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Counsellors at Law

Insurance News

A Newsletter from the Insurance Practice Group at Wiggin and Dana LLP

SPRING 2011

We are pleased to share this latest issue of the Wiggin and Dana Insurance Practice Group Newsletter. We circulate this newsletter by e-mail periodically to bring to the attention of our colleagues in the insurance industry reports on recent developments, cases and legislative/regulatory actions of interest, and happenings at Wiggin and Dana. We welcome your comments and questions.

Wiggin and Dana Insurance Practice Group

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In this Issue:

Wiggin and Dana Expands Philadelphia Office and Adds Investment Management and Broker-Dealer Regulation Practice Group: *Richard Levan Joins Firm's Philadelphia Office*

Wiggin and Dana LLP is pleased to announce the expansion of its Philadelphia office with the addition of Richard Levan and two lawyers who previously practiced with Mr. Levan at his firm, Richard Levan & Associates. Mr. Levan and his colleagues, Susan Kennedy and Conor Mullan, will be members of the firm's White-Collar Defense, Investigations and Corporate Compliance Practice Group, expanding the firm's services in securities law, including investment management and broker-dealer regulation.

For the formal announcement and additional information, please see www.wiggin.com.

CT Privacy Forum Event

Wiggin and Dana is currently organizing and co-sponsoring the September 15, 2011 CT Privacy Forum at the Connecticut Convention Center. A formal invitation to follow soon.

Insurance Coverage for the Computer Age

Sabrina Houlton, a member of the firm's Privacy and Information Security and Insurance Practice Groups, recently published an article in the *Connecticut Law Tribune* related to cyber-security policies needed to deal with data loss and theft.

Business losses resulting from data breaches, computer system malfunction, employees' Internet usage, computer viruses, and other risks relating to information technology infrastructure and activities have grown exponentially with the evolution of the internet and the ability to collect, store, and use electronic data on a mass scale.

For many years, companies had traditional insurance policies written before or without regard to the computer age. Now numerous insurers explicitly exclude IT-related risks and offer separate, specific cyber-security insurance.

The need for such coverage is clear. Larry Clinton, president of the Internet Security Alliance, reports that "some estimates now place the economic loss from known cyber thefts at more than $300 million per day." A study of data breaches from 2009 by the Ponemon Institute calculates the cost of a data breach at over $200 per affected individual, with the average total cost at over $6 million per event.

Attorney Notes

Michael Menapace recently attended the ARIAS-U.S. reinsurance arbitration Spring conference in Miami, FL.

Wiggin and Dana is organizing and co-sponsoring the Connecticut Privacy Forum on September 15, 2011 at the Connecticut Convention Center. Details regarding the forum will be released this month.

Joe Grasso and **Tim Diemand** recently attended the annual meeting of the International Marine Underwriters Association in Chicago, IL.

Joe Grasso recently attended the annual meeting and dinner of the Maritime Law Association in New York, and the Association of Average Adjusters in London.

Alison Weir recently attended the annual meeting and dinner of the Maritime Law Association in New York.

Traditional Insurance Enough?

The insurance coverage questions involving e-commerce and electronically stored data raise a host of novel issues for the courts to decide. There is one common legal question, however, that consistently pervades these decisions: whether a loss of such data constitutes a physical harm sufficient to trigger coverage under traditional policies. The answers offered by the courts are inconsistent.

Several courts concluded that a loss of electronic data does not amount to a loss of property and, therefore, traditional general liability and commercial liability policies do not offer coverage. For example, in *America Online Inc. v. St. Paul Mercury Insurance Co.*, the court considered whether claims from customers that AOL's Version 5.0 had damaged their computer data, software, and systems were covered under AOL's general liability policy. 207 F. Supp. 2d 459 (E.D. Va. 2002).

The policy covered "property damage," defined as "physical damage to tangible property of others, including all resulting loss of use of that property; or loss of use of tangible property of others that isn't physically damaged." The court held that "[c]omputer data, software, and systems do not have or possess physical form and are therefore not tangible property as understood by the Policy."

On appeal, the 4th Circuit affirmed the decision, holding: "The insurance policy in this case covers liability for 'physical damage to tangible property,' not damage to data and software, i.e., the abstract ideas, logic, instructions, and information." *America Online Inc. v. St. Paul Mercury Insurance Co.*., 347 F.3d 89, 96 (4th Circuit, 2003).

Despite this clear statement, earlier in the same year – 2003 – the 4th Circuit held in a different case that loss of data resulting from a disgruntled employee hacking into a company's databases constituted "damage to its property, specifically, damage to the computers." *NMS Services Inc. v. The Hartford*, 62 Fed. Appx. 511, 2003 U.S. App. LEXIS 7442, at *7 (4th Circuit, April 21, 2003).

The California Court of Appeal in *Greco & Traficante v. Fidelity & Guaranty Insurance Co.* (an unpublished 2009 decision) considered the claim of a law firm that mistakenly underreported its bills as part of a settlement, and thereby failed to collect some $57,000 owed to it, as a result of a glitch in its billing software.

Because the law firm could not prove that the glitch was the result of a physical loss, the court held that there was no coverage under the "Electronic Data Processing Systems" provisions in its policy that covered "risks of direct physical loss."

Other decisions have also found that electronic data is not tangible property and, therefore, is not covered under a property liability policy or a general liability policy.

In *American Guarantee & Liability Insurance v. Ingram Micro Inc.*, however, the U.S. District Court in Arizona in 2000 reached a very different conclusion. Ingram, which was a wholesaler of "microcomputer products," suffered a power outage that resulted in a loss of "all of the programming information" from its system to track customers, production, and daily transactions. As a result, the company suffered a significant business interruption and financial harm. The court found coverage, holding that "'physical damage' is not restricted to the physical destruction or harm of computer circuitry but includes loss of access, loss of use, and loss of functionality."

Similarly, in *Southeast Mental Health Center Inc. v. Pacific Insurance Co.*, the court addressed a coverage claim made by a health center after the prescription data contained its pharmacy computer became corrupted as a result of a power outage. 439 F. Supp. 2d 831, 833 (W.D. Tenn. 2006). Relying on *Ingram*, the court held "that the corruption of the pharmacy computer constitutes 'direct physical loss or damage to property' under the business interruption policy."

About Wiggin and Dana's Insurance Practice Group

Highly regarded and deeply experienced, the Wiggin and Dana Insurance Practice Group provides international, national and regional insurers, reinsurers, brokers, other professionals and industry trade groups with effective and efficient representation. Our group members regularly advise clients in connection with coverage issues, defense and monitoring of complex claims, regulatory proceedings, policy wordings, internal business practices, and state and federal investigations. We also defend clients faced with individual lawsuits and class actions - both at trial and on appeal; and represent clients in insurance and reinsurance arbitrations. We have broad experience in many substantive areas, including property, commercial general liability, inland and ocean marine, reinsurance, E&O, D&O, and other professional liability environmental, and aviation. A more detailed description of the Insurance Practice Group, and biographies of our attorneys appear at www.wiggin.com.

In short, courts offer a mixed reading on whether e-commerce injuries or the loss or compromise of electronic data or systems qualify as physical harms sufficient to trigger coverage under traditional insurance policies.

Insurance Companies' Response

Given the varied response of the courts, both insureds and insurers are left without clear guidance on whether a traditional property or general liability policy covers damage to electronic data. In response to this uncertainty, many insurance forms now explicitly exclude electronic information unless added into the coverage through an endorsement. Other insurers have offered limited coverage.

The policy language varies enormously. Some exclude electronic data entirely. Others provide coverage for the cost of replacing or restoring lost or corrupt electronic data, or provide coverage only for replacing the blank media compromised in a data loss, while excluding the costs of recreating or replacing the data. Some policies only cover specific types of data loss, such as the damage caused by a computer virus. And still others provide coverage for electronic media and records with a broad, inclusive definition. Certain policies cover other possible damage, such as data breaches and claims related to Internet usage, with varied approaches.

In addition to the legal uncertainty that insurers face is a lack of market experience in dealing with e-commerce and electronic data risks, which makes pricing cyber-security insurance a challenge. As a result, many insurers have been hesitant to offer expansive insurance that might involve the assumption potentially limitless risk. Instead of following a more traditional model — covering a broad range of risks with the option to purchase additional coverage through endorsements — insurers tends to offer cyber-security insurance on a piecemeal basis to allow insurers to price risk more discretely.

Evaluating Cyber Insurance

As with traditional commercial policies, there are two general categories of risks covered by e-commerce insurance: first party and third party. First party insurance covers the insured's own damages, such as property insurance or business interruption insurance. Third party insurance covers risks of harm to others for which the insured might be held liable. It is critically important to consider both kinds of risk when evaluating cyber security insurance, because cyber-security insurance tends to be offered in a menu format, putting the burden on the insured to make the right selections from that menu.

The e-commerce and other electronic data risks that a business may wish to cover include data loss caused by a power outage, hacking, an IT accident; theft; and defective hardware. Coverage might also include data breach from an accidental sharing of information; hacking; software malfunction; mishandling of data; a rogue employee; defamation or slander related to Internet postings; copyright or trademark violations related to Internet usage; extortion (disabling or threatening to disable a computer system or to destroy data if a certain payment is not made); and corporate espionage.

Additionally, businesses might wish to guard against a loss of income as a result of lost or corrupt data; service outage; damaged hardware or software. Finally, they might seek protection against third party claims, where, for example, a user sues for damage to his or her computer or data as a result of a Web site or product offered.

Businesses must guard against inadvertently purchasing insurance that is too narrow to cover the numerous risks that they may face. But they must also guard against purchasing coverage that is unnecessary because their property liability and general liability policies already cover certain IT-related risks expressly or under applicable case law.

Companies must also be attentive to exclusions of certain types of harm in cyber-security insurance policies. For example, some policies do not cover intentional violations of a company's

privacy policies. As a result, if an employee fails to follow company policy, the resulting harm may not be covered.

Policies also may exclude coverage for government enforcement actions. That means that the costs associated with responding to a Federal Trade Commission investigation into a data breach, or a Department of Health and Human Services investigation into a potential violation of the Health Information Portability and Accessibility Act, may not be covered.

There is one indirect benefit to purchasing cyber-security insurance – encouraging the adoption of best data security and privacy practices. Just as a property insurer will require that property be "up-to-code" and in proper condition, a cyber-security insurer will likely require a company to implement best practices to avoid a covered event. Meeting these insurance requirements may have the unintended benefit of improving your company's IT security practices and procedures – in addition to providing coverage should something go wrong.

FROM THE COURTS

Coverage Barred by Insolvency Exclusion for Allegations that Actuarial Services Firm Contributed to Client's Insolvency

The U.S. Court of Appeals for the Ninth Circuit held, under California law, that an insurer had no duty to defend an insured actuarial services firm in litigation alleging that the insured's reserve reviews and rate level recommendations contributed to the insolvency of a medical malpractice self-insurance fund. *Zurich Specialties London Limited v. Bickerstaff, Whatley, Ryan & Burkhalter, Inc.*, Docket No. 09-56884, 2011 U.S. App. LEXIS 6383 (9th Cir. Mar. 28, 2011). The underlying complaint, filed by the insolvent fund's accountants, sought contribution from the actuarial services firm in an action by the fund's receiver against the accountants. The actuarial services firm sought coverage under its professional liability policy, which excluded claims "arising out of . . . the insolvency or bankruptcy of the Insured or any other person, firm or organization."

The court held that the allegation that the insured played a causal role in the insolvency of the self-insurance fund was sufficient to satisfy California's broad definition of the term "arising out of" and to trigger the insolvency exclusion. The court rejected the insured's assertion that because the fund was already insolvent before the insured was retained the action was a standard malpractice claim based on work performed for an already insolvent client. The court noted that insolvency is an ongoing process, and that the complaint sufficiently alleged that the firm contributed to the fund's worsening financial condition. The court also found the doctrine of concurrent causation inapplicable because the conduct excluded by the policy—the insured firm's alleged contribution to the fund's insolvency—was not independent of any covered malpractice. The court concluded that the duty to defend was not triggered because the underlying action fell squarely within the insolvency exclusion. The insured could not establish a duty to defend by speculating that the financial condition of the currently insolvent entity might improve and potentially render the insolvency exclusion inapplicable.

CGL Policies are not Performance Bonds

VRV Development, a general contractor hired to develop residential lots in Dallas, TX, purchased commercial general liability (CGL) coverage from Mid-Continent Casualty in May 2004, during the development process. The coverage was renewed in May 2005 but not in May 2006. In early 2007, heavy rains caused retaining walls on four lots to collapse after cracks were discovered in one of the walls the prior July; the resulting property damage led to a lawsuit. VRV tendered the suit to Mid-Continental, which refused to defend or indemnify and VRV sued. The U.S. Court of Appeals for the Fifth Circuit affirmed the lower court's entry of summary judgment in favor of the insurer, concluding that while the damage to the walls occurred during the effective period, such damage was subject to the products-completed

operations hazard exclusion. *VRV Development LP v. Mid-Continental Casualty Co*.,630 F.3d 451, 455 (5th Cir. 2011). The court stated that CGL policies generally "do not serve as a performance bond covering an insured's own work." Moreover, the court observed that the property damage was caused by the collapse of the walls, not exposure to the cracks, explaining that "property damage does not necessarily occur at the first link in the causal chain of events," thus the focus must be on "the time of the actual physical damage…not the time of the negligent conduct."

Some Damage Resulting from Subcontractor's Work Covered, 8th Circuit Says
Although defective workmanship resulting in damage to an insured's product is not an occurrence under a commercial general liability (CGL) policy and, thus, is generally not covered, collateral damage that occurs as a result is covered, the U.S. Court of Appeals for the Eighth Circuit held. *Lexicon, Inc. v. ACE*, No. 10-1100, 2010 U.S. App. LEXIS 26271 (8th Cir. Dec. 28, 2010). Lexicon was hired to fabricate six silo storage bins at a direct reduced iron plant and subcontracted the silo work to Damus Ltd. Months after the project was completed, one of the silos collapsed because of faulty welding by Damus, causing millions of dollars in property damage. Lexicon's CGL insurers denied coverage, and Lexicon filed a breach of contract claim against the insurers. The district court ruled that under Arkansas law, property damage resulting from faulty work of a subcontractor was not an occurrence for purposes of a CGL policy; thus the insurers were not obligated to reimburse the contractor for any property damage caused by the subcontractor's failed welds. The appellate court held that Arkansas law limits coverage for damage to the work product itself, *i.e.* the silos, but that the collateral property damage that resulted because the silos collapsed was covered. Under Arkansas law, it was foreseeable that faulty contractor work would damage the silo, but it was not foreseeable that it would cause collateral damage.

Prior Knowledge of Arbitration Does Not Make Arbitrator "Interested"
The U.S. Court of Appeals for the Seventh Circuit rejected attempts by a party to obtain an injunction preventing an arbitrator from serving on a pending arbitration, in a case involving a reinsurance dispute between Trustmark Insurance Company (Trustmark) and John Hancock Life Insurance Company (Hancock). In 2004, a three-member arbitration panel ruled in Hancock's favor on the issue of the issue of the extent of Trustmark's reinsurance obligations. However, Trustmark refused to pay the bill Hancock sent it, causing Hancock to start another arbitration. Hancock named the same party-appointed arbitrator for the second arbitration that it had named in the first. With respect to the confidentiality agreement governing the first arbitration, the umpire and Hancock's arbitrator extended that confidentiality agreement to the second arbitration and ruled that they could consider the evidence and rulings from the first arbitration. Before the arbitration reached a hearing on the merits, Trustmark filed a lawsuit in the Northern District of Illinois, requesting an injunction preventing the arbitration from proceeding with Hancock's appointed arbitrator on the grounds that Hancock's arbitrator was not "disinterested," because he knew what had happened in the first arbitration. Trustmark also contended that the second arbitration panel had no authority to interpret or act on the confidentiality agreement from the first arbitration because the confidentiality agreement did not have its own arbitration clause. The district court granted an injunction in favor of Trustmark preventing Hancock's arbitrator from serving in the second arbitration.

In *Trustmark Ins. Co. v. John Hancock Life Ins. Co. (U.S.A.),* 631 F.3d 869, (7th Cir. 2011), the U.S. Court of Appeals for the Seventh Circuit reversed the district court for two reasons. First, Trustmark had not suffered the irreparable harm necessary for an injunction. The only harm Trustmark would suffer in waiting until the arbitration was completed was monetary, such as fees for attorneys and arbitrators, that was not irreparable. Second, the court went on to reject Trustmark's claims on the merits because Trustmark seemed "determined to tarnish" the reputation of Hancock's arbitrator. It held that Hancock's arbitrator was disinterested because he was "lacking a personal or financial stake in the outcome." An arbitrator does not gain an "interest" through knowledge about a prior proceeding between the same parties. The court also ruled that arbitrators had authority to rule on the effect of the confidentiality agreement because

this was procedural question to be decided by the arbitrators. The confidentiality agreement was closely related to the arbitration and presumptively within the scope of reinsurance agreement's comprehensive arbitration clause.

Prior Knowledge Provision is a Condition Precedent to Coverage; Innocent Insured Exception is Inapplicable
The U.S. Court of Appeals for the Fourth Circuit, applying Virginia law, held that there is no coverage under a professional liability insurance policy where the policy's prior knowledge provision, which is a condition precedent to coverage, was not satisfied. *Bryan Bros., Inc. v. Cont'l Cas. Co*., No. 10-1439, 2011 U.S. App. LEXIS 6131 (4th Cir. Mar. 24, 2011). In July 2008, an accounting firm obtained a professional liability insurance policy, which included a provision that "prior to the effective date of this policy, none of you had a basis to believe that any such act or omission, or interrelated act or omission, might reasonably be expected to be the basis of a claim." The policy also included a "bad acts" exclusion, which excluded claims arising from dishonest, illegal, fraudulent, criminal or malicious acts. Additionally, the policy had an innocent insured exception to the bad acts exclusion, which provided that if the bad acts exclusion otherwise applied, it would not apply to those who did not commit the bad acts.

In 2009, the firm discovered that the firm's account clerk had stolen funds from eight clients' accounts. The thefts began in 2002 and continued sometime after July 2008, during the policy period. The victims asserted tort claims against the accounting firm, which in turn sought insurance coverage of the claims. The insurer denied coverage because the account clerk had reason to believe, before the effective date of the policy, that her actions might be the basis of a claim. The firm argued that because no one other than the accounts clerk had knowledge, the innocent insureds exclusion should apply. The district court granted summary judgment to the insurer based on the account clerk's prior knowledge. The Fourth Circuit agreed, finding that the prior knowledge provision was a condition precedent under Virginia law, which, because the clerk had prior that her acts could be the basis of a claim, was not fulfilled, precluding coverage under the policy. As such, the bad acts exclusion and the innocent insured's exception were never reached.

Insurer May Rely on Undisputed Evidence Outside the Complaint to Deny a Defense
The United States District Court for the Eastern District of Washington held that an insurer may rely on undisputed evidence outside the complaint to deny a defense to the insured when the extrinsic evidence does not bear upon the allegations' truth or scope, but rather, concerns only a discrete, independent coverage issue. *Wendel v. Travelers Cas. and Sur. Co. of Am*., No. Civ. 10-0028-LRS, 2011 WL 864863 (E.D. Wash. Mar. 10, 2011). In 2005, the insured purchased an Employment Practices Liability (EPL) policy from the defendant insurer to protect his business from employment-related claims. The policy was extended when the insurer issued a 2007-2008 renewal EPL policy. In 2007, the widower and personal representative of a deceased former employee of the insured filed suit alleging that the insured had pressured the decedent to engage in an improper and manipulative sexual relationship while she was employed by the insured, ultimately resulting in the decedent's termination from employment and suicide. In 2004, another former employee had sued the insured alleging that she was distressed by the sexual affair between the insured and the decedent and further alleged facts regarding the decedent's firing and suicide. The insurer, relying on the complaint in the 2004 lawsuit, denied coverage for the widower's 2007 suit based upon the policy's "prior and pending litigation" exclusion, which provides in relevant part:

> This insurance shall not apply to, and the Company shall have no duty to defend or pay Defense Expenses for, any Claim…for, based upon, or arising directly or indirectly out of any fact, circumstance, situation, transaction, event or Wrongful Employment Practice… underlying or alleged in any prior and/or pending civil, criminal, administrative or regulatory proceeding as of the applicable Prior and Pending Proceeding Date . . .

The court agreed and found that coverage for the widower's suit was excluded because the facts surrounding the affair with the decedent and her death were alleged in the former

employee's lawsuit before the "prior and pending" date of the policy. The court further found, notwithstanding a lack of Washington law on the subject, that an insurer may rely on undisputed evidence outside the complaint to avoid its duty to defend when the extrinsic evidence bears not upon the allegations' truth or scope but concerns only a discrete, independent coverage issue.

Insurance Does Not Automatically Transfer to New Owner of Property by "Operation of Law" Under CERCLA

Lockheed Martin ("Lockheed") sought access to an insurance policy held by Goodyear Tire & Rubber Company ("Goodyear") before Goodyear sold some of its assets to a company that later merged with Lockheed Martin. In Lockheed Martin Corp. v. Goodyear Tire and Rubber Co., Case No. 5:10 CV 673, 2011 U.S. Dist. LEXIS 13677 (N.D. Ohio Feb. 11, 2011), the parties disputed whether a CGL policy followed the land when the land was determined to be contaminated under federal law. Real property transferred to Lockheed from Goodyear was determined to have been contaminated with polychlorinated biphenyls ("PCBs"), a hazardous material. Under the Comprehensive Environmental Response, Compensation and Liability Act ("CERCLA"), Lockheed was strictly liable for remediation of the property. Relying on a Ohio state decision, Pilkington North America, Inc. v. Travelers Casualty & Surety Co., 861 N.E.2d 121 (Ohio 2006),[1] Lockheed alleged that Travelers, the successor insurer to Aetna which had issued CGL policies to Goodyear, was required to contribute to response costs. Travelers disagreed, noting that Lockheed had expressly disclaimed any rights to the pre-existing insurance policies under the Asset Purchase Agreement, making Lockheed a stranger to the policy. Travelers argued that if Lockheed were allowed to access Goodyear's policies by operation of law because Lockheed had become independently liable for the sites under CERCLA, Goodyear would face the probability that the policy limits would be eroded by payments to an "additional insured" who did not emerge until decades later, and Travelers would have to pay for the defense of the new additional insured (Lockheed) and be subject to the risk that it would have to defend multiple other additional insureds who would have CERCLA liability for the sites. The court agreed with Travelers.

[1]*In Pilkington, the Ohio Supreme Court held that a chose in action arises under an occurrence based policy at the time of loss, and that the chose of action as to the duty to indemnity is unaffected by anti-assignment provisions if the covered loss occurred before a contractual transfer of the liability. The Pilkington court did not reach the question of the liability being transferred by operation of law.*

FROM THE REGULATORS

South Carolina Joins States Where CGL Policies Cover Damage Resulting from Faulty Workmanship by Law

Following a decision of the Supreme Court of South Carolina which held that damage that directly results and is the natural and expected consequence of faulty workmanship is not an occurrence under a Commercial General Liability (CGL) policy, the South Carolina General Assembly passed a bill that defines "occurrence" in a CGL policy to include "property damage or bodily injury resulting from faulty workmanship, exclusive of the faulty workmanship itself." S.C. Code § 38-61-70. In Crossman Communities of North Carolina, Inc. v. Harleysville Mutual Insurance Co., 2011 S.C. LEXIS 2, Opinion No. 26909 (S.C. Jan. 7, 2011), the South Carolina Supreme Court overturned the trial court's determination that property damage resulting from water intrusion following the negligent installation of siding, windows, and flashing, constituted an "occurrence" under the CGL policy. In answering the question whether faulty workmanship that directly causes further damage to non-defective components of the insured's project constitutes an occurrence, the Supreme Court found that "the natural and expected consequence of negligently installing siding is water intrusion and damage to the interior of the units," concluding that there

was no occurrence. Id.at *24. In so ruling, the Court overturned its prior holding in Auto Owners Ins. Co. v. Newman, 395 S.C. 187, 684 S.E.2d 541 (2009). The Crossman Court declared it was applying the "majority rule" in denying CGL coverage of damage resulting from poor workmanship.

The South Carolina General Assembly passed legislation overturning the decision, defining damage resulting from faulty workmanship as an occurrence, thus joining Arkansas and Colorado as states which have passed laws either defining "occurrence" in CGL policies to mean "property damage or bodily injury resulting from faulty workmanship," Ark. Code § 23-79-155, or instructing the state courts to presume that the work of a construction professional that results in property damage is an accident unless the damage is intended and expected by the insured. See Colo. Rev. Stat. § 13-20-808 (2010).

Hawaii also appears ready to join South Carolina, Arkansas and Colorado. Hawaii's General Assembly recently passed a bill stating that a decision of the Hawaii Intermediate Court of Appeals, Group Builders, Inc. v. Admiral Ins. Co., 231 P.3d 67 (Haw. Ct. App. 2010), which found that damage resulting from faulty workmanship was not an occurrence under the CGL policy. The proposed legislation, which is currently before the Hawaiian governor, defines "liability insurance policy" as "a contract of insurance including an owner-controlled, contractor-controlled, or other similar pooled insurance program that covers occurrences of damage or injury during the policy period that insures a construction professional for liability arising from construction-related work." Hawaii H.B. 924 (for a copy of the legislation, please see www.capitol.hawaii.gov/session2011/bills/HB924_SD2_.htm).

McRaith Named Director of Federal Insurance Office
Michael McRaith, Director of the Illinois Division of Insurance, has been named by Treasury Secretary Geithner to be the initial Director of the new Federal Insurance Office, which was created last year by the Dodd-Frank Act. Director McRaith spent 15 years in private practice in Chicago prior to being appointed as Director of the Illinois Division of Insurance in 2005. Among his clients while in private practice were financial institutions, including insurance companies. He has been active in the National Association of Insurance Commissioners (NAIC), currently serving as secretary-treasurer. He has served as chair and vice-chair of the NAIC's Property and Casualty Insurance (C) Committee. Director McRaith will serve as a non-voting member of the Financial Stability Oversight Council. Significantly for our readers, both Director McRaith and Missouri Insurance Director John Huff (a non-voting member of the FSOC appointed by the NAIC) have been members of the NAIC's Reinsurance Task Force. The "insurance expert" voting member of the FSOC remains to be appointed by President Obama.

California Approves Regulations Regarding Dwelling Coverage
As of June 27, 2011, every agent and broker engaged by an insurer to sell dwelling or homeowners insurance in California is subject to new regulations recently approved by the state's Office of Administrative Law. The new regulations, proposed in 2010 by the California Department of Insurance, were prompted in part by reports that policyholders who lost their homes in major wildfires were not fully insured for the cost of replacing them. Among other things, the new regulations require agents and brokers to be trained on the differences between homeowners and fire or dwelling property policies, the differences between actual cash value coverage and replacement cost coverage.

The regulations are available at http://www20.insurance.ca.gov/epubacc/REG/151771.htm.

Connecticut's Insurance Department Issues Notice of Intent to Amend Regulations
Connecticut issued a notice to modify its regulations in accordance with a National Association of Insurance Commissioners (NAIC) Model to strengthen standards and procedures for suitable annuity recommendations, and to strengthen the requirements of insurers to establish a system to supervise recommendations so that the needs and financial objectives of consumers are appropriately addressed. These amendments establish a regulatory framework that holds

insurers responsible for ensuring that the annuity transactions are suitable, whether or not the insurer contracts with a third party to supervise or monitor the recommendations made in the marketing and sales of annuities. These amendments also add a new section to set uniform training standards in the sale of annuities for producers.

Rhode Island Issues Reminder regarding Insurance Certificates
Rhode Island's insurance division recently issued a bulletin reminding insurers that "the improper modification of certificates of insurance is an unacceptable business practice." (For a copy of the Bulletin, please see: www.dbr.state.ri.us/documents/news/insurance/insuranceBulletin2011-1.pdf.) Echoing language issued by several other states in recent years, the bulletin adds that "certificates of insurance cannot be used to amend, expand or alter the terms of the underlying insurance policy. Also, the bulletin states that insurance producers who misrepresent policy terms or conditions will be subject to penalties, including possible suspension or revocation of one's license.

Texas Bans Discretionary Clauses in Insurance Contracts
The Texas Department of Insurance ("TDI") has officially banned the use of discretionary clauses in insurance contracts with an order issued on December 3, 2010 (the "Order"). The ban is the result of a petition filed by the Texas Office of Public Insurance Counsel (OPIC) on October 28, 2009 requesting the ban. Subsequent to the petition, the TDI held a public hearing on July 12, 2010. Discretionary clauses allow insurers to interpret policy terms and evaluate an insured's claim for benefits. In justifying the ban, Insurance Commissioner Mike Geeslin noted among other reasons that "[d]iscretionary clauses are unjust, encourage misrepresentation, and are deceptive because they mislead consumers regarding the terms of coverage."

The Order will be effective for health, life, and disability forms offered, issued or renewed on or after June 1, 2011, except that any forms which include disability income protection coverage providing for periodic payments during disability due to sickness and/or accident will have an earlier effective date of February 1, 2011. The Order does not apply retroactively to forms that have already been issued or delivered and do not contain a renewal date until there is a rate increase or any change, modification, or amendment to the form occurring on or after June 1, 2011.

For a copy of the Order, please see: www.eapdlaw.com/files/upload/3_1201-3_12031.pdf.