because the jury determined that two of the defendants were not liable and due to the four years of statutory prejudgment interest.

Further, the court held that "[u]nderlying this two-step analysis is that the extent of Great Divide's liability was uncertain until the jury returned its verdict, after which Great Divide promptly made full payment."

Suzanne Young Whitehead
Zelle McDonough & Cohen
Boston, Massachusetts

Minnesota

CGL/"Your Product" Exclusion/"Real Property"

While leaving open numerous issues concerning the availability of CGL coverage for a settlement arising out of defects in the insured's "insulated glass units" that failed after being installed in various hotels and commercial buildings, Judge Magnuson has ruled in *National Union Fire Ins. Co. of Pittsburgh, PA v. Viracon, Inc.*, No. 16-482 (D. Minn. June 18, 2018) that the claims sought recovery for "property damage" but that the cost of repairing the IGUs or their component parts were subject to the policy's "your product" exclusion, rejecting the insured's argument that the damaged goods were "real property."

Michael Aylward
Morrison Mahoney
Boston, MA

Missouri

Environmental Liability Insurance

A federal district court has ruled in *Sunflower Redevelopment, Inc. v. Illinois Union Ins. Co.*, [https://protect-us.mimecast.com/s/GgAwC73no3hA9w7WURd0fs?domain=t.e2ma.net] No. 15-577 (W.D. Mo. June 25, 2018) that a Pollution Legal Liability policy insured demands that a brownfields developer had received from the State of Kansas pursuant to its agreement to remediate and develop a polluted former munitions production facility. **Applying Kansas law**, Judge Hays agreed with Sunflower that the PPL policy's coverage for remediation costs was not pre-conditioned on the assertion of a clean-up claim against the insured since it separately covered "claims" and "remediation costs." In any event, the court declared that letters that the insured had received from the Kansas Department of Health and Environmental directing it to implement a pollution work plan were "claims" under the PLL policy. The court further found that the claims were not asserted prior to Illinois Union's policy period and thus excluded.

Michael Aylward
Morrison Mahoney
Boston, MA

New York

Windstorm Exclusion Ambiguous

***7001 East 71st Street LLC v. Continental Casualty Company*, United States Court of Appeals, Second Circuit**

7001 East 71st Street LLC ("7001") allegedly sustained damages to its shopping center during Superstorm Sandy, at least in part, due to rainwater. Its carrier, Continental Casualty disclaimed coverage, citing their policy's windstorm exclusion. That provision, starting with an anti-concurrent clause, read: "We will not pay for loss or damage caused directly or indirectly by any of the following. Such loss or damage is excluded, regardless or any other cause or event that contributes concurrently or in any sequence to the loss. ... including ... earth movement ... nuclear reaction or radiation ... war, including undeclared or civil war ... and an explosion." Further, the provision precluded coverage for a "'Breakdown' that is caused by windstorm or hail" and a "breakdown" in turn is defined as a "sudden and accidental direct physical loss to 'Covered Equipment', which manifests itself by physical damage, necessitating its repair or replacement, unless such loss is otherwise excluded within this Coverage Form." Thus, the court noted, the Windstorm Exclusion actually read, in relevant part and in context:

"We will not pay for loss or damage caused directly or indirectly by a "Breakdown" [*i.e.*, a sudden and accidental direct physical loss to "Covered Equipment," which manifests itself by physical damage] that is caused by windstorm."

The court noted that this exclusion did not simply read "we will not pay for loss or damage caused directly or indirectly by windstorm." It contrasted the above language with the policy's Earth Movement Exclusion, which was clearer: "We will not pay for loss or damage caused directly or indirectly by earth movement." Similarly, the policy's Explosion Exclusion stated: "We will not pay for loss or damage caused directly or indirectly by an explosion." If the Windstorm Exclusion had been drafted as clearly, then clearly there would have been no coverage. However, reading the policy as a whole, the drafter/carrier intended to distinguish between these provisions. Since there were two possible interpretations of the above-cited language, though, it was ambiguous. Since unclear provisions of a contracted are construed against the drafter, the court vacated the earlier win for the carrier and sent the matter back down for further proceedings.

Agnes A. Wilewicz
Hurwitz & Fine, P.C.
Buffalo, NY

Coverage B/"Software" Exclusion

A federal district court has ruled in *BF Advance, LLC v. Sentinel Ins. Co.*, [https://protect-us.mimecast.com/s/DWP-GC82op2S6xE4wtz-Vlb?domain=t.e2ma.net]No. 16-5931 (E.D.N.Y. March 20, 2018) that a lawsuit in which the plaintiff alleged that the insured had improperly infringed upon the claimant's software, its avatars to introduce web sites to online visitors were outside the amended "personal and advertising injury" coverage provided by Sentinel's "Cyber Flex Coverage" endorsement that extended Coverage B to the offense of "copying in your advertisement or on your web site a person or organization's advertising idea or style of advertisement." Judge Matsumoto declared that the claims were clearly subject to an exclusion for violations of intellectual property rights "arising out of … computer code, software or programming" used to enable web sites. The court rejected the insured's argument that the software exclusion was ambiguous because it did not define "computer code, software or programming." In granting summary judgment for Sentinel and denying coverage for this claim, the District court also declined to consider an "expert opinion" from an individual named Scott Stein, declaring that the software language in the endorsement was unambiguous. In granting Sentinel's motion to strike the Stein Declaration, the court declared that it need not consider this information since only the court should consider whether a contract term is ambiguous.

Michael Aylward
Morrison Mahoney
Boston, MA

Intentional Acts/Injuries Prior or Subsequent to Assault

***State Farm Fire and Casualty Co. v. McCabe*, Appellate Division, Third Department, June 14, 2018**

On August 9, 2014, Rebekah was visiting her then boyfriend, McCabe, and McCabe's mother's home. McCabe, nice guy that he was, physically assaulted her, strangled her with a rope and struck her head. He was convicted, after a criminal jury trial, of first degree assault and criminal possession of a weapon in the fourth degree.

Rebekah then sued McCabe and his mother, alleging, among other things, that McCabe rendered her partially incapacitated and, while in that condition, she tripped and fell due to a defective condition on the property.

State Farm was mom's homeowner's carrier and denied coverage, claiming that the injuries did not arise out of an "occurrence" and were not covered by an exclusion for intended injuries or willful and malicious acts.

Generally, when an insurer seeks to disclaim coverage on the basis of an exclusion, the insurer will be required to provide a defense unless it can demonstrate that the allegations of the complaint cast that pleading solely and entirely within the policy exclusions, and, further, that the allegations are subject to no other interpretation. An insurer may avoid coverage under a policy's intentional acts exclusion only if the insurer establishes as a matter of law the absence of any possible legal or factual basis to support a finding that the bodily injury at issue was, from the insured's point of view, unexpected and unintended.

State Farm raised collateral estoppel in support of their motion: "that the identical issue was necessarily decided in the prior action and is decisive in the present action," and that "the party to be precluded from relitigating an issue must have had a full and fair opportunity to contest the prior determination."

The jury's verdict finding McCabe guilty of assault in the first degree and strangulation in the first degree necessarily included findings that McCabe intended to cause serious physical injury to defendant, intended to impede her breathing or circulation, applied pressure to her throat

or neck and caused her serious physical injury by means of a deadly weapon or dangerous instrument.

The intent required in the criminal action would be sufficient to establish the intent element of the insurance policy exclusion as long as they relate to the same conduct. In the underlying action, defendant alleged, among other things, that McCabe permitted and failed to remedy a tripping hazard in a doorway and exacerbated the dangerous condition by obstructing the doorway with a couch and other items, and defendant tripped and fell into a cement wall, causing her serious injuries. Defendant also alleged that McCabe negligently engaged in an activity that rendered her partially incapacitated, then did not exercise reasonable care to obtain prompt medical attention, hold or support her as she attempted to walk through the doorway, or warn her of the dangerous condition.

The court agreed with State Farm that McCabe's intentional actions cannot be magically transformed into negligent ones merely by defendant's allegations trying to recast them. McCabe's conduct that rendered defendant partially incapacitated was his criminal, intentional actions, which cannot be downgraded to mere negligence through artful pleading. On the other hand, the court found that some of Rebekah's allegations addressed McCabe's actions prior to the assault, such as failing to maintain the property by permitting a tripping hazard, and his alleged actions after the assault, such as failing to obtain medical care and allowing defendant to ambulate in an incapacitated state without adequate assistance.

It was claimed that she may have suffered additional injuries due to this negligent conduct, or her injuries from the assault may have been exacerbated by this negligent conduct.

To establish the convictions, it was unnecessary for the jury to have made findings regarding whether McCabe created a tripping hazard, allowed defendant to walk on her own after he had rendered her partially incapacitated or failed to seek medical help for her after the criminal assault. Hence, the issues as to insurance coverage and exclusions are not identical to the issues decided in McCabe's criminal trial, and defendants here did not have a full and fair opportunity in the criminal trial to address some of the issues regarding McCabe's negligence allegedly committed before and after the criminal assault.

As to mom, the carrier did not disclaim coverage and State Farm needs to defend and indemnify her.

Dan D. Kohane
Hurwitz & Fine, P.C.
Buffalo, NY

Equitable Estoppel/Late Denial

***Mazi Building, LLC v. Greenwich Insurance Company*, Appellate Division, Second Department, June 6, 2018**

In January 2006, the Mazi retained nonparty Rovatele Elevator, Inc. ("Rovatele") to perform an elevator renovation project in a Mazi-owned building. Rovatele obtained an insurance policy from Greenwich that named Mazi as an additional insured pursuant to an indemnification agreement between the Mazi and Rovatele. In March 2006, the Mazi assigned its rights under the indemnification agreement to another entity („the "plaintiff").

In October 2006, Samaroo allegedly sustained injuries while working on the elevator renovation project. He sued Mazi and others. In February 2008, Greenwich agreed to defend and indemnify Mazi in connection with the underlying action. Thereafter, Greenwich learned of the plaintiff's assignment of its rights under the insurance policy and, hence, learned of a defense to coverage as early as 2009. However, Greenwich continued to defend the plaintiff in the underlying action for almost four more years, without reserving their rights to disclaim coverage. In 2013, after jury selection in the underlying action, Greenwich disclaimed coverage on the basis that, contrary to what they had believed when they originally accepted the tender for a defense and indemnification, the plaintiff was not an additional insured under the insurance policy at the time of the accident. Ultimately, the plaintiff paid $250,000 to settle the claim against it in the underlying action.

The plaintiff commenced this action, inter alia, seeking declaratory relief and to recoup the $250,000 it paid to settle the claim against it in the underlying action. The plaintiff argued that Greenwich was equitably estopped from denying coverage since they had knowledge of the facts that supported the disclaimer but failed to disclaim coverage until almost four years after attaining that knowledge.

The plaintiff established, prima facie, that Greenwich was estopped from denying coverage. Although the defendants learned by 2009, at the latest, of the plaintiff's pre-accident assignment of its rights under the indemnification agreement, pursuant to which the plaintiff had previously been an additional insured under the insurance policy, the defendants continued to control the plaintiff's defense in the underlying action and had knowledge of the facts constituting the basis of their denial of coverage for almost four years before issuing their coverage disclaimer. Since the Greenwich did not reserve its rights to disclaim

coverage, estoppel barred them from denying coverage under the circumstances of this case.

Dan D. Kohane
Hurwitz & Fine, P.C.
Buffalo, NY

Late Notice

***Cohen v. Sive, Paget & Riesel, P.C.*, Appellate Division, First Department, June 14, 2018**

Failure to Advise of Potential Coverage Can Lead to Legal Malpractice Claim Plaintiff, apparently, commenced this legal malpractice claim after his underlying insurance claim was denied for failure to proffer timely notice. From what we can gleam from a very short opinion, plaintiff maintains that his attorney should have advised him of the condition precedent requiring prompt notice of a claim. Defendant maintained that regardless of whether they failed to advise of the notice requirement, any such failure was not a proximate cause of the loss of coverage as plaintiff's notice was late prior to engaging counsel. Unfortunately, the Record did not conclusively establish when notice could have been provided in relation to retention of counsel. On this basis, defendant's motion was denied.

Steven Peiper
Hurwitz & Fine, P.C.
Buffalo, NY

Business Income Claim

***Bernstein Liebhard, LLP v. Sentinel Ins. Co.*, Appellate Division, First Department, June 28, 2018**

Plaintiff is an operating law firm that sustained a fire loss during the period covered by Sentinel. The instant claim focuses on plaintiff's claimed entitlement to business income loss resultant from the suspension of advertising which was allegedly caused by the fire. Essentially, plaintiff argues that it lost contingency fees when it was forced to suspend advertising in the aftermath of the otherwise covered loss.

Here, the policy covered "actual loss" of business income within twelve months of the fire. Plaintiff seeks fees it argues it would have "earned" in the twelve months post fire. The Court initially noted that fees that would not have been paid until after the expiration of the twelve month limitation are not covered. Thus, work performed during the time period, for contingency fees which would have later been earned, is not covered. The Court, however, suggested that fees "earned" (*i.e.*, fees which were payable) within the twelve month period might be covered.

Here, however, no such argument was presented. Rather, plaintiff only argues that it did not sign up cases which would have resulted in earned fees down the road. That, again, is not covered as "actual loss" within the relevant twelve month period.

Steven Peiper
Hurwitz & Fine, P.C.
Buffalo, NY

Bad Faith

***Corle v. Allstate Insurance Company*, Appellate Division, Fourth Department, June 8, 2018**

Plaintiff Colin Corle was accidently shot by Jeoffrey Lee Bauter Teeter, who was insured under a policy issued by Allstate. James Corle commenced a proceeding on behalf of Colin against Teeter and his father. Allstate disclaimed coverage, asserting that the shooting as not a covered loss under the policy. Corle ultimately obtained a judgment in excess of $350,000.

Corle then brought a direct action against defendant as an injured person/judgment creditor under Insurance Law §3420 (a)(2) and (b)(1). In that action, the court determined that the accidental shooting was a covered loss under the insurance policy and awarded Corle the $50,000 policy limits of the Teeters¬ liability policy.

Thereafter, the Teeters assigned all of their rights and claims against defendant to the Corle who commenced this action alleging that defendant disclaimed coverage in bad faith. Allstate moved to dismiss, arguing that the action was barred by res judicata and that the Complaint failed to state a cause of action.

The Fourth Department concluded that dismissal was not warranted based on res judicata. The court determined that the failure of Corle to litigate the bad faith claim in the prior direct action did not bar litigation of that claim. The court concluded that an injured party commencing a direct action under Insurance Law §3420 (a)(2) and (b)(1) is limited to recovering the policy limits of the insured's policy. However, if the insured assigns his or her rights under the insurance contract to the injured party/judgment creditor, then the injured party/judgment creditor may simultaneously bring a direct action against the insurer pursuant to Insurance Law §3420 (a) (2) along with any other appropriate claim, including a bad faith claim,

seeking a judgment in a total amount beyond the insured's policy limits.

Here, when Corle commenced the direct action, the Teeters had not yet assigned their rights under the insurance contract. As a result, Corle did not have standing to bring a bad faith claim. Accordingly, the court concluded that the doctrine of res judicata did not apply.

Importantly, the Fourth Department noted that the First Department has held otherwise under similar facts in *Cirone v. Tower Ins. Co. of N.Y.* However, the court declined to follow the First Department's ruling in *Cirone*.

The court also concluded that the motion to dismiss the bad faith claim should not have been dismissed for failure to state a cause of action. The facts alleged in the Complaint sufficiently stated a cause of action for bad faith.

Brian Barnas
Hurwitz & Fine, P.C.
Buffalo, NY

South Carolina

Bad Faith

***Monticello Road, LLC v. Auto-Owners Insurance*, United States District Court, District of South Carolina, June 25, 2018**

Plaintiffs operate a gas station and convenience store in Columbia, South Carolina. Plaintiffs allege that in 2016 there was a severe storm that caused damage to various gas pumps, gas equipment, inventory, and a canopy. According to Plaintiffs, water seeped into the underground storage tanks and damaged fuel inventories.

Plaintiffs submitted a claim under its AmGuard Policy seeking coverage for damage to the canopy and the gasoline pumps, but not for the underground gasoline inventory. After investigating the claim, AmGuard issued payment for the canopy, identifying wind damage as the Covered Cause of Loss. AmGuard, however, denied payment for the gasoline pumps. According to AmGuard, the remainder of Plaintiffs' claimed damages was caused by flood waters and is specifically excluded under the AmGuard Policy.

Plaintiff sued AmGuard for breach of contract and bad faith. AmGuard moved for summary judgment on both claims. The Court agreed with AmGuard that there was no coverage for the gasoline pumps because they were damaged by flood water, which was excluded under the policy. It was undisputed that there was no damage to the gasoline pumps.

The bad faith claim was also dismissed. One of the elements of bad faith refusal to pay benefits under South Carolina law is refusal by the insured to pay benefits due under the contract. As AmGuard's refusal to pay benefits was justified, the bad faith cause of action failed.

Plaintiffs also sued AutoOwners, a Write-Your-Own program carrier participating in the National Flood Insurance Program. AutoOwners did not move against Plaintiffs' breach of contract claim, but did move to dismiss Plaintiffs' claims for extra-contractual damages. The Court concluded that Plaintiffs' bad extra-contractual claims under state law were preempted by the National Flood Insurance Act because federal law exclusively governs claims made on policies issued under the NFIA.

Brian D. Barnas
Hurwitz & Fine, P.C.
Buffalo, NY

Legal Malpractice

***Sentry Select Ins. Co. v. Maybank Law Firm, LLC*, No. 2016-001351, --- S.E.2d ---, 2018 WL 2423694 (S.C. May 30, 2018)**

Answering a certified question from the federal district court, the South Carolina Supreme Court held that an insurer may maintain a direct malpractice action against counsel hired to represent the insured where the insurance company had a duty to defend. Sentry Select Insurance Company (Sentry) hired Roy P. Maybank (Maybank) of the Maybank Law Firm to defend a Sentry insured in a personal injury lawsuit. Maybank failed to timely answer requests to admit, and Sentry claimed that as a result of Maybank's negligence it had to settle the case for $900,000 when Maybank had previously represented to Sentry that the case could be settled in the range of $75,000 to $125,000. The Supreme Court held that "an insurer may bring a direct malpractice action against counsel hired to represent its insured. However, we will not place an attorney in a conflict between his client's interests and the interests of the insurer. Thus, the insurer may recover only for the attorney's breach of his duty to his client, when the insurer proves the breach is the proximate cause of damages to the insurer." The Supreme Court also noted that "[i]f the interests of the client are the slightest bit inconsistent with the insurer's interests, there can be no liability of the attor-

ney to the insurer, for we will not permit the attorney's duty to the client to be affected by the interests of the insurance company[]" and as a final limitation on the insurer's right to bring a malpractice action against the lawyer it hired to represent the insured, "the insurer must prove its case by clear and convincing evidence." Because the Supreme Court affirmatively answered the certified question, it indicated that the federal district court should independently determine whether Maybank was negligent based on all the facts and circumstances of the case.

Charles W. Browning
Elaine M. Pohl
Patrick E. Winters
Plunkett Cooney
Bloomfield Hills, MI

Texas

Energy Insurance/"Liability"

The Texas Supreme Court announced last week that it would grant review of the Court of Appeals' 2016 ruling in *Houston Casualty Co., et al., v. Anadarko Petroleum Corp.*, 2016 Tex. App. LEXIS 12354 (Tex. App. 2016) that a well operator could not recover over $100 million for the cost of defending Deepwater Horizon costs because defense costs are a "liability."

Michael Aylward
Morrison Mahoney
Boston, MA

Washington

Auto/PIP

On a certified question from a federal district court, the Washington Supreme Court has declared in *Durant v. State Farm Mutual Automobile Insurance Company*, No. 94771-6 (Wash. June 7, 2018) that efforts by State Farm to cut off PIP benefits under its auto policy after the claimant had reached "maximum medical improvement" violation of WAC 284-30-395(1) seeking to limit benefits beyond the regulations permitted declamation for services that are not reasonable or necessary or otherwise unrelated to the insured's accident.

Michael Aylward
Morrison Mahoney
Boston, MA

Construction Defects/Your Work Exclusion

***Cincinnati Specialty Underwriters v. Milionis Constr., Inc.*, United States District Court for the Eastern District of Washington, June 21, 2018**

This declaratory-judgment action arises out of an underlying construction defects action involving the construction of a residential home. Jeffrey and Anna Wood hired Milionis.

Construction Company ("Milionis") to serve as the general contractor for the construction of the home. In the underlying action, the Woods allege that Milionis breached the parties' agreement by, among other things, failing to (a) perform in a workmanlike manner, (b) follow plans and specifications, (c) purchase and install required materials, (d) provide an accounting for fees, and (e) abandoning the job site. The Woods asserted claims for breach of contract, quantum meruit, promissory estoppel, breach of good faith and fair dealing, negligence, negligent misrepresentation, and violation of the Washington Consumer Protection Act.

After the commencement of the underlying action, Milionis tendered the suit to Cincinnati Specialty Underwriters Insurance Company ("Cincinnati") for defense and indemnity. Cincinnati agreed to defend the underlying suit under a reservation of rights. Cincinnati then filed a declaratory-judgment action seeking a declaration that it did not have a duty to defend or indemnify Milionis in the underlying action.

Cincinnati issued a CGL policy to Milionis, effective from November 23, 2014, to November 23, 2016. The policy provides coverage for "sums that the insured becomes legally obligated to pay as damages because of 'bodily injury' or 'property damage' to which this insurance applies." The policy contains an Independent Contractors Limitations of Coverage Endorsement, which requires Milionis to (a) obtain a formal written contract with all independent contractors and subcontractors verifying valid commercial general liability insurance, (b) obtain a formal written contract stating the independent contractor or subcontractor agrees to indemnify Milionis for any liability, and (c) verify in the contract that the independent contractor or subcontractor has named Milionis as an additional insured on the liability policy. The endorsement provides "this insurance will not apply to any loss, claim or 'suit' for any liability or any damages arising out of operations or completed operations performed for you by any independent contractors or subcontractors unless all of the above conditions are met."

Milionis did not obtain written hold harmless agreements from its subcontractors and was not named as an addi-

tional insured on its subcontractors' policies. Cincinnati moved for summary judgment based on Milionis's failure to comply with those conditions.

The Court noted that the duty to defend is broader than the duty to indemnify and that the duty to defend exists if the policy conceivably covers the allegations, while the duty to indemnify exists only if the policy actually covers the claim. To determine whether an insurer has a duty to defend, a court looks only at the "eight corners" of the policy and the complaint. The Court examined the underlying complaint, which alleged statutory, contractual, and tort claims, and stated that the bases of which are conceivably covered under Milionis's CGL policy with Cincinnati. As such, the Court held that Cincinnati had a duty to defend Milionis in the underlying suit.

In its motion, Cincinnati argued that it had no duty to defend Milionis in the underlying action based on the "Damage to Your Work" exclusion. The exclusion applies to "'property damage' to 'your work' arising out of it or any part of it and included in the 'products-completed operations hazard.'" The products liability operations hazard includes "'all bodily injury' and 'property damage' . . . arising out of 'your product' or 'your work'" if the product is no longer in the insureds' possession or the work has been completed or abandoned. Thus, the "Damage to Your Work" policy exclusion limits coverage to property damage that occurs before the work has been completed or abandoned.

The Court found that the "Damage to Your Work" policy exclusion did not necessarily preclude coverage for the claims asserted in the underlying complaint. The Woods alleged that Milionis "performed numerous tasks in a substandard and unworkmanlike manner" including "failure to assert steel columns at necessary points in the basement walls per the structural detains of the engineering and architectural drawings" and "improperly stepping down the west side foundation . . . [causing] the foundation wall to sit two feet higher than it was supposed to be." These allegations assert property damage that occurred before the work was completed or abandoned. Accordingly, the Court held that the "Damage to Your Work" policy exclusion did not exclude coverage based on the facts alleged in the complaint.

Cincinnati next argued that the Woods' claims are not covered because Milionis failed to comply with the requirements of the subcontractor endorsement. The Court noted that this issue could not be determined from the face of the policy and the complaint. The Court further noted that the underlying complaint alleged causes of action that extend beyond "completed operations performed for [Milionis] by any independent contractors or subcontractors."

Cincinnati also argued that it had no duty to indemnify Milionis for damages incurred in the underlying suit. The Court acknowledged that the duty to indemnify turns on the insured's actual liability to the claimant and the actual coverage under the policy. To determine coverage, an insured must establish that the loss falls within the scope of the policy's insured losses. Because the underlying suit has not yet concluded, The Court concluded that questions of fact remain regarding the basis of Milionis's actual liability, if any, to the Woods. Accordingly, the Court denied summary judgment on the issue of Cincinnati's duty to indemnify.

Brian F. Mark
Hurwitz & Fine, P.C.
Buffalo, NY