COVERAGE OPINIONS

Judicial Opinions Today - Impact On Counsel's Opinions Tomorrow

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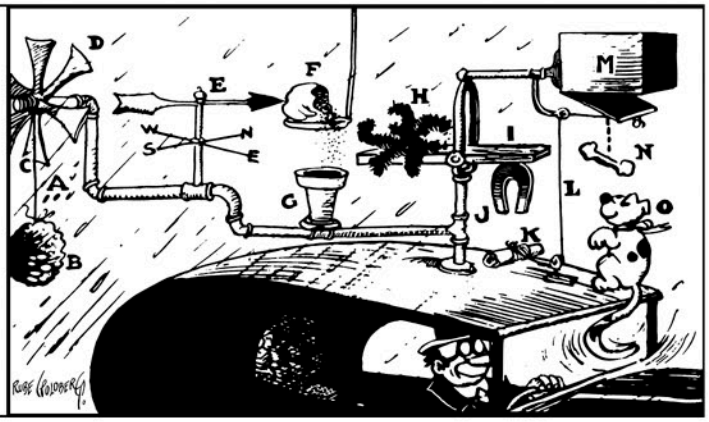
The Cover-age Story

Rube Goldberg's design for a new windshield wiper. Weight of rain (A) in sponge (B) causes string (C) to spin fan (D). Breeze from fan swings weather vane (E) which upsets bag of seeds (F) into flower pot (G). As seeds grow and bloom, caterpillars (H) spin cocoons which naturally become butterflies and fly to flowers, thereby allowing weight of board (I) to lower magnet (J), which attracts iron bar (K) causing string (L) to open box (M). Soup Bone (N) drops in front of Zozzle Hound (O). He wags tail for joy, wiping Rain from windshield. The big problem is to get the butterflies to hatch before the rain stops. Ask the king of Spain about this. He has plenty of time to figure it out.



Eastern District Of Pennsylvania Demonstrates The Many Moving Parts Of Insurance Coverage

Malicious Prosecution Can Never Be Excluded As A "Knowing Violation" Of Rights

It only seems right that the cover story of the inaugural issue of a newsletter, devoted to reporting on insurance coverage decisions, should demonstrate just how complex the subject matter can be. After all, if it were not complex, you would have no need to read a newsletter to keep you abreast of anything. You could just hit delete now and move on to your next e-mail -- from the Nigerian prince that kindly needs your help getting his family's fortune out of the country.

But insurance coverage is complex. Of course, to the uninitiated, this may seem hard to believe. After all, just about every case asks the same question – Is it covered? And there are only two possible answers – yes or no. Easy Peasy. Like a hot knife through butter. Yep, that's what insurance coverage is. No doubt securities law doesn't work like that. But if you are reading this then you know better. Just as Churchill described Russia in 1939, the real story is that insurance coverage can be a riddle wrapped in a mystery inside an enigma. Not buyin' it?

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Declarations: The *Coverage Opinions* Interview with Jerry Oshinsky

Coverage Opinions checks in with Jerry Oshinsky of Jenner and Block's Los Angeles office to see what's on the mind of "the foremost practitioner at the policyholder Bar" in 2012, according to Chambers USA and one of Law360's "10 Most Admired Attorneys" in 2010. Page 12

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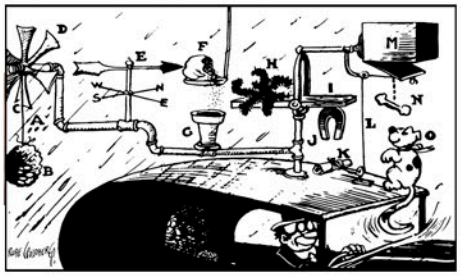

Then take a look at the Eastern District of Pennsylvania's decision in *Regent Insurance Company v. Strausser Enterprises, Inc.* (unpublished). The court was called up to address the potential applicability of the "Knowing Violation" exclusion to an otherwise covered claim for malicious prosecution under Part B of a commercial general liability policy. This was a single-issue coverage case – about a 3 on a scale of 1 to 10 for complexity. But even for something so pedestrian, consider what it took for the court to get from A to B.

At issue in *Strausser* was potential coverage for Strausser Enterprises for an underlying malicious prosecution claim filed against it. The underlying dispute, giving rise to the claim, was complex. Fortunately, those facts can be brushed aside here for purposes of addressing the coverage issues in this format.

Examining the insurer's potential duty to defend and indemnify, the *Strausser* Court quickly concluded that malicious prosecution is expressly included within the scope of coverage B as a "personal and advertising injury." *Strausser* at 18.

The more time consuming question was whether coverage was then precluded by the policy's 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.'" ("'Knowing Violation' exclusion"). *Id*. at 27.

The court began with an explanation of the applicable legal standard that would govern its duty to defend determination. Essentially, if the complaint avers facts that might support recovery under the policy, the insurer has a duty to defend. *Id*. at 14. But duty to defend is just half the story. The insurer's duty to indemnify only arises if the damages are actually (i.e., not just might be) covered by the policy. *Id*. at 16. Lastly, of course, is the standard for interpreting an insurance policy. In general, if the court concludes that the policy is ambiguous, it must interpret it in the manner most favorable to the insured. *Id*. at 15.

With these ground rules in place, the *Strausser* Court got down to the business of determining whether the Knowing Violation exclusion precluded coverage for Strausser for the malicious prosecution claim.

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About The Editor

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Randy J. Maniloff is an attorney in the Philadelphia office of White and Williams, LLP. He concentrates his practice in the representation of insurers in coverage disputes over primary and excess obligations under a host of policies. Randy is the co-author of "General Liability Insurance Coverage: Key Issues In Every State" (Oxford University Press, 2nd Edition, 2012). For the past eleven years Randy has published a year-end article that addresses the ten most significant insurance coverage decisions of the year completed. Randy has been quoted on insurance coverage topics by such media as The Wall Street Journal, The New York Times, USA Today, Dow Jones Newswires and Associated Press. For more biographical information visit www.whiteandwilliams.com. Contact Randy at Maniloff@coverageopinions.info or (215) 864-6311.

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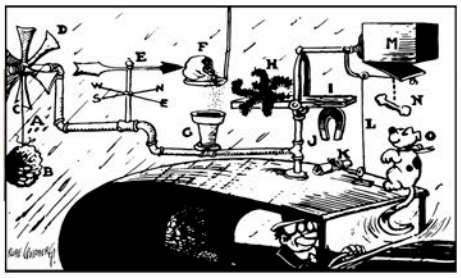
The Cover-age Story



Notwithstanding that, under Pennsylvania law, the insurer's obligation to defend is determined solely by the allegations in the complaint and the terms of the policy, the court was unable to limit its analysis to simply those two documents. Rather, to address the potential applicability of the Knowing Violation exclusion, to the malicious prosecution claim, the court first had to turn to the Pennsylvania statute that defines malicious prosecution (known in Pennsylvania as wrongful use of civil proceedings or the so-called Dragonetti Act). This revealed that, in relevant part, a person is liable for wrongful use of civil proceedings if, when taking part in a civil proceeding, he "acts in a grossly negligent manner or without probable cause." *Id.* at 21 (citing 42 P.S. 8351(a)).

So the issue became whether one's acting in a grossly negligent manner or without probable cause, as required by the Pennsylvania statute for malicious prosecution, qualified as knowledge that the act would violate the rights of another, as required to trigger the Knowing Violation exclusion under the policy.

The Pennsylvania statute did not answer that question. So the *Strausser* Court was next required to turn for guidance to Pennsylvania case law interpreting the statute. And that offered no simple answer. After plowing through the case law, focusing on whether malice is an element of malicious prosecution, the court concluded that it is relatively well-settled that proof of an improper motive is necessary to prevail in a malicious prosecution claim. *Id.* at 25.

Having determined that proof of an improper motive is necessary to prevail on a malicious prosecution claim, the *Strausser* Court concluded that all malicious prosecution claims under Pennsylvania law would fall within the Knowing Violation exclusion. "In sum, if malicious prosecution under Pennsylvania's Dragonetti Act (the wrongful use of civil proceedings statute) is an intentional tort, then Coverage B is a Catch–22: "Regent promises to cover the Strausser defendants for claims of malicious prosecution so long as no exclusion applies to bar coverage, but the 'Knowing Violation' exclusion always applies to malicious prosecution under the Dragonetti Act." *Id.* at 28. This conclusion caused the court to declare the policy ambiguous. Having done so, it concluded that a defense was owed, as well as indemnity, for the malicious prosecution claim.

The *Strausser* Court also had an alternative basis for concluding that the Knowing Violation exclusion did not apply.

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I-name Observations About Insurance Companies

There are a lot of property-casualty insurance companies – nearly 2,700 according to the Insurance Information Institute's last count. While they all have one thing in common -- accepting risks in exchange for premium, they differ a lot in name. A review of a list of United States P&C companies reveals a wide-ranging thought process in how they've chosen to be identified.

Some companies take the bland approach – Accident Insurance Co. On the other end of the spectrum is Lightening Rod Mutual Insurance Company. Nothing bland about those guys. Other companies choose names so you have no doubt where they are located. No problem finding San Antonio Reinsurance Company. Others, like Alamo Title Insurance, tell you where you can find them, but you just need to think about it for a second. Lots of insurance compa nies seem to like the name Farmers. I'm sure there isn't too much confusion between those 60 or so companies.

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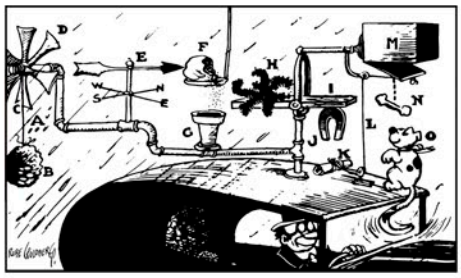

The court observed that, given that an alternative interpretation of the Dragonetti Act could apply, one where only gross negligence needed to be proven, then the Knowing Violation exclusion would not apply. *Id*. at 30.

While *Strausser* does not even begin to scratch the surface of the complexity of insurance coverage, it does demonstrate the point that when it comes to coverage, simple questions can produce far from quick and simple answers. After all, the *Strausser* Court weighed in with a 39 page opinion to resolve a straightforward case, based on a test that called for nothing more than a comparison of the complaint to 32 words of the insurance policy. What's more, given that the court's decision was so heavily tied to Pennsylvania's treatment of malicious prosecution, all bets are off whether a claim in a state that does not begin with the letter P would reach the same conclusion.

Regent Insurance Company v. Strausser Enterprises, Inc., No. 09-3434 (E.D. Pa. Sept. 27, 2012) is available at the Eastern District of Pennsylvania's website.

Emotion For Summary Judgment: 9th Circuit Addresses Whether Anxiety Is "Bodily Injury"

The question whether emotional injury is "bodily injury," for purposes of a commercial general liability, or other type of liability policy, is more complex than it may seem. The vast majority of courts that have addressed the issue, under a policy that defines "bodily injury" as "bodily injury (or bodily harm), sickness or disease," have determined that it does not. A common rationale for this conclusion is that the term "bodily" suggests something physical and corporeal. A notable exception to the majority rule is the New York Court of Appeals, which held in *Lavanant v. Gen. Accident Ins. Co. of Am.* (N.Y. 1992) that emotional injury does qualify as "bodily injury." And if the New York rule can make it there it can make it anywhere. Possible adoption of the New York rule is currently before the Supreme Court of Pennsylvania in *Lipsky v. State Farm.*

But while a substantial majority of courts have concluded that emotional injury does not qualify as "bodily injury," many of those same courts have also held that emotional injury, that is accompanied by physical manifestation, qualifies as "bodily injury."

In *Conley v. First National Insurance Company,* the Ninth Circuit (unpublished) addressed the parameters of coverage under Montana law for emotional injury.

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Some insurers want to leave no doubt about what they insure. Guess what kind of insurance The Dentists Insurance Company sells. I wonder if Balboa Insurance Company and Lewis & Clark LTC RRG, Inc. ever get together and share exploring tips. There are insurance companies that want you to know that they are strong. Don't even think about messing with Olympus Insurance Company. The nation's oldest insurance company might just also have the longest name – Philadelphia Contributionship for the Insurance of Houses from Loss by Fire, Inc. Some insurer's names are just fun to say, like Pymatuning Mutual. And some insurers choose names that make you scratch your head… Elephant Auto Insurance Company. I guess they sell their policies for peanuts.

That's my time.

I'm Randy Spencer.

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Emotion For Summary Judgment: - *Continued*

On one hand, Montana offers no surprises on this issue. As the Montana Supreme Court made clear not too long ago in *Wagner-Ellsworth* (Mont. 2008), "bodily injury" includes "mental or psychological injury that is accompanied by physical manifestation." In other words, Montana follows the majority rule nationally on the issue.

At issue in *Conley* was whether a defense was owed on the basis that an allegation of "anxiety" qualified as "bodily injury" because, unlike emotional distress or mental anguish, anxiety is commonly understood to include physical manifestation. It was also argued that a defense was owed based on a letter sent to the insurers that stated: "[T]he dread of tax liability that the Conleys face [has] taken a serious toll on their health."

The Ninth Circuit affirmed the decision of the District Court, which held that "the Conleys' letter 'fails to make even a generalized reference to physical injury,' and that it was reasonable to read 'a serious toll on their health' in context with the rest of the paragraph, which discussed only the 'emotional cost' of [someone's] bad advice.'"

While Montana law required the insurers to consider the information contained in the letter, for purposes of determining their duty to defend, the insurers did not have to affirmatively disprove a bodily injury where none was alleged. Thus, the insurers did not have to undertake an investigation that would have allegedly revealed extreme weight loss and chronic diarrhea. While *Conley* certainly addresses an important question when it comes to whether emotional injury qualifies as "bodily injury," it also provides guidance on the duty to defend.

Conley v. First National Insurance Company, No. 11-35577 (9th Cir. Sept. 27, 2012) is available at the Ninth Circuit's website.

South Carolina Federal Court: Looking South Of The Border, Of The Complaint, To Determine Duty To Defend

In numerous states (although perhaps fewer than you might think), the determination of an insurer's duty to defend is made by the application of a simple formula: compare the allegations in the complaint with the terms of the policy. If the result is the possibility of coverage – the insurer is obligated to defend. If there is no possibility of coverage then the insurer has no duty to defend. This is of course the "four corners" rule (or "eight corners" rule as some states call it) and the simplest to apply of all the duty to defend tests that courts around the country have developed. [Riddle – Why does Texas call it the "eight corners" rule when almost all states use the term "four corners" to say the same thing? Because everything is bigger in Texas.]

But in some states that apply the "four corners" rule it is necessary for courts to consider what the complaint's allegations *mean* and not just what they say. You see, the straight-jacketed nature of the "four corners" rule gives rise to an opportunity for plaintiffs to take advantage of it, by artfully pleading allegations in their complaint for the sole purpose of trigging a defense for the defendant. In other words, if the insurer is going to be constrained by the four corners of the complaint, to determine if it has a duty to defend,

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Coverage Opinions is a bi-weekly (or more frequently) electronic newsletter reporting and providing commentary on just-issued decisions from courts nationally addressing insurance coverage disputes. Coverage Opinions focuses on decisions that concern numerous issues under commercial general liability and professional liability insurance policies. For more information visit www.coverageopinions.info.

South Carolina Federal Court: - *Continued*

then an underlying plaintiff – who is likely familiar with the basic terms and conditions of a CGL policy -- can draft the complaint to say what is needed to trigger a defense. Needless to say, plaintiffs prefer for their defendants to have insurance that may have an obligation to pay.

Wanting to avoid this situation, some courts are unwilling to apply the "four corners" rule in such a rote manner. Instead, they "look beyond" the precise allegations of the complaint – which may have been pleaded in the manner that it was simply for purposes of triggering a defense -- and make their duty to defend determination based on a realistic review of the nature of the claims at issue. In other words, to these courts, the specifically stated allegations in the complaint will not control when they belie reality.

This is what a South Carolina District Court did in *MCE Automotive, Inc. v. National Casualty Company* (unpublished). At issue in *MCE Automotive* was the potential availability of coverage for *MCE*, for an underlying complaint that alleged that it sold to an 82 year old woman -- a vulnerable adult -- thirteen cars in less than a two year period.
There were various types of insurance policies at issue. The general issue before the court was whether a defense was owed on the basis that the complaint alleged conduct that was accidental in nature. The *MCE Automotive* Court concluded that it did not. The court reached this conclusion despite there being allegations of negligence in the complaint, and despite the complaint being the only document that the court was supposed to look to for purposes of determining whether the allegations triggered a defense.

The *MCE Automotive* Court explained its decision as follows:

"While the complaint does state a cause of action for negligence, the court is to look beyond the label of negligence and determine if National Casualty had a duty to defend. . . . Looking at the factual allegations in the Underlying Complaint, Plaintiff alleges MCE sold 82–year old Kaufman, a vulnerable adult, thirteen cars between July 2, 2007, and March 9, 2009. Plaintiff also alleges MCE knowingly and willfully exploited Kaufman and that MCE's actions included preying upon vulnerable adult consumers. These factual allegations are specifically incorporated into the negligence cause of action alleged in the Underlying Complaint. The factual allegations alleged in the Underlying Complaint constitute intentional and deliberate acts with an alleged purpose of preying upon a vulnerable adult and they cannot be construed as accidental in nature."

MCE Automotive at 8. "MCE (sic) contention that the Underlying Complaint asserts causes of action for both intentional torts and negligence through the use of the phrase should have known is without merit because, in the context of a cause of action alleging an intentional tort, which by definition cannot be committed in a negligent manner, the allegation of negligence is surplusage." *Id*. at 8-9 (citation and internal quotes omitted).

The moral of the story for insurers in simple – press for courts to not use rote application of the "four corners" rule to create an unjustified duty to defend. Explain to the court that it will still be making its duty to defend determination based solely on the allegations within the four corners of the complaint. It's just that the allegations in the complaint are being viewed through a lens of common sense.
MCE Automotive, Inc. v. National Casualty Company, No. 6-11-1245 (D.S.C. Sept. 28, 2012) is available on the PACER system.

Opinion-aided: Michigan Federal Court Addresses Policyholder's Ability To Get Its Hands On Outside Coverage Counsel's Opinion Letter

While the insurer prevailed before the Eastern District of Michigan in *Barton Malow Company v. Certain Underwriters at Lloyd's of London* (unpublished), the win was not without a price – an opinion that should cause some concern for insurers when it comes to maintaining, as privileged, coverage opinions secured from outside counsel.

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Opinion-aided: - *Continued*

Barton Malow Company was involved in litigation with Lloyd's of London over coverage for an arbitration award arising out of the company's role as a construction manager for a University of Michigan project. Barton Malow sought to obtain certain unredacted reports prepared by a law firm that was hired by Lloyd's as coverage counsel before the litigation. Barton Malow maintained that the redacted reports were neither privileged nor subject to the work product doctrine. At the court's urging, Lloyd's produced to Barton Malow redacted portions of five reports prepared by its coverage counsel. After then producing the reports in unredacted form – again at the court's urging – Barton Malow sought to have three of the passages, that Lloyd's wanted to keep redacted, be declared non-privileged and not subject to the work product doctrine. *Barton Malow* at 1-2.

The *Barton Malow* Court set out the following test for determining if communications by attorneys, in the insurance claims process, are subject to attorney-client privilege: "The communication itself must be primarily or predominantly of a legal character. The payment or rejection of claims is a part of the regular business of an insurance company. Consequently, reports which aid it in the process of deciding which of the two indicated actions to pursue are made in the regular course of its business. Merely because such an investigation was undertaken by attorneys will not cloak the reports and communications with privilege because the reports, although prepared by attorneys, are prepared as part of the regular business of the insurance company." *Id*. at 3-4 (citation and internal quotes omitted).

Despite setting out a seemingly broad test, for allowing communications by attorneys, in the insurance claims process, to be outside the scope of attorney-client privilege, the *Barton Malow* Court held that the specific communications at issue were protected by attorney-client privilege: "A review of the selected passages shows that the communications were not the work of an attorney performing a function that was part of the regular course of Underwriter's insurance business. Importantly, the passages must be read in the context of the entire report, including the text appearing before and after the selected passages. In so doing, it is clear that the passages communicate legal advice from Underwriter's counsel regarding the extent, if any, to which Barton Malow's claim was covered. They show counsel's legal opinions regarding the scope of potential liability." *Id*. at 4.

The lesson from the *Barton Malow* Court is that, under its test, it is possible that the entirety of a coverage opinion from outside counsel may not be privileged. A concern for insurers in this regard should be the lack of guidance that the court provided in determining what's privileged and what's not. On one hand, the court stated that, because the payment or rejection of claims is part of the regular business of an insurance company, "reports which aid it in the process of deciding which of the two indicated actions to pursue are made in the regular course of business" and are not privileged.

On the other hand, the court concluded that the specific passages at issue were protected by privilege because it was clear that they communicated legal advice regarding the extent, if any, to which the claim was covered.

On its face, and without any detailed guidance from the court, it can be imagined that the test for what qualifies as a report which aided the insurer in the process of deciding which of the two indicated actions to pursue, and a report that communicated legal advice, regarding the extent, if any, to which the claim was covered, is not a bright line. One take-away from the decision seems to be that insurers that employ outside coverage counsel should insist that counsel provide legal analysis to support its opinion. Sometimes insurers simply seek a more cursory opinion from counsel, which could be argued is non-privileged, as a report which aided the insurer in the process of deciding which of the two indicated actions to pursue.

Barton Malow Company v. Certain Underwriters at Lloyd's of London Subscribing to Policy No. 509/QF004706, No. 10-10681 (E.D. Mich. Oct. 3, 2012) is available on the PACER system.

Lost Cause: Nevada Federal Court: Primary Insurer Unable To Establish That "Cause" Test Leads To A Single Occurrence

Three Bells For Excess Insurer In Construction Defect Claim

Most disputes under general liability policies center around the fundamental question whether an insurer is obligated to defend and/or indemnify its insured for certain "bodily injury" or "property damage." But, in some cases, after it is determined that indemnity is owed, a dispute ensues over the extent of the insurer's obligation. In particular, a significant issue bearing on the amount of the insurer's obligation may be the number of "occurrences" that caused the covered "bodily injury" or "property damage."

In general, courts nationally have adopted two approaches for determining number of occurrences. Under the "effect" test, number of occurrences is determined by examining the effect that an event had, i.e., how many individual claims or injuries resulted from it. Conversely, under the "cause" test, number of occurrences is determined by examining the cause or causes of the damage. The "cause" test is the majority rule nationwide.

A court's adoption of the "cause" test frequently leads to a single "occurrence" determination -- on the basis that, despite multiple injuries or damaged properties, they all have a common cause. That the "cause" test frequently leads to a single "occurrence" determination, despite multiple injuries or damaged properties, is also tied to the fact that the definition of "occurrence" in many policies includes "continuous or repeated exposure to substantially the same general harmful conditions," or some language to that effect.

But not all decisions that apply the "cause" test reach the conclusion that the injuries or damages, for which coverage is being sought, were caused by a single occurrence. Case in point is the *District of Nevada's lesson in Insurance Company of the State of Pennsylvania v. National Fire & Marine Insurance Company* (unpublished). *National Fire* also demonstrates the tension that can sometimes exist between primary and excess insurers when it comes to the question of number of occurrences. They do not always see the issue the same.

In *National Fire*, the court addressed coverage for Riverwalk Development, a builder, for damages arising from a condominium conversion construction project. A primary commercial general liability policy at issue provided coverage for $1 million per occurrence and $2 million general aggregate. An excess policy was only obligated to provide coverage after the primary policy had paid the full amount of its limit. The excess insurer argued that the damages alleged against Riverwalk Development involved multiple occurrences, thereby requiring the primary policy to pay its $2 million general aggregate, and not simply a single $1 million occurrence limit, before the excess insurer was obligated to contribute to any settlement. *National Fire* at 1-2.

In addressing the issue, the Nevada District Court was quick to note that "Nevada, like the majority of jurisdictions, employs the 'cause' test to determine what constitutes an occurrence within the meaning of a 'per occurrence' clause in an insurance policy." *Id*. at 7 (citations omitted).

But despite the fact that Nevada is a "cause" test state, which often leads to a single occurrence determination, the *National Fire* Court concluded that the evidence before it could not support a determination that all of the damage emanated from one common cause. The court stated: "These expert reports identify various independent defects in the structural components and electrical and plumbing systems, all of which independently caused damages. For instance, the architectural consultant identifies various defects in the roof of the Project leading to water intrusion resulting in damages to the substrates and building interiors. The electrical consultant identifies various faulty electrical installations and code violations, such as exposed wires, all of which resulted in safety hazards. The plumbing consultant identifies various defects including faulty installation of toilets, bathtubs, and showers; improper washing

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Lost Cause: - *Continued*

machine, dishwasher, and refrigerator hook-ups; and defects in the common area swimming pool's draining pipe." *Id*. at 8.

While it can be convenient to use labels, and resulting generalizations, when addressing certain coverage issues, they offer no certainties in their predictiveness. That's the general take-away from *National Fire*. More specifically, given that CD claims sometimes involve an excess policy over a primary policy with a $1 million occurrence limit and a $2 million aggregate limit, the decision can be a basis for tension between the primary and excess insurers when it comes to possible settlement.

Insurance Company of the State of Pennsylvania v. National Fire & Marine Insurance Company, No. 11-2033 (D. Nev. Sept. 26, 2012) is available on the PACER system.

Wisconsin Appeals Court: "Expected Or Intended" Property Damage Based On Insured's Expectations At The Time Of The Conduct Causing The Damage

Most "expected or intended" coverage cases involve "bodily injury." And the circumstances surrounding such cases are not surprising – fights in various contexts and sexual assaults make up a lot of them. But there are situations where the question is whether property damage was "expected or intended" by the insured. One involves long-ago releases of hazardous substances that allegedly caused damage to the environment.

Unlike an insured that cold-cocks someone in a bar fight, where the question whether the "bodily injury" was "expected or intended" can be somewhat apparent, the issue can be more opaque in the context of environmental property damage.

In *NCR Corporation v. Transport Insurance Company* (recommended for publication), the Wisconsin Court of Appeals addressed whether an umbrella policy, on the risk in 1983-1984, provided coverage to NCR Corporation for its liability for PCB contamination of the Lower Fox River in Wisconsin. Specifically, the issue was whether NCR expected or intended the damage. If it did, coverage would not be available.

The underlying facts that gave rise to the coverage question are that "NCR's paper mills manufactured carbonless copy paper using an emulsion coating that contained PCBs, specifically Aroclor 1242. NCR last used PCBs and released them into the Fox River in May 1971. However, NCR sold PCB-containing paper waste to other mills on the river for several years thereafter, knowing that their recycling processes would release additional PCBs into the river." *NCR* at 16.

The coverage issue arose on account of the policy's definition of "occurrence:" "an accident or event including continuous repeated exposure to conditions, which results, during the policy period, in personal injury or property damage neither expected nor intended from the standpoint of the insured." *Id*. at 13.

As an initial matter, the *NCR* Court held that the insured's expectations must be evaluated at the time of the conduct causing the damage. The court rejected the insurer's argument that the insured's expectation of damage is evaluated up through the time of policy inception. *Id*. at 13-15

The *NCR* Court then reviewed the world's historic knowledge of concerns caused by PCBs, including the first study on the subject, published in Sweden in 1966. This was followed by an examination of, among other things, other studies, the historic use of PCBs in commercial products, the existence (or not) of state or federal laws addressing the use of PCBs, the timing of the adoption of effluent limits for PCBs, and what an NCR research manager knew by 1969 about the environmental effects of PCBs. *Id.* at 16-18.

Following the *NCR* Court's review of this information, it held that it could not conclude, as a matter of law, that NCR intended or expected with substantial certainty that its PCB releases would cause environmental harm: "Considering the early focus on effluent limits, one could conclude that in the early 1970s the scientific community did not believe

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Wisconsin Appeals Court: - *Continued*

that all PCB discharges were harmful to the environment. The record does not indicate the amount of PCBs NCR was introducing into the Fox River. Further, there were, at the very least, unanswered questions concerning the potential effects of differing types of PCBs. Yet, there was mounting evidence that PCBs were harmful and, at some point, NCR clearly would have known or expected that releases of Aroclor 1242 would cause environmental harm. Some of this evidence was known or available while NCR was still using the product. Therefore, it is appropriate for a jury to determine what NCR actually knew or expected and when it gained that knowledge or expectation." Id. at 18-19 (emphasis in original).

NCR Corporation v. Transport Insurance Company, No. 2011AP192, (Wisc. Ct. App. Sept. 25, 2012) is available on the Wisconsin Court of Appeals website.

Illinois Federal Court Allows Excess Insurer To Sue Primary Insurer's Selected Defense Counsel For Malpractice

On one hand, the Southern District of Illinois's decision in *ACE American Insurance Company v. Sandberg, Phoenix & Von Gontard, P.C.* (unpublished) does not involve a "coverage" issue, in the usual sense of that term. On the other hand, it clearly involves claims handling and the amount of an insurer's liability for a covered claim. For these reasons, and because the decision addresses an issue that is not drowning in judicial guidance – and reaches a conclusion that is contrary to some of the few cases that do exist – it warranted a spot in *Coverage Opinions.*

At issue before the Illinois federal court was whether an excess insurer can sue its insured's defense counsel, who had been retained by the primary insurer, alleging that, because counsel mishandled the defense, it resulted in an unnecessarily large settlement, that increased the excess insurer's liability.

It is not entirely surprising that a situation like this would arise. In general, defense counsel is chosen by the primary insurer. Unlike the primary insurer, who may have a long-standing panel relationship with defense counsel, the excess insurer may not know defense counsel from Adam. Given this lack of a personal relationship, and that counsel was hired by the primary insurer, the excess insurer may not be getting the same frequency of status reports as the primary insurer. Likewise, the excess insurer may not be as involved in the case's day-to-day activities as the primary insurer. In addition to reporting deficiencies, defense counsel also may be painting too rosy of a picture of the insured's potential to avoid liability or significant damages. Defense counsel may not be making the excess insurer aware of of the true potential for an unfavorable outcome. Because of this, the excess insurer may not be monitoring the case as closely as it otherwise would, if the case were on its radar as one having a chance of impacting its policy.

For all these reasons, a higher than expected verdict or pre-trial settlement demand may come as more of a surprise to the excess insurer than the primary insurer. And, insurance companies do not like surprises. What's more, if defense counsel commits malpractice, or fails to accurately report on the problems in a case, it may be a "no harm, no foul" situation for the primary insurer. After all, the claim may have exhausted the primary policy's limits no matter what defense counsel did. Therefore, the consequences of defense counsel malpractice, overly optimistic reporting or deficient reporting, can be much greater for the excess insurer than the primary insurer.

Yet, despite being more affected by the malpractice, it would appear, on its face, that the excess insurer has a harder road to travel if it wishes to sue defense counsel, since it was probably the primary insurer that hired counsel. In other words, the excess insurer has no privity with defense counsel. That is certainly the rationale used by some courts to preclude excess insurers from bringing malpractice actions against defense counsel.

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Illinois Federal Court

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The Southern District of Illinois held in *ACE American Insurance Company v. Sandberg, Phoenix & Von Gontard, P.C.* (unpublished) that ACE and Federal Insurance Company could maintain a legal malpractice action against the law firm retained by their insured's primary insurer to defend a products liability suit. The suit "culminated in a settlement right after the trial court judge (1) determined that defense counsel deliberately had failed to disclose responsive documents in discovery and (2) issued a sanctions order finding flagrant violations by defendants and striking their pleadings. The sanctions order established liability and left [the insured] with the choice of proceeding to trial on damages or settling the case." *Sandberg, Phoenix & Von Gontard* at 3. Federal and ACE alleged that this increased the potential verdict of any damages-only trial, drove up the value of the case and resulted in a negotiated settlement of a substantial amount. *Id*. at 4.

Following a lengthy choice of law analysis (Illinois versus Missouri. Illinois won.) the *Sandberg, Phoenix & Von Gontard* Court turned to a review of case law nationally, as well as from other Illinois federal courts, that has addressed whether an excess insurer can bring a legal malpractice action, based on equitable subrogation, against defense counsel retained by the primary insurer.

Acknowledging that there are valid arguments and legitimate policy considerations on both sides, the court held that the Illinois Supreme Court would allow such an action to be maintained. *Id*. at 17.

Some of the rationales for the court's decision were as follows: There are exceptions to the general rule that legal malpractice actions are not assignable. *Id.* at 16. As it is the excess insurer that bears the cost of the verdict, and not the insured, it is equitable and just to allow an excess insurer to recoup its losses by way of equitable subrogation. *Id.* at 18. "Unlike assignment, subrogation would not lead to the merchandising of malpractice claims. Though a claim can be assigned to anyone willing to pay for it, subrogation rights can be exercised only by those who have fulfilled a duty, imposed by contract or law, to pay for another's loss. Thus, allowing subrogation of legal malpractice claims would not make them a commodity available to the highest bidder." *Id*. To not allow subrogation would be tantamount to declaring that the defense counsel could never owe a duty to the excess insurer. *Id.* at 20. Allowing such actions would not declare open season on defense attorneys or be detrimental to the legal profession as insurers in general, and especially excess insurers, rarely bring legal malpractice claims against attorneys (for several reasons set out by the court). *Id.*

ACE American Insurance Company v. Sandberg, Phoenix & Von Gontard, P.C., No. 12-0242 (S.D. Ill. Oct. 2, 2012) is available on the Southern District of Illinois website.

Declarations:

The *Coverage Opinions* Interview With Jerry Oshinsky

For the first issue, *Coverage Opinions* checks in with Jerry Oshinsky of Jenner and Block's Los Angeles office to see what's on the mind of "the foremost practitioner at the policyholder Bar" in 2012, according to Chambers USA and one of Law360's "10 Most Admired Attorneys" in 2010. It makes sense for Jerry to be the inaugural *Coverage Opinions* interviewee. After all, he was one of the architects behind *Keene Corp. v. Insurance Company of North America* (D.C. Cir. 1981), the inaugural case that adopted the continuous trigger – a coverage doctrine that significantly altered how courts, policyholders and insurers approached claims for asbestos and other toxic torts as well as hazardous waste. The continuous trigger has also led to an overall change in thinking about claims – with the question being asked, in a variety of other claims scenarios, whether the doctrine has applicability on the basis that "bodily injury" or "property damage" was potentially taking place during more than one policy period.

Tell me about your background?

I grew up on the East Coast. My father and mother both are from families of eight brothers and sisters. As far as I know, I was the first member of the extended family to graduate from a 4-year college or law school.

After graduating from Columbia Law School, I was an associate at Chadbourne Parke in New York City. I was a general commercial litigator. Chadbourne partner Gene Anderson left to form his own firm and by 1972, a number of Chadbourne lawyers, including me, joined him. One major client was Keene Corp. We had all sorts of cases. For example, I tried a case for Keene before the Armed Services Board of Contract Appeals in Alexandria, VA. Keene had acquired a former asbestos products manufacturer and, by 1978, had become embroiled in numerous asbestos cases. Early insurers denied coverage, arguing that manifestations of injury occurred after their policy periods. Later insurers denied coverage, arguing that the exposure to asbestos occurred before their policy periods.

At Columbia Law School, I had a number of world-renowned professors; Telford Taylor –Chief Prosecutor at Nuremberg; Louis Henkin – International Law; William Cary – SEC Chairman under President Kennedy; Willis Reese – Author of the Restatement of Conflicts; Hans Smit – Civil Procedure Scholar; Jack Weinstein – later an E.D.N.Y. Judge. I really enjoyed my time with all of these interesting notables.

Jerry Oshinsky

Your policyholder coverage practice is no secret. What have been some other aspects of your practice?

As a young lawyer, I represented Don McLean in a royalty dispute with his record company; Janie Blalock, a very prominent golfer who had been accused falsely of cheating on the LPGA tour; and I handled the litigation that ultimately resulted in the disbarment of Roy Cohn. In Tony Kushner's Angels in America, the case that the Roy Cohn character is trying to fix is my case.

I also devoted much of my early years to the company that was then North American Aviation (now Rockwell), including investigating the fire that killed three astronauts in 1966, and the dispute over the rights to the contract to build the engines for the space shuttle which we litigated before the General Accounting Office and the Comptroller General of the United States. I still have the bound volume from that case. I wrote the first drafts of most of our briefs.

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Declarations: - *Continued*

I suppose if I had stayed at Chadbourne, I would have been a securities and government contracts litigator.

What's keeping you busy these days?

Pursuing coverage for Penn State University for Jerry Sandusky claims; seven arbitrations in which I am a Party Appointed Arbitrator; coverage for an antitrust case against Santa Barbara Cottage Hospital; Numerous D&O coverage matters; Duke University; Tyson Co. - coverage for property damage litigation brought by the Attorney General of Oklahoma; Entertainment law coverage matters including a case for the rock band Tool, and a case brought against my clients by Dwayne "the Bounty Hunter" Chapman.

You've been at this for a long time. How has the practice of insurance law changed over the years?

At first, coverage was viewed as a unique specialty. Now, every law firm has a practice. This can lead to all sorts of odd results. The insurers usually have their main law firm. Policyholders often forget that they need someone who really knows the landscape and often hire their general litigator who is not an expert in the field.

Keene was decided over 30 years ago. Did you ever imagine that the continuous trigger would have the impact that it did on asbestos and hazardous waste claims, not to mention change how some other types of liability claims are approached?

Keene decided three major issues. First, the court decided that the policies covered injury during the policy period, and that all policies from a claimant's first exposure to asbestos through manifestation of injury were triggered. Second, the policyholder was authorized to decide which triggered year should pay for each loss and no part of any loss would be allocated to uninsured years. Finally, the Court placed the burden of proof on the insurance companies to prove that injury did not occur during their policy years. Thus, *Keene* presumed the happening of bodily injury from exposure through manifestation in asbestos bodily injury cases.

We and others soon realized the general applicability of *Keene*. Indeed, when the insurance industry drafted the standard form policy language in issue, they used environmental cases in their deliberations when deciding that injury or damage during the policy period would be the trigger of coverage. These principles were later applied in environmental property damage cases, product liability cases, discrimination and other workplace cases, and indeed in any case where the allegations involve a span of years from the first act giving rise to liability until the discovery of the alleged injury or harm. *Keene* can be viewed as the Magna Carta of insurance coverage litigation in this country.

At the time we viewed *Keene* as just another litigation for an important client. We did not promote or market in those days. But soon after *Keene*, asbestos and environmental defendants wanted to hire me to pursue coverage. Among others, our many new clients included Independent Petrochemical Co., National Gypsum, Abex Corp., Olin Corp., W.R. Grace, McKesson, Celotex, Hercules, Monsanto, North American Phillips and many others. I had moved to Fairfax, VA in 1979 and opened my then law firm's office in Washington, D.C. and we were off to the races.

You're originally an East Coast guy. What are some differences between practicing there and in California?

In New York, I knew practically everyone that I dealt with on my side and the other side. California is so vast that we often deal with many different lawyers on many cases. Also, in California, judges often decide cases with a written "Tentative" Opinion before Oral Argument. The "Tentative" almost always is the final decision. That is a unique feature of California Practice.

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Declarations: - *Continued*

What do you enjoy doing when you are not reading insurance policies?

Books on History. Also, novels usually legal – Rumpole of the Bailey has always been my favorite. Sadly, Rumpole's creator, John Mortimer is gone. I also have read every novel by Louis Auchincloss. I am also an actor and a producer and director of plays. I have performed in Twelve Angry Men (Juror No. 7), The Man Who Came to Dinner , Frost/Nixon, Inherit The Wind, The Persians, The Exonerated, Spoon River Anthology and many others. I recently produced, directed and also performed one of the monologues in "The Vagina Monologues."

L.A. is famous for its congested freeways. What do you listen to during those long traffic jams?

Lady Gaga and Sirius Rock 'N Roll from the 1950s

If someone were in L.A. for just one night, what restaurant should they not miss?

CAPO or NOBU

Late-r Notice:
A Look At Decisions To Come

In *Ryan v. National Union Fire Insurance Company*, the Second Circuit Court of Appeals certified the following questions to the Supreme Court of Connecticut: (1) Does Connecticut law permit a policyholder to recover consequential damages in a breach of contract action against an insurer predicated on the insurer's breach of its duty to defend? (2) If consequential damages are available, may such damages include damages for harm to reputation and loss of income?

While an insurer may be obligated to reimburse more than simply defense costs when a breach of the duty to defend was committed in bad faith, *Ryan* involves a situation with no bad faith component. Since the vast majority of breaches of the duty to defend are not committed in bad faith, *Ryan* could increase insurers' exposure in more duty to defend cases – at least where the appropriate damages can be established by the insured.

Ryan v. National Union Fire Insurance Company, 10-4528 (2nd Cir. Aug. 27, 2012) is available at the Second Circuit website.