A Survey of Recent Developments in Coverage and Bad Faith

Presentation by: **Christopher E. Ballod**
Pietragallo, Gordon, Alfano, Bosick & Raspanti, LLP

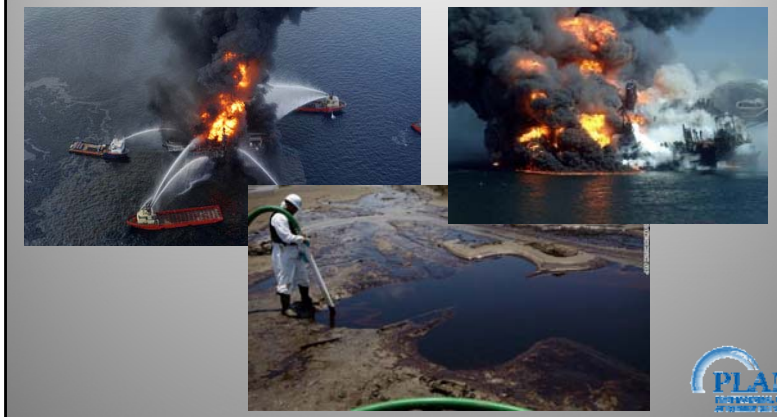
OVERVIEW

- Interesting and/or notable coverage and bad faith cases from 2014-2015
- Some groundbreaking or, at least, new:
  - Deep Water Horizon expands the “four corners” of the policy
  - Cyber coverage continues to develop
- Some familiar:
  - Certificate of insurance does not change the policy
  - The “notice-prejudice rule” does not apply to claims-made policies
  - Bad faith in the failure to settle a claim

COVERAGE

EXPANDING THE "FOUR CORNERS" OF THE POLICY

***In re: Deepwater Horizon, Relator*, No. 13-0670 (TX 2015)**



In re: Deepwater Horizon, Relator, No. 13-0670 (TX 2015)

- Facts
  - Claims for environmental damage arising out of the April 2010 explosion and sinking of the *Deepwater Horizon* oil-drilling rig in the Gulf of Mexico
  - BP was the oil field developer
  - Transocean was the drilling rig owner
  - Drilling Contract between Transocean and BP
  - Transocean agreed to indemnify BP for surface pollution
  - BP agreed to indemnify Transocean for subsurface pollution

In re: Deepwater Horizon, Relator, No. 13-0670 (TX 2015)

- Facts
  - Drilling Contract required Transocean to name BP as additional insured on primary GL and four layers of excess ($700 million in coverage)
  - Additional insured provision required AI status for "liabilities assumed by [Transocean] under the terms of this contract."
  - I.e., surface pollution but ***not*** subsurface pollution
  - Policies had an "Insured Contract" provision
    - Extended "Insured" to include any person "to whom the 'Insured' is obliged by oral or written 'Insured Contract' … to provide insurance such as afforded by [the] Policy."
  - No dispute that the Drilling Contract was an "Insured Contract"

In re: Deepwater Horizon, Relator, No. 13-0670 (TX 2015)

- Facts
  - BP submitted a claim to Transocean's carriers
  - The insurers filed a declaratory judgment action: *In re Deepwater Horizon*, 2011 WL 5547259 (E.D. La. Nov. 15, 2011)
  - The insurers argued that BP was not entitled to coverage for the subsurface claims because of the Drilling Contract
  - BP argued that the policies themselves did not contain this limitation
  - The district court ruled in favor of the insurers – the terms of the Drilling Contract limited the coverage afforded by the policies
  - The Fifth Circuit reversed: coverage defined by the "four corners" of the policies
  - The question was certified to the Texas Supreme Court

In re: Deepwater Horizon, Relator, No. 13-0670 (TX 2015)

- Holding
  - Two approaches:
    1. A policy may incorporate an external limit on additional insured coverage (citing *Urrutia v. Decker,* 992 S.W.2d 440 (Tex. 1999))
    2. "A named insured may gratuitously choose to secure more coverage for an additional insured than it is contractually required to provide." (citing *Evanston Ins. Co. v. ATOFINA Petrochemicals,* 256 S.W.3d 660 (Tex. 2008))
  - Under first approach, the insurers win
  - Under second approach, BP wins.

In re: Deepwater Horizon, Relator, No. 13-0670 (TX 2015)

- Distinguished *ATOFINA*:

  The existence of a ***certificate of insurance*** naming ATOFINA as an additional insured meant that … there was no need to look to the underlying service contract to ascertain ATOFINA's status as [an additional insured.] Moreover, section III.B.6 of the policy in *ATOFINA* made ***no reference to the service contract in determining the scope of additional-insured coverage***, while the Transocean policies refer to an "Insured Contract" that requires Transocean to provide the insurance as a predicate to status as an "Insured."

- In other words, had there been a certificate of insurance saying BP was an AI and/or there was no "Insured Contract" provision, there would have been no need to look at the Drilling Contract

In re: Deepwater Horizon, Relator, No. 13-0670 (TX 2015)

- "The language in the insurance policies providing additional-insured coverage 'where required' and as 'obliged' requires us to consult the Drilling Contract's additional-insured clause to determine whether the stated conditions exist. … [W]hen we do so, it becomes apparent that the only reasonable interpretation of that clause is that the parties did not intend for BP to be named as an additional insured for the subsurface pollution liabilities BP expressly assumed in the Drilling Contract."
- How is this unusual? Why was *ATOFINA* so different?

Certificate of Insurance Does Not Alter Policy

***Daniels v. SMG Crystal LLC*, 2014-1012 (La.App. 4 Cir. 3/25/15)**


CERTIFICATE OF LIABILITY INSURANCE

Daniels v. SMG Crystal LLC, 2014-1012 (La.App. 4 Cir. 3/25/15)

- Facts
  - Slip and fall case at a festival in the Superdome
  - Location of incident not covered under the policy but the COI listed the location
- Holding
  - The COI does not modify the policy terms
  - Awarded costs and fees for "frivolous" appeal by insured

CYBER LIABILITY COVERAGE

***Zurich Am. Ins. Co. v. Sony*, No. 651982/2011 (N.Y. Sup. Ct. Feb. 21, 2014)**

***Zurich Am. Ins. Co. v. Sony*, No. 651982/2011 (N.Y. Sup. Ct. Feb. 21, 2014)**

- Facts
  - Sony network hacked
  - More than 50 class action complaints filed across the U.S.
  - Old CGL form
  - Policy covered:

    "oral or written publication in any manner of material that that violates any person's right of privacy"

***Zurich Am. Ins. Co. v. Sony*, No. 651982/2011 (N.Y. Sup. Ct. Feb. 21, 2014)**

- Holding
  - No "personal and advertising injury" coverage
  - Breach did result in a "publication."

    In this electronic age, "by just merely opening up that safeguard or that safe box where all of the information was . . . My finding is that that is publication."
  - Publication was not by the insured

    "I am not convinced that this is oral or written publication in any manner done by Sony. That is an oral or written publication that was perpetrated by the hackers"

PEEPING TOM SPIES FUTURE OF CYBER COVERAGE

***Penn-America Ins. Co. v. Sunkissed Tanning & Spa*,**
No. 3917 of 2012 (Pa. Ct. Comm. Pl., Westmoreland Cty. Feb. 19, 2015)

***Penn-America Ins. Co. v. Sunkissed Tanning & Spa*,**
No. 3917 of 2012 (Pa. Ct. Comm. Pl., Westmoreland Cty. Feb. 19, 2015)

- Facts
  - Female patrons sued tanning salon for surreptitiously videotaping unclothed patrons
  - Videos posted on the internet for public viewing
- Holding
  - No coverage under Coverage B for "oral or written publication" because posting of videos on internet is not an "oral or written publication"
  - Even if video posting is a "publication," policy excludes coverage for "violation of a statute, prohibiting the distribution of material or information"

***Penn-America Ins. Co. v. Sunkissed Tanning & Spa*,**
No. 3917 of 2012 (Pa. Ct. Comm. Pl., Westmoreland Cty. Feb. 19, 2015)

- Holding
  - Lower court opinion but interesting divergence re the "publication" requirement
  - Also interesting because it demonstrates that violation of statute exclusion guts Coverage B coverage for internet publications

PRIORITY OF EXCESS/OCIP

***Certain Underwriters v. Illinois Nat. Ins. Co.*,**
No. 09 Civ. 04418 (S.D.N.Y. March 13, 2015)

***Certain Underwriters v. Illinois Nat. Ins. Co.*,**
No. 09 Civ. 04418 (S.D.N.Y. March 13, 2015)

- Facts
  - Trucking accident on construction site
  - Two competing, virtually identical "other insurance" clauses
  - Policies incorporated into an Owner Controlled Insurance Program ("OCIP")
  - OCIP listed Underwriters' policy as an excess policy in the program
  - OCIP did not include coverage for truckers, drivers and haulers, including Continental's insured
  - Continental and UW policies both purported to be excess over other insurance

***Certain Underwriters v. Illinois Nat. Ins. Co.*,**
No. 09 Civ. 04418 (S.D.N.Y. March 13, 2015)

- Facts
  - Continental's argument that UW policy is excess over Continental policy because UW policy was issued per the OCIP which was …
    - a "contract" that "specifically requires that [the UW policy] be primary and contributory,"
    - thereby making the UW policy primary under an exception to the UW "Other Insurance" clause
- Holding
  - "Because OCIP constitutes neither an express nor an implied contract triggering that exception, both 'other insurance' clauses remain in effect and are mutually repugnant on their faces"
  - Both policies provide pro-rata excess coverage

Notice-Prejudice Rule Does Not Apply to Claims-Made Policies

***Craft v. Philadelphia Indemnity Insurance Co.*, 343 P.3d 951 (Colo. 2015)**

- Facts
  - President and majority owner of a contracting company sued for misrepresentations made during merger negotiations
  - Company CGL included D & O coverage
  - Plaintiff did not learn of that coverage until the case resolved more than a year after the end of the policy term
  - Claims-made policy

***Craft v. Philadelphia Indemnity Insurance Co.*, 343 P.3d 951 (Colo. 2015)**

- Facts
  - Plaintiff sued in federal court and 10th Circuit certified two questions to Colorado Supreme Court:

  (1) whether the notice-prejudice rule applies to claims-made liability policies in general; and

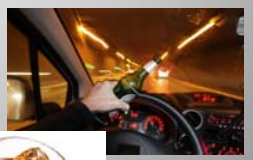
  (2) if so, whether the rule applies to both types of notice requirements in those policies.
- Holding
  - No.
  - "In a claims-made insurance policy, the date-certain notice requirement defines the scope of coverage. Thus, to excuse late notice in violation of such a requirement would re-write a fundamental term of the insurance contract."

***Anderson v. Aul*, 2013AP500 (Wis. Feb. 25, 2015)**

- Facts
  - Legal malpractice case where the attorney's carrier intervened on the coverage issue
  - Claims-made-and-reported policy
  - Wisconsin codifies the notice-prejudice rule: an insured's failure to furnish timely notice will not bar coverage unless (i) timely notice was "reasonably possible," and (ii) the insurance company was "prejudiced" by the delay. Wis. Stat. § § 631.81(1) and 632.26(2).
- Holding
  - Language of claims-made-and-reported policies trumps the Wisconsin statute
  - Even if it did not, "[r]equiring an insurance company to provide coverage for a claim reported after the end of a claims-made-and-reported policy period is per se prejudicial to the insurance company"

RESERVATION OF RIGHTS INEFFECTIVE WHEN NOT SENT TO ADDITIONAL INSURED

Erie Ins. Ex. v. Lobenthal, 2015 WL 1668183 (Pa. Super. 2015)



Erie Ins. Ex. v. Lobenthal, 2015 WL 1668183 (Pa. Super. 2015)

- Facts
  - Plaintiffs injured in a car accident
  - Alleged that the additional insured — Ms. Lobenthal — was liable for the accident because she provided drugs and alcohol to the driver of the car
  - Erie sent a reservation of rights letter, and then a second 9 months later, to Ms. Lobenthal's parents and her attorney
  - Both letters only reserved the right to disclaim coverage against the parents, and made no mention of Ms. Lobenthal
  - In declaratory judgment action the trial court granted summary judgment to Erie ruling that Erie had no duty to defend or indemnify Lobenthal

Erie Ins. Ex. v. Lobenthal, 2015 WL 1668183 (Pa. Super. 2015)

- Holding
  - The Court found no notice to Ms. Lobenthal
  - Erie first referenced the controlled substances exclusion in the policy in its second letter, sent more than seven months after the complaint was filed
  - Given the information available to Erie, the letter was untimely and the court ordered Erie to defend and indemnify Ms. Lobenthal
  - Erie's reservation of rights letter to an additional insured was ineffective where the letter was untimely and was not addressed to the additional insured herself, but rather to her parents (the named insureds) and her attorney
  - Erie was required to defend and indemnify the additional insured

Breach of Duty to Defend – Revisited

***K2 Investment Group, LLC v. American Guarantee & Liability*,**
6 N.E.3d 1117, 983 N.Y.S.2d 761 (Feb.18, 2014)

K2 Investment Group, LLC v. American Guarantee & Liability,
6 N.E.3d 1117, 983 N.Y.S.2d 761 (Feb.18, 2014)

- Facts
  - Insurer wrongfully refused to defend insured
  - Insured's assignee argued that insurer could not rely on policy defenses to defeat liability for default judgment against insured
- Holding
  - In first K2 case, we held that insurer who breached duty to defend may not assert defenses to indemnity
  - First K2 case conflicted with another decision, *Servidone Constr. Corp. v. Security Ins. Co. of Hartford*, 64 N.Y.2d 419, 488 N.Y.S.2d 139, 477 N.E.2d 441 (1985)

K2 Investment Group, LLC v. American Guarantee & Liability, 6 N.E.3d 1117, 983 N.Y.S.2d 761 (Feb.18, 2014)

- Holding
  - The court followed *Servidone*
  - Insurer allowed to assert policy defenses and summary judgment against insurer reversed based on the existence of a question of fact as to whether policy exclusion applied
  - NC law: Insurer who breaches duty to defend is estopped to deny coverage
  - Majority rule: follows *Servidone*

COVERAGE COUNSEL AS DEPONENT

***Everest Indemnity Co. v. QBE*, 980 F.Supp.2d 1273 (W.D.Wash. 2013)**

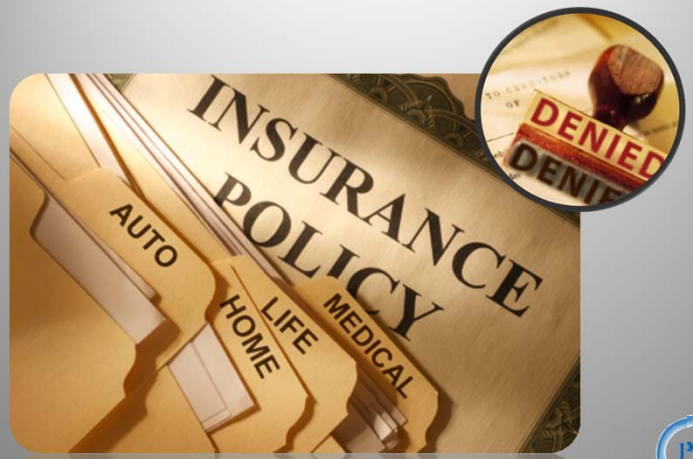
Everest Indemnity Co. v. QBE, 980 F.Supp.2d 1273 (W.D.Wash. 2013)

- Facts
  - Insured sued for property damage at a condo project and tendered defense to QBE/CAU
  - After QBE/CAU rejected defense, Everest Indemnity assumed defense and, as assignee, brought bad faith action against QBE/CAU
  - Everest noticed deposition of QBE/CAU's coverage counsel
  - Complaint alleged that insurer failed to do any investigation on its own – which court found "troubling"

Everest Indemnity Co. v. QBE, 980 F.Supp.2d 1273 (W.D.Wash. 2013)

- Holding
  - "Should Everest's assumptions prove true," QBE/CAU's "delegation of all investigative and claims handling responsibilities to [the coverage attorney]would have the effect of shielding relevant bad faith evidence from discovery since no other QBE/CAU employee would have knowledge about QBE/CAU's basis for the denial of [the] tender"
  - Motion for protective order denied
  - However, if, during deposition the coverage attorney in "good faith" believes that a question seeks to elicit "privileged information," the attorney may make "proper objection"

BAD FAITH



INSURER CAN BE LIABLE FOR NEGLIGENCE IN CLAIM HANDLING

***Bruno v. Erie Ins. Co.*, 106 A.3d 48 (Pa. Dec. 2014)**

Bruno v. Erie Ins. Co., 106 A.3d 48 (Pa. Dec. 2014)

- Facts
  - The Brunos bought a home in 2007 and obtained a homeowners' policy from Erie
  - The policy covered physical loss to the property caused by "fungi," included in a separate endorsement
  - Pursuant to the endorsement, Erie would be required to pay the Brunos up to $5,000 for a direct physical loss caused by mold
  - When the Brunos found black mold in their basement, they contacted Erie
  - Erie sent Rudick Forensic Engineering to investigate the mold problem
  - Rudick said the mold was harmless
  - The claim was not paid

Bruno v. Erie Ins. Co., 106 A.3d 48 (Pa. Dec. 2014)

- Facts
  - The Brunos stayed in the house and found more mold growing on leaking pipes
  - They told Erie, who tested it, but did not disclose the results of the tests
  - The Bruno family suffered severe respiratory ailments
  - By January 2008, the Brunos decided to have the mold tested on their own
  - They discovered that the mold was toxic and hazardous to their health
  - They again asked Erie for the full mold benefit, and Erie made the $5,000 payment to the Brunos

Bruno v. Erie Ins. Co., 106 A.3d 48 (Pa. Dec. 2014)

- Facts
  - The Brunos were forced to demolish their house
  - The wife, Angela Bruno, developed esophageal cancer as a result of exposure to the toxic mold
  - The Brunos filed a breach of contract and bad faith action that also included a negligence claim against Erie for its actions during the claim handling process, and the actions of its agent, Rudick
  - Erie filed preliminary objections as to the negligence claim based on the gist of the action doctrine
  - The trial court sustained the preliminary objections, and the intermediate appellate court affirmed

Bruno v. Erie Ins. Co., 106 A.3d 48 (Pa. Dec. 2014)

- Holding
  - Reversed
  - "If the facts of a particular claim establish that the duty breached is one created by the parties by the terms of the contract (i.e., a specific promise to do something that a party would not ordinarily have been obligated to do, but for the existence of the contract), then the claim is to be viewed as one for breach of contract"

    – gist of the action applies
  - "if, however, the facts establish that the claim involves the defendant's violation of a broader social duty owed to all individuals which is imposed by the law of torts and, hence, exists regardless of the contract, then it must be regarded as a tort"

    – gist of the action does ***not*** apply

Bruno v. Erie Ins. Co., 106 A.3d 48 (Pa. Dec. 2014)

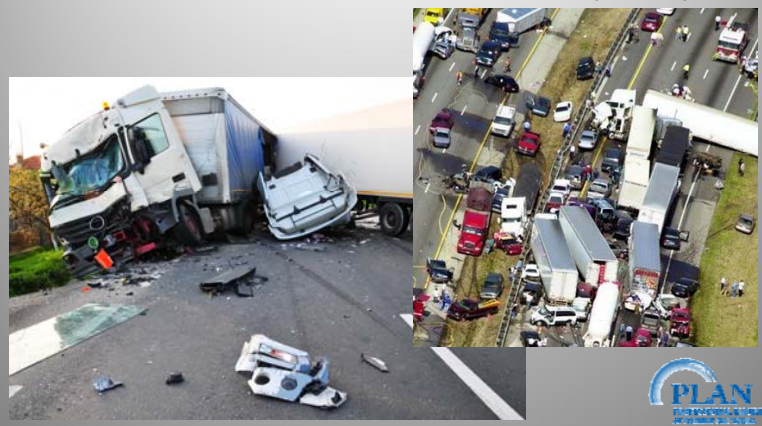
- Holding
  - An insurer can be liable for negligent acts undertaken during the claims handling process:

    "A negligence claim based on the actions of the contracting party in performing contractual obligations is not viewed as an action on the underlying contract itself, since it is not found on the breach of any specific executory promises that comprise the contract

    Instead, the contract is regarded merely as the vehicle or mechanism which established the relationship between the parties during which the tort of negligence was committed."
  - So, while Erie had contractual obligations under its policy to investigate whether mold was present and also pay for all property damage caused by the mold, the substance of the claim is that Erie's agents were negligent "***during the course of fulfilling these obligations***"

EXCESS CAN SUE PRIMARY FOR BAD FAITH FAILURE TO SETTLE

***Scottsdale Insurance v. Addison Insurance*, SC93792 (MO 2014)**



Scottsdale Insurance v. Addison Insurance, SC93792 (MO 2014)

- Facts
  - The family of a motorist killed in a 2007 accident with a truck operated by Wells Trucking stated a claim against Wells Trucking
  - The state police investigation determined that the Wells Trucking driver was at fault
  - Wells Trucking's primary carrier ($1 million policy) was United Fire (Addison Ins. Co.)
  - Wells Trucking formally demanded that United Fire settle the case within the limits
  - There was evidence that the suit could have been settled within the primary limits
  - United Fire made several offers that Wells Trucking would later characterize as "low and unreasonable"

Scottsdale Insurance v. Addison Insurance, SC93792 (MO 2014)

- Facts
  - The family grew frustrated and filed a wrongful death suit
  - The excess carrier, Scottsdale, was put on notice
  - Scottsdale demanded that United Fire attempt to settle within the primary limits "while it still had the opportunity to do so"
  - Shortly thereafter, the family made another demand of $1 million
  - United Fire rejected that demand and the family raised their demand to $3 million
  - The case resolved at mediation for $2 million; $1 million from United Fire, and $1 million from Scottsdale

Scottsdale Insurance v. Addison Insurance, SC93792 (MO 2014)

- Facts
  - Wells Trucking assigned its rights to Scottsdale, and Scottsdale filed a bad faith action against United Fire
  - The trial court granted United Fire's motion for summary judgment:

> "an excess insurer cannot recover from a primary insurer under a claim of bad faith refusal to settle and that bad faith refusal to settle could not be proven because United Fire settled the claim against Wells Trucking and paid its policy limits and Wells Trucking did not suffer an excess judgment."

Scottsdale Insurance v. Addison Insurance, SC93792 (MO 2014)

- Holding
  - On appeal, the Supreme Court of Missouri reversed holding that "an insurer's ultimate settlement for its policy limits does not negate the insurer's earlier bad faith refusal to settle and that an excess judgment is not essential to a bad faith refusal to settle action."
  - The excess carrier can establish a bad faith claim where the primary

    (1) Reserves the exclusive right to contest or settle any claim;

    (2) Prohibits the insured from voluntarily assuming any liability or settling any claims without consent; and

    (3) Is guilty of fraud or bad faith in refusing to settle a claim within the limits of the policy

QUESTIONS?