MM Insurance Law News
2018: The Year In Review

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In a year so full of turmoil, controversy and man-made and natural disasters, where should we start in picking the most consequential legislative, regulatory and legal developments of 2018 that will impact the insurance industry in 2019 and for years to come? Here, for better or worse, are your editor's choices:

I. Most Interesting Insurance Coverage Trends

- Emerging consensus among federal appellate courts finding "computer fraud" coverage for cyber-losses from "spoofing" and other types of social engineering fraud.
- Growing willingness of courts to find coverage for "innocent" insureds.
- Will the "unavailability" extends to pro rata allocation extend beyond New Jersey>
- If an insurer fails to defend, are its obligated capped by the policy limit?

II. External Developments

- Electoral developments and retirements led to the appointment of new state insurance commissioners in Michigan, New Hampshire, Tennessee and Wisconsin.
- American Law Institute approves Restatement of Law, Liability Insurance.
- Governor Jerry Brown signs California Consumer Privacy Act.
- Missouri enacts HB 1531 creating interpleader protection for liability insurers.
- Ohio enacts infrastructure legislation "disapproving" the ALI Restatement.
- South Carolina and Ohio enact NAIC's model data security act protect the data and confidential information of policyholders.

III. Changes In the Insurance Industry

2018 saw unprecedented turnover in the senior leadership positions at Lloyd's even as the London Market struggles to cope with Brexit-generated uncertainty; U.S. P/C companies suffering from a never-ending soft market were buffered by cat losses from wildfires in California and other severe weather events; QBE North America sold its personal lines business to Liberty Mutual; AXA SA swallowed up XL Group; 2019 will see new state insurance commissioners in Michigan, New Hampshire, Tennessee and Wisconsin; AIA and PCIAA announced plans to merge and insurers continued to grapple with how to successfully underwrite emerging markets for cyber-claims; autonomous vehicles and marijuana.

IV. The Most Significant Insurance Coverage Rulings of 2018

1. California Insurers Must Defend Negligent Supervision Claims

In a startling and disturbing ruling, the California Supreme Court declared in Liberty Surplus Ins. Co. v. Ledesma & Meyer Construction Co., 418 P.3d 400 (Cal. 2018) that allegations that an employer was negligent in its hiring, training and supervision of an employee who sexually assaulted a third party required a defense under a CGL policy. On a certified question from the Ninth Circuit, the Supreme Court held that such claims constitute an "occurrence" because he insured did not intend for the injury to occur. The court emphasized that the tort of negligent supervision relied on independent acts of negligence and did not rest on theories of vicarious liability for the employee's intentional acts. The court concluded that "[a]bsent an applicable exclusion, employers may legitimately expect coverage for such claims under comprehensive general liability insurance policies, just as they do for other claims of negligence." Justice Liu added a concurring opinion, questioning whether some of the cases cited by the majority were reliable authority in light of the attenuated relationship between the insured's acts and the resulting injuries.

2. New York's High Court Rejects "Unavailability" Allocation Exception

Notwithstanding concerns that its ruling in Viking Pump might reflect second thoughts with respect to the advisability of pro rata allocation, the New York Court of Appeals has reaffirmed the conclusion that it earlier adopted in Consolidated Edison that pro rata allocation is required in the absence of express policy provisions to the contrary. Further, the court ruled in KeySpan - East Corp v. Munich Re No. 20, 2018 WL 1472635 (N.Y. Mar 27, 2018) that there is no "unavailability" exception exempting periods of time when insured's allegedly could not purchase insurance coverage for environmental liabilities. The Court of Appeals declared that the cases recognizing an "unavailability" exception have generally done so on public policy grounds, whereas its adoption of pro rata allocation in Consolidated Edison was based on policy provisions limiting coverage to loss occurring "during the policy period."

3. New Jersey Rejects Equitable Exception to "Unavailability"

The New Jersey Supreme Court has ruled that allocation issues arising out of asbestos bodily injury claims must be interpreted in accordance with New Jersey law and therefore preclude any allocation of "unavailable" years of coverage to the insured. Notwithstanding the fact that the named insured under these policies had been headquartered in Michigan at the time of issuance, the court declared in Continental Ins. Co. v. Honeywell International, Inc., 2018 WL 3130638 (N.J. June 27, 2018) that New Jersey had the more significant interest in this dispute in light of the various Section 188 Restatement factors that it found controlling years ago in Pfizer. Furthermore, the court rejected arguments by Travelers that it should recognize an equitable exception to the "unavailability doctrine" in cases where corporations continued to manufacture and

distribute dangerous products even after insurance became unavailable owing to the known risks associated with such operations and products. Judge Albin dissented from this latter aspect of the court's ruling, declaring that the majority's ruling gives insureds a "free pass" to market known dangerous products and still obtain insurance coverage for any resulting liabilities.

4. Wisconsin Supreme Court Rejects Coverage for Negligent Supervision

In contrast to Ledesma, a sharply-divided Wisconsin Supreme Court ruled in Talley v. Mustafa, 911 N.W.2d 55 (Wis. 2018) that a CGL policy does not cover allegations of negligent supervision when a negligent supervision claim rests solely on an employee's intentional act of assault and battery without any separate basis for a negligence claim against the employer, no coverage exists. In reversing the decision of the Court of Appeals, the majority found that coverage could not be based upon the employer's failure to tell his employees not to punch employees in the face and that coverage would only arise in such cases if the employer's own acts were found to have accidentally caused the plaintiff's injuries. Writing in dissent, Justice Bradley (joined by Justices Abrahamson and Kelly) argued that the majority had erred in not considering the meaning of "accidental" from the standpoint of the employer and that the majority had improperly that coverage would not apply because no jury would award damages on the theory that an employer had a duty to instruct employees not to punch customers. Justice Kelly filed a separate dissent, echoing Justice Bradley and insinuating that the majority had seized this case as an excuse to eliminate coverage for negligent supervision claims.

5. Second Circuit Opens Reinsurer Obligations Beyond Stated Limits

In 2018, the Second Circuit issued a significant reinsurance opinion expanding upon the New York Court of Appeals recent ruling in Global Re v. Century Ind. Co., 30 N.Y. 3d 508 (2017) while also opening new doors with respect to potential problems for cedents seeking recovery from their reinsurers. In Utica Mutual Ins. Co. v. Clearwater Insurance Company, No. 16-2535 (2nd Cir. Sept. 25, 2018), the Court of Appeals ruled that a New York District Court erred in ruling that Clearwater's maximum obligation under various facultative certificates was the stated liability limit of $5 million. As with Global Re, the Second Circuit pointed out that the certificates contained "follow the form" language that obliged the reinsurer to reimburse the cedent for indemnity payments as well as expenses paid by Utica in its handling and defense of the underlying asbestos claims even to the extent that the result required a payment in excess of $5 million. The Second Circuit was not persuaded by Utica's argument that it should defer to the amounts that it had paid pursuant to settlements with Gould Pumps, moreover, and declared that the District Court would need to make further findings with respect to the extent to which these payments were covered. Significantly, the Second Circuit also rejected the District Court's conclusion that the amount of the Goulds Pumps' settlement that Utica had allocated to Clearwater was reasonable or that a "follow the settlements" obligation could be inferred in this case. Even though the certificates stated that Clearwater "shall follow the ceding

Company's liability in accordance with the terms and conditions of the policy," the Second Circuit declined to read this language as setting forth a "follow the settlements" obligation. Finally, the court ruled that Utica Mutual had violated the terms of the facultative certificate by failing to obtain the reinsurer's consent before entering into these settlements notwithstanding Utica's claim that it should be relieved of any such obligation pursuant to the doctrine of "impossibility." The court declared that, "Even if Utica had shown that obtaining TPF&C's authorization was impossible and thus excused, Utica also needed to establish that Clearwater's performance was also not excused by reason of the unrealized condition – the authorization for settlement." As a result, the court ruled that Clearwater was not obligated to follow Utica's settlements with Gould's Pumps but rather must indemnify Utica according to Utica's proven liability on the umbrella policies. The case was herefore remanded to the District Court for further proceedings wherein Utica would have the burden of proving that the loss was specifically caused by a risk covered by these facultative certificates.

6. $54 Million California Bad Faith Verdict Reversed

A $54 million bad faith verdict against AIG was set aside due to errors by the trial judge in allowing the insured to interrogate a company representative with respect to discovery responses that she had verified, the judge's own "intensive questioning" of the witness, and judge's mishandling of the representative's subsequent invocation of the Fifth Amendment privilege after the judge made a preliminary finding that she had perjured herself in her earlier testimony. In a 54 page opinion, the First District ruled in Victaulic Co. v. American Home Assur. Co., 20 Cal. App. 5th 958 (1st Dist. 2018) that it was error to interrogate the witness concerning responses to Requests for Admission that she had merely verified and had not herself personally prepared as that the denial of a request for admission is not evidence that is admissible at trial. The Court of Appeal also criticized the trial judge for his active intervention in the examination of the witness and his pointed comments with respect to claimed inconsistencies in her testimony as to whether the "potential for coverage" was determined differently in claims handling as opposed to coverage litigation. While acknowledging the right of the trial judge to ask questions during the course of a trial, the Court of Appeal ruled that in this case the trial judge had openly mocked the witness and acted as an advocate on behalf of the policyholder plaintiff.

7. South Carolina Supreme Court Allows Suits against Defense Counsel

South Carolina has joined the growing number of states that permit liability insurers to sue appointed defense counsel for malpractice. On certified questions from a U.S. District Court, the state Supreme Court ruled in Sentry Select Ins. Co. v. Maybank Law Firm, LLC, 2018 WL 2429364 (S.C. May 30, 2018) that even though the insurer was not a client of the firm, it could pursue an action based on defense counsel's breach of his duties to the insured client. The Maybank Law Firm had argued that allowing a direct right of action would destroy the sanctity and integrity of the attorney client relationship by: (1) dividing

the loyalty of the attorney between the client and the insurer; (2) threatening the attorney- client privilege; (3) allowing the insurer to direct the litigation even though the insured is the client; and (4) opening the door to other non-clients to sue attorneys for legal malpractice. The Supreme Court acknowledged these concerns and cautioned insurers not to place an attorney in a conflict between his client's interests and the interests of the insurer. The court declared the insurer may recover only for the attorney's breach of his duty to his client, when the insurer proves the breach is the proximate cause of damages to the insurer. "If the interests of the client are the slightest bit inconsistent with the insurer's interests, there can be no liability of the attorney to the insurer, for we will not permit the attorney's duty to the client to be affected by the interests of the insurance company. Whether there is any inconsistency between the client's and the insurer's interests in the circumstances of an individual case is a question of law to be answered by the trial court." Chief Justice Beatty dissented, arguing that South Carolina should not allow insurers to bring such actions or pursue assignments of legal malpractice claims.

8. Federal Courts of Appeal Find Coverage for Cyber-"Spoofing" Claims

In Medidata Solutions, Inc. v. Federal Ins. Co., 2018 WL 3339245 (2d Cir. July 6, 2018), the Second Circuit summarily affirmed a New York District Court's ruling that the victim of a cyber "spoofing" attack was entitled to coverage for its loss under a Computer Fraud policy. In a brief opinion, the Second Circuit declared that actual hacking was not required to trigger coverage so long as a third party had fraudulent inserted of data into the insured's computer system. In this case, the Court of Appeals declared that the spoofing attack quite clearly amounted to a "violation of the integrity of the computer system through deceitful and dishonest access" since the fraudsters were able to alter the appearance of their emails so as to falsely indicate that the emails were sent by a high-ranking member of the company. The court also rejected Federal's argument a "direct loss" had not resulted from a covered. While acknowledging that Medidata employees themselves had to take action in order to cause the transfer and resulting loss of funds, the court concluded that "we do not see their actions as sufficient to sever the causal relationship between the spoofing attack and the losses incurred."

In keeping with Medidata, the Sixth Circuit ruled a week later that a Michigan manufacturer was entitled to coverage for $834,000.00 that was stolen from it by a fraudster that masqueraded as its vendor in China. In American Tooling Center, Inc. v. Travelers Cas. and Sur. Co. of America, 2018 WL 3404708 (6th Cir. July 13, 2018), the Sixth Circuit ruled that this was a "direct physical loss" as ATC "immediately lost its money when it transferred the approximately $834,000.00 to the impersonator; there was no intervening event." On the issue of whether this theft constituted "computer fraud", the Sixth Circuit contrasted the facts in this case to Pestmaster Services, in which the Ninth Circuit had ruled in favor of Travelers on this issue in a case where the fraudulent conduct occurred without the use of a computer. The Sixth Circuit declared that in this case the

impersonator had sent ATC fraudulent emails using a computer and that these emails fraudulently caused the insured to transfer the funds to a third-party account. The Court of Appeals declared that if Travelers had intended to limit the scope of its "computer fraud" coverage to situations in which a third party gains access to or actually hacks into the insured's computer, it should have drafted the operative policy language more narrowly.

9. Texas Supreme Court "Clarifies" Bad Faith Damages

A full year after the Texas Supreme Court issued a confusing and controversial opinion analyzing the extent to which a policy holder may recover damages based upon an insurer's violation of the Texas Insurance Code in a case where the jury separately found that the insurer did not owe coverage for the insured's first party loss, the Supreme Court has issued a series of new and conflicting opinions on rehearing. In the principal 66 page opinion for the majority, Justice Boyd declared in USAA Texas Lloyds Co. v. Menchaca, No. 14-0721 (Tex. April 13, 2018) that the court was standing by the five rules that it adopted in 2017 in Menchacha I. Despite a bewildering welter of conflicting concurrent an dissenting opinions, the court remanded the case for a new trial consistent with these new rules for recovery.

10. Bad Faith Law Gets Worse In Florida

A narrowly divided Supreme Court of Florida has further expanded the scope of bad faith in the Sunshine State. In Harvey v. GEICO General Insurance Company, 2108 WL 4496566 (Fla. Sept. 20, 2018), a majority of the justices ruled that the Fourth District Court of Appeal had misapplied cases such as Boston Old Colony and Berges in setting aside a bad faith verdict against a liability insurer for allowing an excess verdict to enter against the policyholder. The majority found that the Fourth District had erred in finding that an insurer cannot be liable for bad faith where the excess judgment was due in part to the insured's own action or inaction. Further, the court declared that the fiduciary obligation that it had identified in Berges required insurers to be proactive and to initiate settlement negotiations in cases where the insured's liability was clear and injuries were so serious that a judgment in excess of policy limits was likely. The majority criticized decisions of the Eleventh Circuit and other federal courts that have taken a more lenient view of the obligation of insurers to protect the interests of the policy holders. The majority declared that GEICO had not fulfilled its obligations in this case. Even though it had tendered its $100,000.00 policy limit only 9 days after the accident, the court found that the insurer's obligations did not end when it tendered its limits where, as here, the claimants had demanded a financial accounting of the insured's assets not provided in a timely fashion. Accordingly, the Supreme Court declined to excuse GEICO's conduct in this case even though it was the insured whose inaction and delay had caused the settlement to fail. It ruled that, "[a]n insured's actions cannot let the insurer off the hook when the evidence clearly establishes that the insurer acted in bad faith in handling the insured's claim." Three of the seven justices joined two separate dissents that variously argued that the

insured's conduct is irrelevant in assessing a bad faith failure to settle. The dissenters contended majority's analysis "muddies the waters between negligence and bad faith" and will bolster "contrived bad faith claims." Justice Polston separately dissented and said the court lacked jurisdiction since the Fourth District's case did not directly conflict with the court's prior precedents.

11. Massachusetts Court Finds Coverage for "Advertising Idea"

The Supreme Judicial Court of Massachusetts ruled in Holyoke Mut. Ins. Co. v. Vibram USA, Inc., 480 Mass. 480 (2018) that a running shoe manufacturer's use of the name of a famed African barefoot marathon runner alleged the use of "another's advertising idea" so as to trigger a duty to defend under Coverage B. Whereas the insurers argued that the family's suit against Vibram only involved a claim for a right of publicity and did not involve an "advertising idea" because the name "Bikila" did not contain any "secondary meaning" associated with the advertised product, the Supreme Judicial Court ruled that "advertising idea" is a broad term that encompasses "a wide variety of concepts, methods and activities related to calling the public's attention to a business, product or service." Having found that the insurers had a duty to defend, the SJC did not reach the other issue that had been briefed to the court, namely whether the insurers were entitled to recoup defense costs they had paid up to the time that the court ruled that they did not have a duty to defend.

12. Illinois Court Caps Damages from Failure to Defend At Policy Limit

In an important new opinion clarifying the impact of estoppel in Illinois, the Seventh Circuit ruled in Hyland v. Liberty Mutual Fire Ins. Co., 2018 WL 1324593 (7th Cir. Mar. 15, 2018) that Liberty Mutual's failure to either defend its insured or to bring a declaratory judgment action estopped it from disputing its indemnity duty after it was found to have owed a defense. Nevertheless, the court ruled that the insurer's obligations were capped by its $25,000 policy limit rather he $4.6 million default judgment that entered against its insured. Judge Easterbrook declined to find that Liberty Mutual's failure to defend could have caused any injury beyond what the policy provided for, as there was no evidence that a vigorous defense would have defeated the plaintiff's personal injury claim or diminished the damages to which he was entitled.

13. English High Court Relaxes Standard for Reinsurance Arbitrators

The Court of Appeal has reversed the High Court's conclusion that language in a reinsurance arbitration clause requiring that appointed arbitrators have at least "ten years' experience of insurance or reinsurance" could only be satisfied by employment in the insurance industry itself. Instead, the Court of Appeal ruled in Allianz Insurance PLC & Ors v Tonicstar, Ltd., EWCA Civ 434 (2018) that a Queen's Counsel who specialized in insurance work and had represented insurers and reinsurers for more than a decade was qualified to serve as an arbitrator.

14. New York Court of Appeals Restrict Additional Insured's Rights

A divided New York Court of Appeals ruled in Gilbane Building Co. v. St. Paul Fire & Marine Ins. Co., 97 N.E.3d 711 (N.Y. 2018) that language in CGL policies extending additional insured coverage "where required by written contract" only applied where the contract was between the named insured and the putative additional insured. Two justices dissented, arguing that the language in question was ambiguous and that the majority was contorting the provision in question to undermine an important device that the construction industry had develop to transfer loss.

15. Illinois Court Finds Bad Faith in Traveler's Failure to Settle Pollution Claim

Despite the fact that Travelers paid for the insured's independent counsel to defend a pollution case, the Illinois Appellate Court ruled that it was estopped to contest its indemnity obligations and had acted in bad faith in failed to settle. Even though Travelers had paid for the insured's defense through independent counsel while its declaratory judgment action proceeded, the Fifth District ruled in Rogers Cartage Co. v. Travelers Ind. Co., 2018 WL 1661799 (Ill App. April 5, 2018) that Travelers' refusal to make a further settlement offer after the underlying claimants asserted that they would not consider any further reduction in their demand was, in fact, an effort to intimidate its insured and put a stop to settlement negotiations. The Appellate Court found that although Travelers had initially allowed Peppers counsel to control the defense, as the date of trial approached it, in effect, took over the defense by refusing to allow its insured to settle at a crucial time during negotiations. Notwithstanding its conclusion that Travelers was therefore estopped from contesting its duty to pay the $7.5 million settlement that its insured negotiated over Travelers' objections, the Fifth District further found that Travelers' pollution exclusion defense would have been to no avail because the insured had placed chemical wastes into so-called containment ponds and had not expected or intended that they would be released into the environment. The court also rejected Travelers' argument that the $7.5 million settlement was unreasonable or the product of collusion despite evidence that the insured had never informed Travelers that it would have settled for a $4 million cash payment from Travelers. Finally, the Appellate Court found that Travelers had acted vexatiously and in bad faith in refusing to settle and in threatening its insured by filing this action for declaratory relief. The court also sustained the lower court's award of $2.6 million for the insured's coverage fees, even though the $7.5 million agreement stipulated that any recovery would reimburse the insured's fees in full before any remaining amount was disbursed to third parties.

16. Wisconsin Court of Appeals Rejects Excess "Drop Down"

One of the longest running environmental coverage disputes in the country took an unexpected turn last year when the Wisconsin Court of Appeals ruled that excess insurers should have dropped down and accepted the defense of claims that were covered by underlying policies but which the underlying insurers had declined to defend.

Notwithstanding general language to this effect in the Supreme Court's 2010 Johnson Controls opinion, District I of the Court of Appeals declared in Johnson Controls, Inc. v. Central Nat. Ins. Co. of Omaha, 2018 WL 1957131 (Wis. App. April 25, 2018) that this general rule could not countermand specific language in the Central National policies declaring that a duty to defend only arose if a loss was covered that was not covered by the primary policy. In such circumstances, the court declared that "no reasonable insured would expect the Central National policy language to establish a duty upon Central National to drop down and provide a defense in the event the primary insurer refused to do so where it is undisputed the primary and excess policies provided identical coverage for the claimed loss."

17. "Knock Off" Claims Trigger Coverage B Under New York Law

The Second Circuit ruled in High Point Design, LLC v. LM Ins. Corp., 2018 WL 6625763 (2d Cir. Dec. 19, 2018) that allegations that the insured infringed a competitor's design patent by "offering" knock-off goods for sale triggered a duty to defend under Coverage B. In rejecting Liberty Mutual's argument that such claims solely sought recovery for trade dress infringement, the Court of Appeals ruled that "offering for sale" could be construed as a form of advertisement so as to bring the trade dress infringement claims within the exception to Coverage B's exclusion for intellectual property claims. Further, the court found that even if the allegations in the counter-claim against the insurer failed to put LM on notice of an "advertising injury," a duty to defend was triggered by discovery that the insured subsequently received concerting its advertisements for the offending Snoozie slipper products. As a result, the court only required LM to reimburse High Point for costs incurred after the insured provided copies of this discovery to it. In a concurring opinion, Judge Newman disagreed that "offering for sale" connoted an "advertising" injury but agreed that a duty to defend arose from the point in time that discovery against the insured made clear that its product advertising was at issue.

18. Auto Insurer Not Vicariously Liable For Misconduct of Staff Counsel

In one of the few encouraging rulings from Florida this year, the Eleventh Circuit ruled that an auto insurer was not vicariously liable for alleged deficiencies in the defense that staff counsel provided to its insured. Despite the insured's argument that defense counsel's failure to take certain measures caused the underlying case not to settle, the court declared in Kapral v. GEICO Ind. Co., 723 Fed. Appx. 768, 2018 WL 509308 (11th Cir. Jan. 23, 2018) that a liability insurer is not vicariously liable for the negligence of appointed defense counsel that is "competent and qualified." The court declined to draw any distinction between an insurer's liability for the acts of outside counsel and staff counsel in such cases.

19. Asbestos Liabilities Aggregated As One "Occurrence" In Illinois

The Illinois Appellate Court has ruled in United Conveyor Corp. v. Allstate Ins. Co., 2017 IL App. (1st) 162314 (Ill. App. Ct. March 2, 2018) that a product manufacturer's asbestos liabilities resulted from the "single occurrence of continuous manufacturing and selling ash-handling conveyor systems containing asbestos parts." Notwithstanding the insured's effort to distinguish cases such as Nicor and U.S. Gypsum, the court ruled that the same analysis should apply whether the question is a single occurrence for purposes of determining the deductible for which an insured is responsible or the occurrence limit that an insurer must pay.

20. Successive Auto Collisions Deemed One "Occurrence" in Texas

In a dispute between a primary and an excess liability insurer with respect to the number of "accidents" resulting from a chain collision, the Fifth Circuit ruled in Evanston Ins. Co. v. Mid-Continent Cas. Co., 2018 WL 6037507 (5th Cir. Nov. 19, 2018) that the proper application of the "cause" test under Texas law focused on "the events that caused the injuries that give rise to the insured's liability, rather than on the number of injurious effects." Whereas the federal Magistrate had focused on an "immediate cause" of the underlying injuries, the Fifth Circuit declared that it was permissible to look to the "overarching cause" of the several collisions when it was a "proximate, uninterrupted and continuing cause." As there was no evidence in this case that the driver ever regained control of his truck or that his negligence was otherwise interrupted between collisions, the court declared that all of the collisions resulted from the same continuous condition and therefore only triggered a single $1 million "accident" limit in the primary policy.

21. Fifth Circuit Gives Effect to "Criminal Acts" Exclusion in Texas

The Fifth Circuit has ruled that a "criminal acts" exclusion precluded any duty to defend allegations that a restaurant operator plied an 18 year old girl with liquor before sexually assaulting her. Even though the law suit did not specifically describe the insured's conduct as "criminal," the court ruled in Century Surety Co. v. Seidel, No. 17-10026 (5th Cir. June 25, 2018) that this fact was implicit in the Complaint's allegation that she was a minor (serving alcohol to a minor is a Class A misdemeanor in Texas). The court also refused to find ambiguity based on the fact that the policy separately referred to the violation of liquor liability statutes, noting that this language was contained in an exclusion for liquor liability claims and not a grant of coverage.

22. Inebriation of Driver Does Not Affect "Permissive Use" For Auto Coverage

The Missouri Supreme Court ruled in Griffitts v. Old Republic Ins. Co., 550 S.W.3d 474 (Mo. 2018) the issue of whether a vehicle operator was a permissive user under the omnibus clause of Old Republic's policy was not affected by the fact that the operator was drunk at the time of the accident. Old Republic had argued that because the employer's rules precluded drinking and driving, the operator was in violation of these

rules and could not be operating the vehicle with the named insured's authorization or permission. The Supreme Court distinguished between the "operation" and "use" of a covered auto, declaring that Campbell's use (as distinct from his "operation" of the vehicle was within the scope of permission given by the named insured and therefore covered under the omnibus insurance clause.

23. Maine Court Bars Coverage Based On Intent to Injure

The Maine Supreme Judicial Court has ruled that a trial court erred in declining to find that the insured's son had not expected to cause bodily injuries when he assaulted a fellow class-mate, punching him repeatedly. Whereas the trial court had found that the insured had a subjective intent to cause injury but had not anticipated the severity of the injuries suffered, the court declared in Vermont Mut. Ins. Co. v. Ben-Ami, 193 A.3d 187 125 (Me. 2018) that this premeditated assault clearly involved a subjective intent to injure, even if the court refused to agree with Vermont Mutual that an intent to injure should be presumed in cases of this sort. Two justices signed a concurring opinion asserting that the court should have found that an assault of this sort was inherently injurious and not insurable.

24. Colorado Supreme Court Protects Insurer's Privileged Communications

The Colorado Supreme Court ruled in State Farm v. Griggs, 419 P.3d 572 (Colo 2018) that an insurer did not place any privileged communications "at issue" when it submitted an affidavit from its former attorney to rebut allegations of discovery misconduct. The Supreme Court declared that an implied waiver should only be found where a client is asserting a claim or defense that depends on privileged information. In this case, the court found that the attorney's affidavit only set forth facts and did not refer to any claims or defenses nor did it refer to any legal advice that counsel had given to State Farm or, indeed, to any communications between counsel and State Farm. Finally, the court emphasized the fact that State Farm had not offered the affidavit in support of any claim or defense that depended on privileged information or advice of counsel.

25. Sixth Circuit Limits Scope of Liquor Liability Exclusion in Ohio

The U.S. Court of Appeals for the Sixth Circuit has ruled in Mesa Underwriters Specialty Ins. Co. v. Secret's Gentleman's Club, No. 17-3779 (6th Cir. Oct. 16, 2018) that an Ohio District Court did not err in requiring a liability insurer to afford coverage for a judgment against a men's drinking establishment for causing the intoxication of an individual who was soon thereafter involved in a fatal car accident. The court refused to give effect to a liquor liability exclusion in the policy, declaring that the insured's liability was premised on common law negligence and not based upon the selling or furnishing of alcoholic beverages or any other statutory violation of Ohio's dram shop statute. Further, the court ruled that Mesa was collaterally estopped to contest a judgment that a state trial judge had entered following an evidentiary hearing that was conducted after the parties

entered into a consent judgment. The Sixth Circuit emphasized that the consent judgment entered into between the parties had not conceded liability and that a full evidentiary hearing was heard by the state judge. The court rejected Mesa's argument that these findings were not binding since they pertained to the issue of Secret's liability for negligence not the applicability of insurance coverage for the sale of service of alcohol. Further, the court found that because Mesa was in privity with its insured, the requirement of mutuality for estoppel was met.

26. Filing A DJ in Utah Is Not Bad Faith

The Supreme Court of Utah ruled in in Fire Insurance Exchange v. Oltmanns, 2018 UT 10 (Utah Feb. 28, 2018) that the decision of a homeowner's insurer to commence a declaratory judgment action against its insured to clarify the scope of its coverage with respect to an accident involving a water craft was "fairly debatable". In affirming the ruling of lower courts that the insured was not entitled to recovery of its attorney's fees for litigating this coverage action, the Supreme Court rejected the argument of various concurring justices who suggested that a distinction should be drawn between first and third-party insurance claims and that insurers should defend all third-party liability claims that could "conceivably" fall within the scope of coverage.

27. **Delaware Supreme Court Reverses Bad Faith, Disallows Assignment**

The Delaware Supreme Court ruled in Travelers Ind. Co. v. CNH Industrial America, Inc., 2018 WL 3434562 (Del. July 16, 2018) that a trial court erred in applying Wisconsin law to the issue of whether the original insured's rights could be validly assigned to a successor entity without the insurer's consent. The policies in question had been assigned to CNH by the insured's parent corporation (Tenneco) as part of a 1994 corporate reorganization. In light of its 2017 holding in Chemtura that policies insuring risks around the country should be interpreted in accordance with Section 188 of the Restatement (Second), Conflicts of Law with an emphasis on consistency and predictability, the Delaware Supreme Court ruled that Texas law should have applied as being the state with the most significant relationship to the policies, as they had been negotiated and procured through Tenneco's offices in Texas. As Texas law does not permit unconsented-to assignments, the Supreme Court set aside a $17.3 million judgment that the trial court had entered against Travelers for CNH's inherited asbestos liabilities.

28. Delaware Supreme Court Reverses Bad Faith, Disallows Assignment

In a second victory for insurers in Delaware, the Supreme Court ruled in Motors Liquidation Co. DIP Lenders Trust v. Allstate Ins. Co., et al., 2018 WL 3360976 (Del. July 10, 2018) that the successor of General Motors was barred from obtaining excess coverage for legacy asbestos liabilities in light of representations that GM made in an earlier law suit against its primary insurer (Royal). The Supreme Court affirmed a Delaware trial court's finding that the successor entity was judicially estopped from

arguing for an "all sums" allocation of these liabilities based on Delaware law applied or that GM's post-1971 policies applied to these claims in light of contrary assertion that GM had made in earlier litigation against its primary insurer (Royal) in convincing the Delaware court to stay the insured's proceedings in favor of GM's DJ in Michigan. The Delaware Supreme Court noted that GM's counsel had assured the trial court at the time that the post-1971 policies were all written on a "claims made" basis and had further assured the court that it never intended to make a claim under these policies. Additionally, despite the fact that these excess policies contain "occurrence"- based wording, whereas the primary Royal policies were amended after 1971 to provide coverage on a "claims made" basis, the Supreme Court ruled that any inconsistency between these provisions must give way to language in the excess policy stating that they only applied to losses that were also covered by the primary policy.

29. First Circuit Finds Coverage for Bill Cosby Despite Sexual Assault Exclusion

The U.S. Court of Appeals for the First Circuit ruled in AIG Property Cas. Co. v. Cosby, 2018 WL 2730762 (1st Cir. June 7, 2018), that a Massachusetts District Court was correct in ruling that a sexual abuse exclusion in AIG's homeowner's policy did not unambiguously precluded numerous suits by women who claim that Cosby defamed them in denying their allegations of rape and sexual assault. The court did not reach the issue of whether the coverage triggering allegations of sexual assault "arose out of" the original incidents of assault, holding instead merely that the exclusion in AIG's homeowner's policy was ambiguous with respect to such claims because the umbrella policy issued to Cosby had a much more tightly worded sexual assault exclusion in a separate coverage part for "Limited Charitable Trustees and Directors Liability."

30. Georgia Supreme Court Upholds "Other Insurance Wordings

On a certified question from a federal district court, the Georgia Supreme Court ruled in National Cas. Co. v. Georgia School Boards Association, S18Q0757 (Ga. Aug. 14, 2018) that the conventional rules for interpreting conflicting "other insurance" clauses apply even where one clause is contained in a commercial liability insurance policy and the other is set forth in an "inter-local risk management fund." In rejecting the Fund's argument that commercial insurance must always be exhausted before any publicly fund risk management monies are spent, the Supreme Court ruled that the legislature's enactment of OCGA § 20-2-990, requiring public schools to protect themselves from liability exposure by either purchasing conventional liability insurance or pooling their risks through inter-local risk management agreements, did not create any public policy requiring courts to deviate from conventional rules of policy interpretation and that, in fact, creating such an exception would violate the "bedrock public policy of freedom of contract."

31. Seventh Circuit Bars Coverage for Economic Loss from Defective Products

The Seventh Circuit has ruled that a settlement that an insured negotiated to resolve a customer's claim for lost profits due to its inability to sell plastic containers due to a defective component supplied by the insured failed to seek recovery for "property damage" under Indiana law. In Berry Plastics Corp. v. Illinois National Ins. Co., 903 F.3d 630 (7th Cir. 2018), the court observed liability insurance is intended to provide coverage for bodily injury or property damage that is caused by the insured's product after it leaves the manufacturer's hands and are not intended to insure "risk from the disappointed commercial expectations of the manufacturer's customer." Whereas the insured had argued that the lost profits should be deemed to have occurred "because of" the damage to some of the containers because the loss would never have occurred "but for" the failure of those containers, the Seventh Circuit predicted that the Indiana Supreme Court would take a narrower view and declared that coverage did not apply here because the lost profits were not specifically due to property damage but rather resulted from the failure of the insured's foil laminate product "to function as expected and warranted." Having refused to find coverage, the Seventh Circuit also affirmed the lower court's dismissal of the insured's bad faith claim.

32. Illinois Supreme Court Rules That Cause of Action Against Agent for Failure to Procure Proper Insurance Arises At Issuance of Policy, Not When Claim Is Denied

The Illinois Supreme Court has ruled that an insured's cause of action against an insurance agent for selling an insurance policy that did not meet its needs arose when the policy was issued and not, as the insured contended, when the insurer ultimately denied a claim. Overturning the appellate court's ruling that a "discovery rule" should apply under the circumstances, the court ruled in American Family Mutual Ins. Co. v. Krop, 2018 IL 122556 (Ill. Oct 18 2018) that the Illinois legislature had made clear through its 1997 enactment of the Insurance Placement Liability Act made clear that agents (unlike brokers) do not have a fiduciary duty to policyholders. In the absence of any fiduciary duty, the court concluded that the ordinary rules requiring insureds to read policies apply. Justice Theis and Kilbride dissented, arguing that as the insured's claim was one in tort for negligence, it should not accrue until the insured actually suffered an injury at the point in time when its claim was denied by the insurer.

33. Insurer May Not Rely on Post-Denial Evidence to Preclude Bad Faith Recovery

The Colorado Supreme Court has ruled in Schultz v. GEICO Cas. Co., 2018 CO 87 (Colo. Nov. 5, 2018) that GEICO did not have a "fairly debatable" basis for refusing to pay its insured for medical benefits arising out of an auto accident because the medical evidence that GEICO was relying on to raise questions of causation resulted from an independent medical examination that was not performed until 3 years after the accident and 18 months after GEICO's original denial of coverage. The Supreme Court declared that whether an insurer's coverage position was "fairly debatable" can only be based upon the

evidence in existence at the time that the position was adopted. Under the circumstances, the Supreme Court ruled that GEICO's coverage position was not "fairly debatable" and that the trial court abused its discretion in ordering the IME over the objection of claimant's counsel.

34. Tenth Circuit Finds Coverage for Faulty Workmanship Under NY Law

The U.S. Court of Appeals for the Tenth Circuit ruled in Black & Veatch Corp. v. Aspen Ins. Co. (UK), 882 F.3d 952 (10th Cir. 2018) that a subcontractor's negligent installation of emissions scrubbing equipment at a customer's coal- fired power plants triggered CGL coverage under New York law. In an exceptionally long opinion tracing the evolution of the "your work" exclusion in the CGL policy form, the Tenth Circuit reversed a Kansas District Court's entry of summary judgment for Aspen and declared instead that this damage resulted from an "occurrence" and that the insured's own work exclusion did not apply where, as here, the damage resulted from the faulty workmanship of a subcontractor.

35. Tenth Circuit Finds Coverage for Faulty Workmanship Under NY Law

The Third Circuit has adopted the view of several other circuits that courts are under no duty to ferret out the reasonable amount of fees owed in cases where the claimant's fee demand is outrageous. Rather, the court ruled in Clemens v. New York Central Mutual Fire Insurance Company No. 17-3150 (3d Cir. 2018 12 2018), No. 17-3150 (3d Cir. Sept. 12, 2018) that "where a fee shifting statute provides a court discretion to award attorney's fees, such discretion includes the ability to deny a fee request altogether when, under the circumstances, the amount requested is 'outrageously excessive.'" As a result, the Third Circuit tossed out an insured's claim for $900,000 in attorney's fees for a UIM claim for which the jury had only awarded $100,000 in punitive damages under Section 8371. Apart from the disproportionate size of the fee claim, the Court of Appeals took note of the fact that it was not supported by contemporaneous time records and that the description of tasks was remarkably non-specific and vague (e.g. "communicate-other"). The court was also skeptical of counsel's claim that she had spent 562 hours for "trial preparation" with no further description of the nature of the work that the attorney allegedly performed.

V. Where Will Coverage Disputes Come From in 2019?

1. "Me Too": Larry Nassr, Catholic Church, etc.
2. Drones
3. New privacy requirements
4. Data security
5. Marijuana

6. Columbia Gas explosion losses (MA)
7. Crumbling concrete foundations (CT)
8. Wildfires

VI. Insurance Coverage Appeals to Watch In 2019

- **California**: The California Supreme Court is expected to rule in 2019 with respect to the Fourth District's ruling in Travelers Property Casualty Company of America v. Actavis, Inc., 16 Cal. App. 5th 1026 (2017) that a pharmaceutical manufacturer was not entitled to CGL coverage for contributing to America's opioid crisis by over-marketing prescription drugs. The Supreme Court is also expected to rule shortly on a certified question from the Ninth Circuit asking whether "California's common law notice-prejudice rule a fundamental public policy for the purpose of choice- of-law analysis?" At issue in Spitzer College v. Indian Harbor Ins. Co., No. 14-56017 (9th Cir. Jan. 13, 2017) is whether a California District Court, applying New York law, correctly granted summary judgment to an EIL insurer based upon the insured's decision to carry out an environmental cleanup without give notice to or obtaining the insured's consent for the work. The Ninth Circuit has also asked the Supreme Court to decide whether the consent requirement in Indian Harbor's EIL policy is a notice condition subject to a requirement of prejudice to preclude coverage.

- **Connecticut**: The Connecticut Supreme Court will rule later this year with respect to whether the Court of Appeals erred in allowing an "unavailability" exception for long-tail claim allocations. In R.T. Vanderbilt Co. v. Hartford Acc. & Ind. Co., 171 Conn. App. 61 (2017), the Court of Appeals held that the allocation of bodily injury claims arising out of asbestos in the insured's talc products should not include a share for years where insurance was unavailable after 1986. If sustained, this would be the first "time on the risk" state to recognize an "unavailability" exception.

  The Connecticut Supreme Court has also agreed to accept review of numerous legal issues arising out of the first party crumbling foundation claims that have dominated state and federal insurance litigation since 2016, including:

  1. Is "substantial impairment of structural integrity" the applicable standard for "collapse" under the contract of insurance provision at issue?
  2. If the answer to Question One is "Yes," then what constitutes "substantial impairment of structural integrity" for purposes of applying the "collapse" provision of the homeowner's insurance policy at issue?
  3. Under Connecticut law, do the terms "foundation" and/or "retaining wall" in a homeowner's insurance policy unambiguously include basement walls? If not, and if those terms are ambiguous, should extrinsic evidence as to the meaning of "foundation" and/or "retaining wall" be considered?

- **Florida**: The Florida Supreme Court announced on December 27, 2018 that it would address the scope of so-called "assignment of benefits" clauses in homeowner's policy, an issue on which the Fourth and Fifth District Court of Appeals have disagreed.

- **Georgia**: The Georgia Supreme Court agreed in 2018 to review Ruth v. Cherokee Funding LLC, a case that will provide the court with an opportunity to consider whether litigation financing arrangements constitute a "loan" under Georgia state law and are therefore subject to regulation.

- **South Carolina**: The South Carolina Supreme Court has accepted a certified question from the U.S. Court of Appeals for the Fourth Circuit in In Re: Mt. Hawley Ins. Co., No. 18-1401 (4th Cir. June 28, 2018): "Does South Carolina law support application of the "at issue" exception to the attorney-client privilege such that a party may waive the privilege by denying liability in its answer?"