

FDCC REINSURANCE, EXCESS AND SURPLUS LINES SECTION OCTOBER 2011 UPDATE

HOT CASES—HELP NEEDED

I just confirmed that we have hot case duty next week. Please forward any cases of interest to me and I will get them to the correct person to post on the FDCC website.

CALLING ALL APPS!

At the last meeting we learned that the FDCC is rolling out a new smart phone app, which also works on a lap top, that gives you complete conference information wirelessly: www.thefederation.mobi. At the next meeting, come and learn how to use it!

There is a plenary session at the Winter meeting in Arizona that includes the topic: **“There’s An App for That”**.

Learn how your iPad and smart phone can make you a more productive and effective lawyer. The panelists will explain the benefits and capabilities of their favorite legal applications. (If you don’t know what an “application” is, you *really* need to come to this program.) Bring your smart phone or iPad and be prepared to use it!

If you have any favorite app that you would like the panel to know about, please forward to me (for full disclosure: I am on the panel and may beg to use your suggestion).

Upcoming FDCC Events

Insurance Industry Institute

New York Athletic Club, New York, New York - November 16 through 18, 2011

This year’s Insurance Industry Institute, entitled “Addressing Industry-Wide Challenges in Unsettled Times,” will focus on four areas that senior level insurance executives and their counsel will confront in coming years: (a) the changing regulatory landscape; (b) challenges to the protection of privileged information; (c) privacy protection and legal exposures; and (d) the blurring of international borders in insurance claims arising out of claim exposures and natural disasters that cross boundaries.



2012 Winter Meeting at Waldorf Astoria Arizona Biltmore in Phoenix

http://www.thefederation.org/process.cfm?PageID=4&TopLevel=6&calendarDate=2012_03&Day=03&EventID=129

Come out to the ball park! GO RANGERS. Ok I had to throw that in. But, our meeting in Phoenix has a major baseball theme. Register and book your hotel rooms early but do not overbook.

The FDCC is paying a heavy attrition penalty to the conference hotels due to members who block multiple rooms and cancel some at the last minute (or book a full week and then cancel all but a few days).

Section Meeting:

We are co-sponsoring a meeting with the Insurance Coverage, Appellate Law, and the Extra Contractual Sections.

Meeting Topic and Speakers Preview:

Multiple Claimants and Insufficient Limits - Can Insurers Lessen their Exposure to Bad Faith Claims?

When multiple claimants are vying for insufficient policy limits, an insurer's bad faith exposure is magnified. If a settlement of some, but not all, claims exhausts the available policy limits, the insured is exposed to ongoing litigation without defense coverage. If the insurer conditions settlement on resolving all existing and potential claims, the insurer may face bad faith failure to settle claims from the plaintiff(s) unwilling to await a global resolution or dissatisfied with their share of the policy proceeds.

Judicial approaches to this situation vary, with some courts permitting insurers to proceed on a "first come, first serve" basis and others favoring a "first to settle" or "first to judgment" approach. In some jurisdictions, insurers can interplead the policy limits and call upon the court to assist in resolving the competing claims. In other jurisdictions, legislation has been proposed to offer insurers some protection against bad faith claims arising out of the multiple claimants/insufficient limits scenario. Our distinguished panel will explore the real world conundrums insurers face in this situation and share their views regarding effective ways to minimize extra contractual liability exposures.

Moderator: Barbara O'Donnell, Zelle McDonough & Cohen LLP

Speakers:

John Weihmuller, Butler Pappas

Paul Garrison, Corporate Counsel, Infinity Insurance Company

Phillip Priore, McCormick & Priore, P.C.

John Briggs, Claims Counsel, Scottsdale Insurance Company

Miscellaneous

If any of you are interested in reporting new reinsurance cases or any other insurance topic that is relevant to our Section, please let me know. The hot cases are listed on the FDCC website daily, but many times there are no Reinsurance-related cases or issues. I would like to receive information from you to include in an email to Section members to keep everyone apprised of cases that affect us and our practices.

Case Law

Mike Aylward has provided us with the following new case information:

1. Triggering Excess Policies

As discussed in our last issue, there have been a number of recent cases interpreting what constitutes exhaustion of underlying limits in order to trigger an excess insurer's obligations. Of late, these disputes have particularly focused on (1) whether "underlying insurance" means all of the policies in the layer below or just the policy referenced on the excess policy's Schedule of Underlying Insurance and (2) what constitutes exhaustion of those limits.

In a case now pending before the California Supreme Court, the Second District of the California Court of Appeal has ruled that language in ICSOP's umbrella insurance requiring the insured to pay the limit of liability indicated in the schedule of underlying policies "plus the applicable limits of any other underlying insurance collectible by the insured" extended to all primary policies and not just the single primary policy underlying the umbrella policy. While affirming California's "horizontal exhaustion" rule, the Second District held in *Kaiser Cement v. Ins. Co. of the State of Pennsylvania*,

B222310 (Cal. App. June 3, 2011), the Court of Appeal rejected ICSOP's argument that the primary insurer must pay a \$500,000 per occurrence limit for each triggered year. Rather, the court adopted the position of the primary insurer (Truck) and Kaiser that Truck is only responsible to pay policy limits once per occurrence, not once per occurrence per year or once per occurrence per policy. In particular, the court held that there was no requirement that policy limits be stacked. Rather, the court found that Truck's obligation to pay was limited to \$500,000 "per occurrence" not \$500,000 per occurrence per year. The California Supreme Court agreed to accept review but has stayed further action on the case pending its disposition of a related "stacking" issue in the State of California litigation.

The Fifth Circuit has ruled in a Texas case that various excess insurers' indemnity duties required the actual payment of the underlying insurer's limits and therefore were not triggered by a settlement in which the insured had accepted less than the carrier's full limits. In *Citigroup, Inc. v. National Union Fire Ins. Co. of PA*, No. 10-20445 (5th Cir. August 5, 2011), Citigroup sued various excess insurers seeking a declaration of coverage for class action claims that an affiliate had violated truth in lending statutes by misrepresenting that refinancing its customers' debts into a single loan secured by their homes would be beneficial. Citigroup eventually settled its claims against Lloyd's for \$15 million in consideration of the dismissal of a layer of insurance with a \$50 million limit. As a result, despite Citigroup's argument that its settlement with Lloyd's had "exhausted" the underlying limits, the Fifth Circuit agreed with a Texas District Court that the excess policies in the layer above the Lloyd's policy were not triggered. The Court of Appeals noted that a Chubb policy that stated that coverage attaches only after "(a) all Underlying Insurance carriers have paid in cash the full amount of their respective liabilities, (b) the full amount of the Underlying Insurance policies have been collected by the plaintiffs, the Insureds or the Insureds' counsel, and (c) all Underlying Insurance has been exhausted" unambiguously required that the underlying policies have actually paid their full limits. Likewise, the court reached similar conclusion with respect to language in the Steadfast policy dictating that its coverage did not attach until the underlying insurer makes a payment equal to all the underlying insurer's limits of liability." The

Fifth Circuit declined to find that the excess policies exhaustion requirement were ambiguous,, nor did it accept Citigroup's request that it follow the Second Circuit's analysis of similar issues in *Zeig*.

Several recent federal cases have also addressed the impact of self-insured retentions on excess carriers.

The Fifth Circuit ruled in another Texas case that the entry of a judgment in excess of the insured's self-insured limit did not trigger the excess coverage since the insured had not yet actually paid the SIR. In *Estate of Bradley v. Royal Surplus Lines Ins. Co.*, 2011 WL 2817089 (5th Cir. July 19, 2011), the court ruled that the excess insurer's duty to defend was determined solely by reference to its own policy provisions which required that "the applicable limits of the underlying insurance and other insurance have been used up in the payment of judgments or settlements."

Similarly, the Eleventh Circuit ruled in *Georgia-Pacific, LLC v. USF&G*, No. 10-11904 (11th Cir. August 29, 2011) that USF&G had no obligation to provide a defense to the insured railroad in several underlying cases in Mississippi until such time as the underlying \$2.5 million "self-funded retention endorsement" had been exhausted. As did the Georgia District Court, the Eleventh Circuit held in this unpublished opinion that the endorsement was clear and unambiguous in its terms and that, while the policy wordings were "unusual," the District Court's interpretation of them was neither "illogical nor unjust." The Eleventh Circuit ruled, however, that the district court had acted prematurely in assessing the merits of the underlying claim in holding that USF&G would not in any event owe coverage for any losses that might penetrate the SIR.

On the other hand, while seemingly acknowledging that the insured's inability to fund its SIR obligations does not require an umbrella carrier to "drop down," the U.S. Court of Appeals for the First Circuit has ruled that the insured's failure to pay does not eliminate the insurer's duty to pay what it would have owed had the insured paid as promised. Even though the excess policy stated that its coverage would not arise until

there had been a “complete expenditure” of the insured’s retained limit by the payment of judgments, settlements or defense costs, the First Circuit has ruled that a Rhode Island District Court erred in holding that the insured’s failure to pay the SIR due to bankruptcy relieved the insurer from any obligation to pay damages over the \$500,000 SIR that it would have owed anyway. In *Rosciti v. Insurance Co. of the State of Pennsylvania*, No. 10-2087 (1st Cir. October 7, 2011), the court agreed with ICSOP that the Retained Limit provision was unambiguous and not in conflict with a separate provision dealing with the insured’s bankruptcy. Nevertheless, the court held the clause was unenforceable on public policy grounds because it would nullify the value of R.I. G.L. § 27-7-2.4, which allows plaintiffs to pursue direct action claims in the event of policyholder insolvency. Even if this analysis caused ICSOP to pay more defense costs than its underwriters had anticipated, the court held that such a conclusion was not contrary to public policy.

2. Follow Form Wordings

In *Estate of Bradley v. Royal Surplus Lines Ins. Co.*, 2011 WL 2817089 (5th Cir. July 19, 2011), the Fifth Circuit held that an excess insurer did not have a duty to defend because it only followed form with respect to a specific underlying policy issued by Lexington that did not contain a duty to defend. Accordingly, the court ruled that the excess insurer’s duty to defend was determined solely by reference to its own policy provisions which required that “the applicable limits of the underlying insurance and other insurance have been used up in the payment of judgments or settlements.”

3. Reinsurance Obligations

In a case now on appeal to the U.S. Court of Appeals for the First Circuit, a District Court in Massachusetts ruled that where a facultative certificate stated that the defendant was only reinsuring a liability policy issued by Commercial Union for a single year, a federal district court has rejected OneBeacon’s contention that the reinsurer was also obligated to reimburse it for losses involving coverage that was allegedly renewed for an additional two years. In *OneBeacon America Ins. Co. v. Commercial Union*

Assurance Co. of Canada, No. 10-10164 (D. Mass. August 18, 2011), Senior Judge Tauro denied OneBeacon's motion for summary judgment, holding that the evidence that it claimed to rely on with respect to these renewals was inadmissible as involving "sham affidavit" testimony beyond the personal knowledge of the affiant. Further, in granting defendant's motion for summary judgment, the Court ruled that there was, in fact, significant evidence that the 1981 and 1982 policies were not renewals of the reinsured agreement.

An appeal that had promised to shed some light on whether Massachusetts would acknowledge cut through obligations on the part of a reinsurer that took an active role in placing primary insurance has been dismissed pursuant to a settlement between the parties. In *Neles-Jamesbury, Inc. v. Pohjola Ins. Co., Ltd.*, 10-CV-40055 (D. Mass. December 7, 2010), appeal dismissed, No. 11-1023 (1st Cir. 2011), the District Court had ruled that a Finnish insurance company that facultatively reinsured 100% of the risk that Lumbermens Mutual Casualty Company took with respect to a general liability policy issued to a Massachusetts corporation lacked sufficient contacts with Massachusetts to support a claim of jurisdiction. The District Court rejected the insured's argument that the contractual arrangement between Lumbermens and Pohjola as well as Pohjola's role in procuring the Lumbermens policy, established that Lumbermens was acting as Pohjola's agent in Massachusetts. The Court distinguished the Pennsylvania court's decision in *Koken*, holding that in this case Lumbermens acted independently in negotiating the terms of the insurance policy and handling the underlying asbestos claims and was not a mere "pass through" as in *Koken*. In light of the fact that Lumbermens was not the mere agent of Pohjola and because Pohjola reinsured the risk rather than issuing a policy directly to the insured, the court found that Pohjola did not "contract to insure any person, property or risk located within the Commonwealth" within the meaning of the Massachusetts Long Arm Statute.

4. Excess/Surplus Issues

The Colorado Supreme Court has ruled that the statutory requirement that auto policies include coverage for uninsured motorists claims has no application to umbrella insurance. In *Apodaca v. Allstate Ins. Co.*, 2011 WL 2449841 (Colo. June 20, 2011), the court declared that the policy's inclusion of supplemental liability coverage for automobiles or motor vehicles did not transform it into an "automobile liability or motor vehicle liability policy" subject to the requirement of Section 10-4-609(1)(a) that auto insurers include UM/UIM coverage as part of the policy.

5. Characterizing Coverage

The Texas Supreme Court heard oral argument on September 14 in the matter of *Texas Dept. of Ins. v. American National Ins. Co.* At issue is whether the Texas Department of Insurance has authority to regulate stop-loss agreements that the carriers claim is not subject to the TDI's oversight because it is a form of "reinsurance."

Section Chairs

If you have any questions about the Section or the FDCC, please feel free to contact me or one of your Vice Chairs:

- Chair Meloney Perry, Meckler Bulger Tilson Marick & Pearson LLP Dallas TX
- Vice Chair Russell Allison, Carr Allison Birmingham AL
- Vice Chair Michael Aylward, Morrison Mahoney & Miller, LLP Boston MA
- Vice Chair Charles Henderson, Henderson Consulting and Risk Management Newtown Square PA
- Vice Chair Milton Thurm, McIntosh, Sawran, Peltz & Cartaya, P.A. West Palm Beach FL

For our detailed contact information and a list of all of our Section Members click on this link, which is on the FDCC website:

<http://www.thefederation.org/process.cfm?pageID=6&groupID=256>

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