

INSURANCE NEWS

SUMMER 2014



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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.*

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Art, Yachts, and Insider Plots

David L. Hall, Wiggin and Dana LLP

Suppose your name is Radu and you're a young plumber working in Bucharest during the endless month of February. This is when you decide you've had enough of Bucharest in February. You find yourself in sunny Genoa, and manage to obtain employment with a yacht services company by lying about your maritime experience. The salt air, the turquoise water: this is a real step up from Bucharest. But plumbing is plumbing; your back hurts and you can't get your hands clean. How unfair that you are stooped in a cramped engineering space turning a wrench while carefree yachtsmen are gallivanting around the Riviera.

You're aboard HAPPY WIFE, a 75-meter yacht with a Jacuzzi, a master suite, expansive berthing for four additional couples, a galley designed by an Iron Chef runner up, a tender, three Zodiacs, SCUBA gear, and liquor enough to sink a destroyer. That's when it occurs to you: the Picasso in the main salon is just sitting there waiting to be taken. It's probably worth millions. There is an alarm system, but it doesn't work when the power is down, which it often is during servicing. The Picasso is secured to the bulkhead with wall mount locks. But you have every conceivable type of wrench, don't you? You start thinking. There is cousin Niku who is studying fine arts nearby. True, you haven't been in touch for a while, but he'll get over it when he hears about the millions.

Two months later, HAPPY WIFE is back at sea, with new head plumbing, a new bilge water system, and a new Picasso; not a real one, mind you, but a forgery by Niku -- good enough to fool the American owner, who has not to date displayed a deep appreciation for cubism. There were a couple of close calls with Niku, who insisted on coming aboard to

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FROM
TheCOURTS**Brokers' Duties to Clients**

Voss v. Netherlands Insurance and CH Insurance Brokerage Services, 2014-01259
(N.Y. Feb. 25, 2014)

In this case, New York's highest court examined the issue of a broker's liability related to placement of business interruption coverage. Deborah Voss owned several businesses in New York City and used CH Insurance to place property coverage. In 2004 during the initial placement of coverage, Voss asked her broker if \$75,000 of business interruption coverage was sufficient, to which the broker replied in the affirmative. Thereafter, Voss purchased a new, larger building and moved all of her businesses into it. Voss again discussed her insurance with the producer, and the policy was renewed with the \$75,000 in business interruption coverage. Not long afterward, the property experienced multiple problems, including a leaking roof, which forced the businesses to temporarily close. Nevertheless, when Voss met with a different producer at CH Insurance, the producer lowered the business interruption limits to \$30,000.

Voss sued CH Insurance for its failure to advise her as to appropriate limits of business interruption coverage. In New York, the general rule is that insurance brokers "have a common-law duty to obtain requested coverage for their clients within a reasonable time or inform the client of the inability to do so; however, they have no continuing duty to advise, guide or direct a client to obtain additional coverage." Thus, a client can only prevail if she has made a specific request related to coverage, and

such coverage was not procured. However, where a "special relationship" exists between the broker and client, there can be liability even without a specific request. A special relationship can exist when (1) the broker receives compensation for services beyond commission; (2) there is a question regarding coverage with the client relying on the expertise of the broker; and (3) there is a course of dealing over time that puts the broker on notice that their advice is being specially relied upon by the client. Here, the court determined that the evidence suggested that Voss was relying upon the expertise of the broker with respect to business interruption coverage, and the trier of fact needed to determine if a special relationship existed. The case was therefore remanded.

Duty to Defend

Composite Structures Inc. v. The Continental Insurance Co., No. 12-15866
(11th Cir. Mar. 20, 2014)

Applying Florida law, the U.S. Court of Appeals for the Eleventh Circuit held that underwriters did not have to defend a boat manufacturer against claims of injuries from carbon monoxide exposure. In the underlying lawsuit, two men who had been working on a vessel built by the manufacturer claimed that they were exposed to excessive carbon monoxide fumes. While the manufacturer did not dispute that the underlying suit fell within the pollution exclusion of its general liability policy, it argued that underwriters nonetheless had a duty to defend because an exception to the exclusion applied

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that provided coverage as long as it met certain conditions, including several short deadlines. The Eleventh Circuit held that it would have been impossible for the manufacturer to meet those deadlines.

The court therefore found an exception to the general rule that courts can consider only the allegations in the complaint and the insurance policy in determining whether underwriters have a duty to defend; and the court held that there was no duty to defend here considering the date that Composite provided written notice of the claim to underwriters.

Horizontal Exhaustion of Policy Limits

Viking Pump Inc. et al. v. Century Indemnity Co. et al., No. 10C-06-141 FSS CCLD (Apr. 9, 2014)

The Delaware Superior Court recently held that under New York law, as long as a lower-level excess policy in a given year is exhausted, the excess policy that sits above it can be triggered, even where other primary coverages remain available. Thus, excess policies do not have to be horizontally exhausted in a long-tail coverage case.

The horizontal exhaustion issue comes into play when a policyholder's losses occur gradually over multiple policy periods, and a court is required to determine the order in which insurance policies spanning those periods should be triggered.

This case arose after Viking Pump sought coverage from its primary, umbrella, and excess insurers for asbestos claims filed against it. After eight years of litigation, the Delaware trial court (applying New York law) held that "all sums" allocation applied, but that horizontal exhaustion was required. The excess insurers thereafter sought clarification of how horizontal exhaustion would apply to their policies.

Although New York's accepted rule is that horizontal exhaustion is required before excess policies are triggered, New York courts have not actually addressed the problem of whether horizontal exhaustion applies to every layer or only the primary and umbrella layers. Thus, the Delaware Court had to predict that New York's highest court would not require policyholders to horizontally exhaust excess policies in long-tail coverage cases. It remains to be seen whether *Viking Pump* will be followed by courts in New York.

Duty to Defend-Cyber Risks

Zurich American Insurance Co. v. Sony Corp. of America et al., No. 651982/2011 (Feb. 21, 2014)

A New York Court held that underwriters had no duty to defend certain units of Sony Corp. in numerous lawsuits stemming from a 2011 cyberattack on Sony's PlayStation Network. The breach of Sony's network was one of the largest recorded data security breaches at the time, and Sony shut down the network for about a month while it responded to the breach. The court found that the relevant insurance policy provision

Art, Yachts, and Insider Plots

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paint the forgery in situ, but – with the owner away -- you managed to avoid detection. You're feeling pretty smart except for one thing: you don't know exactly how to sell a Picasso. But you are from Bucharest and surely someone there can help.

And so it goes: the unsuspecting American happily sails off with his forged Picasso as the real one enters the stream of commerce in Bucharest. Radu will be disappointed in his take, assuming he enjoys one at all. The theft eventually will be discovered, commonly in one of two ways: the American yachtsman dies and his estate seeks a valuation of the forged Picasso; or a subsequent good faith purchaser of the real Picasso tries to sell it, and someone notices an inconsistency in provenance. But in all likelihood, years will pass before the theft is detected and years more will pass before the intervening transactions are unwound.

A yacht is not the perfect place to exhibit fine art for a number of reasons, starting with the harsh marine environment. A yacht is also a relatively easy target for theft, particularly given the large number of insiders with access, including the crew. But if your main salon requires a Picasso to fulfill its promise, consider enhanced security (such as a security guard and video monitoring) and make sure you have insurance coverage for the full value of the painting.

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applied only to Sony as the policyholder, not to the actions of the third party hackers who stole PlayStation Network users' confidential information; thus, coverage under the policy did not extend to third parties.

The lawsuit was brought by Zurich in July 2011, seeking a declaratory judgment that there was no coverage for nearly sixty lawsuits against Sony that resulted from the hackers' theft of personal information belonging to millions of PlayStation Network users. Zurich participated in one general liability policy that was part of a tower of general liability policies covering Sony. Zurich successfully argued that none of the suits asserted claims for "bodily injury, property damage or personal and advertising injury," for which Sony would be entitled to defense or indemnity.

Timeliness of Declination of Coverage

***Country-Wide v. Preferred Trucking Services et al.*, No. 21 (Feb. 18, 2014)**

In this case, New York State's highest court excused an insurer's four-month delay in disclaiming coverage, based on an insured's failure to cooperate. The court held that the facts confirmed that the insurer disclaimed coverage as soon as "reasonably possible" after it determined that the insured would not cooperate. Under New York law, there is no specific time frame within which an insurer must disclaim coverage; the court reaffirmed that the inquiry "is necessarily case specific."

The underlying claim arose from a trucking accident in which Filippo Gallina was injured while unloading a vehicle that was

owned by Preferred Trucking and operated by its employee, Carlos Arias. Preferred Trucking was insured by Country-Wide under a business-auto policy. In March 2006, Gallina and his wife commenced a personal injury action against Preferred Trucking and Arias, and in September 2007, the Gallinas' attorneys filed a motion for a default judgment against them. The attorneys provided a copy of the motion to Country-Wide in October 2007, which constituted the first formal notice of the lawsuit to Country-Wide, and thereafter Country-Wide retained attorneys to defend Preferred and Arias. Thereafter Country-Wide made continuous efforts to obtain the cooperation of the insureds, but received little response; thus, in November 2008, Country-Wide disclaimed its obligation to defend and indemnify them as a result of their non-cooperation. The Gallinas then obtained a judgment against the defendants, and were awarded \$2,550,000 in damages. Country-Wide commenced a declaratory judgment action against Preferred, Arias and the Gallinas for a declaration that it had no obligation to defend and indemnify Preferred and Arias with respect to the underlying action and judgment. The trial court held that Country-Wide was obligated to indemnify Preferred Trucking (but not Arias), and Country-Wide appealed.

The Court of Appeals reversed, emphasizing that insurers are encouraged to disclaim for non-cooperation only when multiple further attempts to provoke cooperation are unsuccessful.

Note: The New York Court of Appeals gave underwriters another victory on June 10th when it ruled that a New York State insurance law requiring disclaimers of coverage "as soon as reasonably possible"

applies only to death and injury claims arising out of auto and other accident in New York. *KeySpan Gas East Corp. v. Munich Reinsurance America, Inc.*, 2014 N.Y. LEXIS 1319 (N.Y. June 10, 2014)

Bad Faith; Effect of Covenant Judgment

***Ryan E. Miller v. Safeco Insurance Co.*, No. 68594-5-1 (Apr. 28, 2014)**

In 2000, Patrick Kenny rear-ended a cement truck, causing his three passengers to sustain severe injuries. Kenny was driving the car of one of the passengers (with her permission), and therefore argued that he was covered under the passenger's parents' Safeco policy. In 2003, Kenny settled with the passengers, agreeing to pay \$1.8 million in insurance proceeds available, which included \$1.5 million from Safeco. He also agreed to assign his rights to one of the passengers, Ryan Miller, to sue Safeco for bad faith claims. In return, the passengers granted Kenny a covenant not to execute on or enforce any excess judgment. Safeco agreed on \$4.15 million for the covenant judgment, which was the amount of damages that remained unpaid.

Miller asserted claims of bad faith, negligence, Consumer Protection Act violations, and other theories against Safeco, contending that the insurer could have promoted an earlier policy limits settlement. The jury returned a plaintiff's verdict of \$13 million in addition to prejudgment interest of \$7 million, post-judgment interest at twelve percent, attorneys' fees and costs of \$1.7 million, and Consumer Protection Act treble damages,

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leading to a total verdict of \$21,837,286.73. On appeal, Safeco argued that the jury impermissibly awarded damages exceeding the covenant judgment amount. The Washington Court of Appeals held that “in an insurance bad faith case, the amount of a reasonable covenant judgment sets a floor, not a ceiling, on the damages the jury may award,” and affirmed the jury verdict. The Court reasoned that the covenant judgment is for the injured party, while the insured’s damages must be determined in a bad faith case, and the covenant is not a limitation.

Marine Insurance - Misrepresentation/Nondisclosure

***Fireman’s Fund Insurance Co. et al. v. Great American Ins. Co. of New York et al.*, 10 Civ. 1653 (S.D.N.Y. Mar. 31, 2014)**

In late August 2009, AFDB-5 (the “Drydock”) sank at its berth in calm waters in Port Arthur, Texas. The plaintiffs brought an action against defendants Great American Insurance Company of New York (“Great American”), Max Specialty Insurance Company (“MSI”), and the insured, Signal International, LLC (“Signal”), seeking a declaration as to the rights and obligations of the parties under various insurance policies. Years of discovery gave way to documents reflecting the Drydock’s dilapidated condition, and disagreement over the extent of coverage led to accusations of fraud and concealment.

The Court held that the case was appropriate for resolution on summary judgment, explaining that in light of the information regarding the Drydock that

Signal failed to provide to MSI, “it is beyond genuine dispute” that a 2009 Property Submission was “incomplete, misleading, and arguably false,” and the submission did not provide a complete or accurate picture of the value and condition of the Drydock.

Furthermore, the undisclosed information was material because it may have led a “prudent insurer” to require a higher premium to cover the Drydock. The Court thus granted MSI’s motion for summary judgment on its material misrepresentation claim.

Duty to Defend Triggered by Subpoena/Investigation

***Syracuse University v. National Union Fire Insurance Co. of Pittsburgh, Pa.*, 2013 WL 6823101 (N.Y. App. Div. Dec. 27, 2013)**

A New York appellate court held that investigations and subpoenas possibly implicating an insured may trigger the duty to defend and to advance defense costs. The underlying dispute arose out of government investigations of child molestation allegations against a former basketball coach. Syracuse was served with six subpoenas in connection with state and federal grand jury investigations that demanded a wide range of materials from Syracuse, including, among other information, a list of all secretaries who ever worked for the coach, a list of the coach’s hotel accommodations, and a list of bus companies that drove the basketball team. Syracuse provided notice of the subpoenas to National Union, which had insured Syracuse under a not-for-profit individual

and organization liability policy, but National Union denied coverage, contending that the subpoenas did not constitute policy claims and did not involve alleged “wrongful acts” against Syracuse. The coverage litigation began in August 2012.

The Appellate Division applied the well-settled rule that an insurer has a duty to defend, as long as the claim involves facts or allegations that potentially fall within coverage, and concluded that the subpoenas triggered the insurer’s defense obligations. The judge noted that even if Syracuse was not a target at the time of the issuance of the subpoenas, prosecutors could still bring charges against the college based on information they learned from the subpoenas. Accordingly, the court determined that “the information sought meets the standard of a potential claim implicating the policy’s coverage.” Because the court concluded that the subpoenas could implicate the policy’s coverage, it held that the insurer had a duty to provide defense costs relating to the subpoenas, stating that “an insurer’s duty to defend and to pay defense costs under liability insurance policies may be construed broadly in favor of the policy holder.”

Impact of Refusal to Provide Defense-Redux

***K2 Inv. Grp., LLC v. Am. Guarantee & Liab. Ins. Co.*, 22 N.Y.3d 578, 983 N.Y.S.2d 761 (2014) reargument denied, 2014-315, 2014 WL 1775888 (N.Y. May 6, 2014)**

Readers may recall this case from our last Newsletter; the New York Court of Appeals

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has now reversed itself and reaffirmed an earlier ruling in *Servidone Construction Corp. v. Security Insurance Company of Hartford* (64 NY2d 419 (1985)). In doing so, the Court of Appeals reestablished the rule that a liability insurer who breaches a contractual duty to defend its insured is not barred from contesting the duty to indemnify, where coverage is disputed.

In K2, clients who had obtained a default judgment in a legal malpractice action against their attorney, and had subsequently been assigned all of his rights against his law firm's legal malpractice insurer, brought an action against the insurer for breach of contract and bad faith to defend and indemnify. In relevant part, the Court of Appeals held that res judicata principles did not preclude the insurer's defense to indemnification claims, based on policy exclusions. The insurer was exempted from indemnity because the insured's liability was based on conduct within a policy exclusion. The Court of Appeals noted that while an insurer is not permitted to relitigate issues in the underlying case if it breaches its duty to defend, this issue is separate and distinct from whether an insurer is permitted to litigate its indemnity obligation subsequent to a wrongful denial of its duty to defend. In explaining its decision to follow the *Servidone* holding, the Court of Appeals stated that "[w]hen our Court decides a question of insurance law, insurers and insureds alike should ordinarily be entitled to assume that the decision will remain unchanged unless or until the Legislature decides otherwise. In other words, the rule of stare decisis, while it is not inexorable, is strong enough to govern this case."

FROM
TheREGULATORS

Louisiana House Bill 1195 signed into law. In late June, Governor Jindal signed into law legislation on unfair trade practices in the business of insurance. The act contains the following provision: "... to provide that any policy or contract without notice indicating that the policy or contract contains defense costs within the limits of liability shall be deemed such an unfair trade practice." The act further states that "The following are declared to be unfair methods of competition and unfair or deceptive acts or practices in the business of insurance: ... Failure by an admitted insurer upon renewal or issuance of any policy or contract of insurance which includes a provision that the policy or contract contains defense costs within the limits of liability to provide notice of such provision through a separate notice or inclusion on the declaration page of the insurance policy or contract."

Connecticut passed legislation with "point of entry" mechanism for non-U.S. insurers. The Connecticut legislature recently passed HB 5053, "An Act Strengthening Connecticut's Insurance Industry Competitiveness." The legislation aims to grow the Connecticut insurance industry by providing the "point of entry" mechanism, which allows for a non-U.S. insurer to enter the U.S. market through the State of Connecticut without the current lengthy process of separately incorporating and licensing a subsidiary in the state.

Connecticut updates laws regarding captive insurers. Senate Bill 188, "AAC Captive Insurance Companies," recently signed into law eases captives insurers looking to transfer their domicile to Connecticut and provides for the evaluation of credit for reinsurance.

Maryland now requires explanation for commercial policy cancellation. Insurers in Maryland now must provide insureds a written reason for cancellation or non-renewal of a policy providing commercial property and liability coverage. Under a new regulation from the Maryland Insurance Administration, the insurer's written statement to the named insured is to include the "actual reason" for the insurer's action when not related to the nonpayment of premium, and an address to which the insured can send a request (within 30 days) for additional information about the insurer's action. The directive does not apply to policies in effect for 45 days or fewer, or to workers compensation and other types of policies specified in the regulation.

AttorneyNOTES

Wiggin and Dana expands Intellectual Property practice and welcomes four new partners to its New York office: Joseph Casino, Michael Kasdan, Abraham Kasdan and Sapna Palla

"Based on current and projected client demand, we targeted intellectual property as an especially promising growth area for the firm," comments Bob Benjamin, chair of the firm's Executive Committee. "With the addition of this dynamic group, we have greatly enhanced our ability to provide a wide range of IP services to our clients, from intellectual property litigation to licensing and prosecution."

In his nearly 20-year career, Joseph Casino has been lead counsel in major patent litigations in many jurisdictions throughout the United States involving a wide variety of technologies, including consumer electronics, medical devices, and automotive equipment. He has also handled numerous matters before the International Trade Commission. In addition to his litigation practice, Joe counsels clients on the strategic development of their patent portfolios and negotiates complex license agreements.

Michael Kasdan focuses his practice on negotiating, defending and asserting intellectual property rights before the courts, the U.S. Patent and Trademark Office and the International Trade Commission, and in private arbitration and mediation. Mike is trained in electrical engineering and works on a broad range of technologies. He dedicates a significant part of his practice to advising startup and early stage

companies on evaluating, obtaining, valuing, licensing and developing patent portfolios and trademarks.

Joe and Mike have each worked in-house for a major Japanese corporation, in Japan, and are well-versed in Japanese corporate culture.

Abraham Kasdan concentrates his practice on all aspects of patents involving complex technologies. With a Ph.D. in Physics and more than fifteen years of research and development experience at a number of prominent research laboratories, Abe has hands-on, in-depth knowledge covering a wide range of technologies, including electronics, optics, semiconductor processing and materials science. In addition to his work on litigation and licensing matters, he oversees patent prosecution programs for his clients.

Sapna Palla focuses her practice on the fields of pharmaceuticals, biotechnology, drug delivery systems and medical devices, with an emphasis on Hatch-Waxman patent infringement cases for branded pharmaceutical manufacturers and on the emerging patent litigation system in India.

Joe Grasso, David Hall and Michael Thompson presented a master class for the Lloyd's Market Association Academy in the Old Library at Lloyd's in January. Their class provided attendees with an overview of the legal issues relating to risk assessment, insurance coverage disputes and recoveries in the fine art sphere. They discussed art theft, art fraud, and art litigation, as well as best practices for art

loan and consignment contracts. They also presented a program for the International Underwriting Association on Legal Implications of Electronic Communications. Their program provided attendees with an overview of the legal implications arising from electronic communications, including the risks inherent in the use of email (and avoiding "smoking guns"); maintaining confidentiality and privilege in electronic communications; cyber security and vulnerability; and other compliance concerns.

Joe Grasso was a speaker at an ACI program on hot topics in admiralty and maritime law in Houston on February 27, 2014. The program examined recent court cases, including cases from the Supreme Court and various U.S. Circuit Courts, and discussed the implications of those cases. The program also covered emerging trends in Admiralty & Maritime Claims and Litigation, including the latest developments in the BP oil spill litigation, the decline in piracy, the rise in public/private port partnerships and the development of technology and use of AIS.

Michael Menapace co-presented a program on Changes to Federal Rules of Civil Procedure for the Hartford County Bar Association on April 3, 2014. The program reviewed the recently enacted changes to the Federal Rules of Civil Procedure and the proposed changes that have garnered much attention and debate, specifically the proposed change to balance the amount in dispute with the scope of discovery requests.

**Wiggin and Dana
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**About Wiggin and Dana's
Insurance Practice Group**

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 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, energy and aviation. A more detailed description of the Insurance Practice Group, and biographies of our attorneys, appear at www.wiggin.com.

About Wiggin and Dana LLP

Wiggin and Dana is a full service firm with more than 150 attorneys serving clients domestically and abroad from offices in Connecticut, New York and Philadelphia. For more information on the firm, visit our website at www.wiggin.com.

AttorneyNOTES CONTINUED

Michael Menapace taught Insurance Law at the Quinnipiac University School of Law in the Spring 2014 semester. Mr. Menapace has been teaching this course for the past 5 years.

Michael Menapace and **Michael Thompson** moderated a panel at the Fifth Annual Connecticut Privacy Forum hosted by the firm on April 25, 2014. Their panel discussed the key issues in evaluating cyber risk insurance products, including why businesses should consider cybersecurity coverage, representative products on the mark and emerging terms and underwriting requirements.

Joe Grasso has been appointed Chair of the International working Group on Marine Insurance of the Comité International Maritime.

This Newsletter is a periodic newsletter designed to inform clients and others about recent developments in the law. Nothing in the Newsletter constitutes legal advice, which can only be obtained as a result of personal consultation with an attorney. The information published here is believed to be accurate at the time of publication, but is subject to change and does not purport to be a complete statement of all relevant issues. In certain jurisdictions this may constitute attorney advertising.

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