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5 Insurance Battlegrounds To Watch In New York

By **Jeff Sistrunk**

Law360, Los Angeles (May 13, 2015, 2:19 PM ET) -- More than two years after Superstorm Sandy battered the East Coast, New York courts are continuing to grapple with a slew of insurance coverage issues tied to the storm.

Those lawsuits and other high-stakes battles, including JPMorgan Securities Inc.'s bid for $200 million in coverage for regulatory settlements and an attorney-client privilege dispute with potential implications for professional liability coverage actions, have lawyers' attention. Here, experts discuss five issues they're keeping a close eye on.

Sandy Coverage Spats

Among the most notable issues being litigated in Sandy coverage suits is the interplay between deductibles, additional coverage grants, sublimits and causation, said Sherilyn Pastor, the practice group leader for McCarter & English LLP's insurance coverage group.

For instance, in the case of El-Ad 250 West LLC v. Zurich American Insurance Co., the policyholder — a Manhattan real estate developer — purchased additional coverage for delay in completion risks. The trial judge ruled, in a case of apparent first impression, that a $5 million limit in a Zurich American Insurance Co. policy for flood losses applies to the developer's claims for construction delays stemming from Sandy.

On appeal, the policyholder is contending that the Zurich policy's $7 million sublimit was the proper cap.

"How the issue plays out, ultimately, will be important, not only for this particular policyholder and on this type of policy, but more broadly when it comes to the interplay, if any, among coverages, additional coverages, sublimits and/or deductibles," Pastor said.

Also capturing attorneys' attention is transportation giant Amtrak's $1 billion row with a host of insurers over Sandy-related losses. That case involves disputes over the definition of "flood" in the policies' flood sublimit, the definition of an occurrence and the potential availability of consequential damages.

In a brief filed last month, Amtrak asserted that storm surge was included in the definition of flood in only one of the policies in its 2011-2012 insurance program. The other insurers added those words to their flood definitions only after Sandy hit, according to the transportation giant.

"This counsels policyholders to pay close attention to the specific language in their program," said Jenner & Block LLP associate Jan Larson. "Each case will be dependent on the specific policy language. If there is a difference in the definition of ‘flood’ between earlier and later policies, Amtrak may have a good argument that the policy language is ambiguous as to whether wind-driven storm surge falls within the definition of flood."

The parties also disagree over whether damage caused by water can constitute a separate occurrence from damage caused by salt present in the water.

"This dispute highlights the key role that causation issues can play in coverage cases," Larson said. "Policyholders will want to consider causation issues early on and consider working with an expert."

Amtrak is seeking consequential damages based on its insurers' alleged breaches of contract. A New York federal judge in February granted the insurers' partial motion to dismiss Amtrak's consequential damages demand, except as it related to the railroad's claims of unnecessary expenses brought on by an "unduly protracted" adjustment process.

Following the state high court's landmark 2008 decision in Bi-Economy Market Inc. v. Harleysville Insurance Co. of New York, the courts "still seem to be addressing when consequential damages should be awarded against insurers, and how they should be measured," according to Pastor.

"The appropriate measure of damages continues to be an issue in this case and, more generally, under New York law," Pastor said.

JPMorgan's Settlement Coverage Fight

Attorneys say they'll be tracking JPMorgan's efforts to secure $200 million in coverage for massive settlements of regulators' market-timing trade allegations against Bear Stearns Cos. Inc., which the bank now owns.

Bear Stearns in 2006 agreed to pay $160 million in disgorgement and $90 million in penalties to the U.S. Securities and Exchange Commission and the New York Stock Exchange to resolve accusations that it was involved in illegal late trading and deceptive market timing that enriched hedge fund clients. The bank neither admitted nor denied wrongdoing.

The insurance coverage case, which dates back to 2009, has touched on a number of contentious issues, including the definition of a "judgment or other final adjudication" of wrongdoing under the relevant professional liability policy's dishonest acts exclusion.

In January, a state appellate panel found that JPMorgan's insurers can't invoke the dishonest acts exclusion to bar coverage because Bear Stearns' agreements with the SEC and the NYSE resulted from negotiations and don't qualify as a judgment or other final adjudication of wrongdoing.

"That comes back to the general New York rule that, if an insurer is going to refuse coverage by an exclusion, it has to do so clearly and unmistakably," said Anderson Kill PC shareholder William G. Passannante.

Had that exclusion applied, there would have been no coverage, at least for the SEC settlement and the NYSE stipulation, Passannante noted.

On remand, the insurers will still be able to fight coverage based on their contention that allowing JPMorgan to seek indemnification for the settlement sums would violate New York public policy disfavoring coverage for intentionally harmful conduct.

Scope of Attorney-Client Privilege

The outcome of a pending appeal in a malpractice case against Philadelphia-based law firm Schnader Harrison Segal & Lewis LLP may affect the scope of attorney-client privilege in battles over coverage under professional liability policies, according to Pastor.

Former Schnader Harrison client and onetime MasterCard International Inc. employee Keith Stock sued the law firm for allegedly failing to advise him that his departure from the company would accelerate the expiration date for his stock options.

In the midst of a dispute over privileged documents, a New York state judge ruled that Schnader Harrison attorneys' communications with their in-house general counsel at the firm were not protected by the attorney-client privilege. The firm appealed the decision.

The issues involved in the case "impact the protections associated with communications between firm partners and general counsel not only in an underlying malpractice case, but potentially in professional liability coverage disputes," Pastor said.

"Does an insurer have the right to lawyers' communications with a firm's general counsel regarding ethical obligations to a client that later alleges malpractice?" Pastor said. "If those protected documents must be produced to the client under an exception to the attorney-client privilege, does that make them somehow discoverable in the coverage dispute?"

Cyber Coverage Litigation Post-Sony

While Sony Corp. of America's settlement with two insurers in litigation over coverage for the infamous PlayStation Network cyberattack forestalled an appellate-level decision in New York addressing key issues regarding data breach coverage under commercial general liability policies, those issues will remain prominent, according to attorneys.

"Sony won't be the last we hear about these issues," Pastor said.

The trial court judge in the case ruled from the bench that hackers' theft of confidential data on tens of millions of Sony PlayStation users was a "publication" of private information, as required by the relevant policy, but that the cyberattack still didn't trigger the insurers' obligation to defend Sony from resulting litigation. Sony appealed, but the parties reached a settlement before the appellate court issued an opinion.

"It would have been a big deal to have an appellate decision on what constitutes a publication under these policies," said Jenner partner Brian S. Scarbrough. "That issue comes up in nondata contexts as well."

With the proliferation of cyber exclusions in CGL policies, companies are increasingly turning to cyber-specific insurance policies to protect themselves. However, many will still look to more traditional policies for coverage for some time to come, so the trial court's decision in Sony will likely continue to have an impact in cyber coverage litigation, according to attorneys.

"Ambiguous exclusions being added to traditional policies, directed at cyber liabilities and risks, are also likely to be the subject of litigation, particularly as to claims for coverage for invasion of privacy," Pastor said.

False Claims Act Coverage Suits

Disputes over insurance coverage for costs incurred by policyholders in defending against whistleblower, or qui tam, suits brought under the False Claims Act continue to be heavily litigated in New York, according to attorneys.

Due to the structure of the FCA, coverage disputes over qui tam litigation feature unique issues.

In one high-profile case, a New York appeals court last month freed Lloyd's of London underwriters from paying Huron Consulting Group Inc.'s $2.7 million defense tab in a whistleblower suit involving alleged overbilling by a hospital, concluding that an exclusion in the Lloyd's policy for government suits applies even though the government declined to intervene in the underlying action.

While a private individual pursued the underlying suit, the government was still the real party in interest in that case, and the exclusion therefore applied, the court found.

"The takeaway is that policyholders need to pay attention to those particular sorts of exclusions," Scarbrough said. "The preamble wording will be key in terms of defining how broad it will be and what sort of governmental entities will qualify. Policyholders should remove or narrow those exclusions to whatever extent they can."

--Editing by Kat Laskowski and Philip Shea.
