



EDITOR'S NOTE

On this, the occasion of our first post-September 11th Insurance Newsletter, we again take time to thank our friends and clients for their heartfelt expressions of sympathy and offers of assistance.

We are pleased to announce the opening of our new Manhattan location at One Penn Plaza, New York, New York 10119, where our phone and facsimile numbers will be (212) 682-4500 and (212) 947-8180, respectively.

We are also pleased to announce that within a few months our new and expanded Nassau County office will open at 1010 Franklin Avenue, Garden City, New York 11530. We will provide additional information as the opening date becomes fixed and draws near.

NEW YORK COURT OF APPEALS SUSTAINS SUIT AGAINST AUTOMOBILE MANUFACTURER BY WIDOW OF DRUNK DRIVER

The New York Court of Appeals has allowed a widow to continue with a products liability suit against a car manufacturer, notwithstanding that her late husband's intoxication was In *Alami v. Volkswagen of America, Inc.*, 2002 WL 234564, 2002 NY.Slip.Op. 01337 (N.Y. February 19, 2002), the Court limited the application of the *Barker/Manning* rule, which generally provides that "where a plaintiff has engaged in unlawful conduct, the courts will not entertain suit if the plaintiff's conduct constitutes a serious violation of the law and the injuries for which the plaintiff seeks recovery are the direct result of that violation."

Plaintiff's late husband, Silhadi Alami, was driving alone in his Volkswagen Jetta. Traveling at approximately 35 miles per hour, the car left an exit ramp and collided with a utility pole. At the time of the accident, Alami, who died as a result of his injuries, blood alcohol level exceeding the legal limit.

In her suit against Volkswagen of America, Inc., plaintiff sought to recover on the theory that a

defect in the vehicle's design enhanced her late husband's injuries, and as such, contributed to his death. Volkswagen moved for summary judgment arguing that Mr. Almani's intoxication was the sole cause for the crash and no defect or malfunction in the Jetta caused or contributed to it. In response, plaintiff proffered expert testimony that had Volkswagen provided safety features which were readily available and in common use in the automobile industry—her late husband would have survived the crash with minimal injury.

The trial court applied the *Barker/Manning* rule and granted Volkswagen's motion. The court precluded plaintiff's claim based on its finding that "decendent's drunk driving constituted a serious violation of the law and that his injuries were the direct result of that violation." Thereafter, the Appellate Division affirmed.

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The Court of Appeals reversed, holding that while the *Barker/Manning* rule is sound, its application should be limited to cases falling within two narrow categories: (1) those in which the parties to the suit were involved in the underlying criminal conduct, and (2) those in which the criminal plaintiff seeks to impose a duty “arising out” of an illegal act.

The Court found that plaintiff was not seeking to impose a duty on Volkswagen “arising out of” her late husband’s illegal intoxication. Rather, plaintiff was simply seeking to invoke a duty owed by Volkswagen to any driver of a Jetta involved in a crash, regardless of the initial cause—namely, the duty to produce a product that does not unreasonably enhance or aggravate a user’s injuries. The Court concluded that applying the *Barker/Manning* rule to the present case would impermissibly relieve Volkswagen of its duty to manufacture a safe vehicle. ✎

—Elizabeth Lauriello Neumann

FAILURE TO PROVIDE NOTICE OF DISCLAIMER TO INJURED PARTY INVALIDATES ATTEMPTED DISCLAIMER

The New York Court of Appeals has expressly held that an insurer’s failure to give timely written notice of its disclaimer to the injured party violated New York Insurance Law § 3420 (d). In a decision that could have a broad impact on insurers, the Court indicated that a timely disclaimer pursuant to Insurance Law § 3420 (d) is required when a claim falls within the coverage, but is denied based on a policy exclusion.

In *Markevics v. Liberty Mutual Insurance Co.*, 97 N.Y.2d 646, 761 N.E.2d 557, 735 N.Y.S.2d 865 (2001), plaintiff commenced an action seeking a declaratory judgment that Liberty Mutual must defend and indemnify Kerry O’Brien pursuant to a homeowner’s policy issued to O’Brien’s parents.

In the underlying personal injury action, plaintiff alleged that O’Brien served liquor to a visibly intoxicated Sandro Perez at O’Brien’s Bar. After leaving the bar, Perez drove his automobile into a utility pole, injuring plaintiff, who was a passenger in the car.

O’Brien’s Bar was a family enterprise operated

by O’Brien’s parents. O’Brien worked there as a bartender and lived at her parent’s home. Liberty Mutual wrote a “deluxe” homeowner’s policy to the O’Briens, which not only provided coverage for the “insured premises”, but also for liability claims against an insured individual. Excluded from the personal liability coverage, however, were claims injuries arising out of the business pursuits of the insured. The parties did not dispute that O’Brien was an insured under the policy.

After commencement of the personal injury action, O’Brien’s attorney tendered her defense to Liberty Mutual in a letter dated July 23, 1997. Liberty Mutual disclaimed coverage on November 7, 1997, relying on the policy’s business pursuits exclusion. Liberty Mutual did not, however, send a copy of the disclaimer letter to plaintiff or her attorney.

The Court of Appeals held that since Liberty Mutual’s denial was based solely on a policy exclusion, a disclaimer pursuant to Insurance Law § 3420 (d) was required. As Liberty Mutual’s attempt to disclaim coverage did not meet this requirement in that Liberty Mutual did not give timely written notice of its disclaimer to the injured party, the requirements of § 3420 (d) were not satisfied. As a result, Liberty Mutual was required to defend and indemnify O’Brien. ✎

—Elizabeth Lauriello Neumann

NEW YORK COURT OF APPEALS REJECTS AGGREGATE THEORY ON REINSURANCE RECOVERY

The New York Court of Appeals has rejected a theory which would have allowed an insurer to aggregate its payment of environmental damage claims arising at different times and places to be aggregated into a single loss in order to reach the threshold which would invoke a reinsurance policy. In *Travelers Casualty and Surety Company v. Certain Underwriters at Lloyd’s of London*, 96 N.Y.2d 583, 760 N.E.2d 319, 734 N.Y.S.2d 531 (2001), Travelers sued its reinsurers, seeking monetary damages and declaratory relief for settlements paid by Travelers to its insureds. The Appellate Division, First Department had previously ruled in favor of the reinsurers. See *New York Appellate Court Holds Reinsurers Not Obligated to Treat Settlements as*

One Loss, OHRENSTEIN & BROWN INS. NEWSLETTER, Winter 2001 at 9.

Between 1960s and 1980s, Travelers issued primary insurance policies to Koppers and purchased reinsurance in connection with the policies. The policies issued to Koppers provided coverage for loss arising out of “disaster and/or casualty” which was defined as “loss resulting from a series of accidents, occurrences and/or causative incidents having a common origin and/or being traceable to the same act, omission, error and/or mistake.”

In the early 1980s, governments and private parties brought environmental actions against Koppers, which in turn, sued Travelers, claiming that it was obligated to defend and indemnify Koppers for potential liabilities at the sites. Following a decade of litigation, Travelers settled with Koppers for \$140 million. Travelers apportioned the \$140 million to the underlying insurance policies, treating each of the Koppers sites as separate occurrences. Subsequently, Travelers sought reimbursement of \$61.5 million of this settlement from reinsurers under the rationale that Koppers’ loss resulted from a “common origin” and/or was “traceable to the same act, omission, error and/or mistake” made by Koppers in its company-wide practice even though the occurrences happened at different times and places.

Travelers made the same argument in a similar matter involving its insured, DuPont. With regard to DuPont, Travelers sought reimbursement of \$34 million from reinsurers after having paid DuPont \$72.5 million for claims arising from pollution liabilities. Travelers argued that the polluted sites shared a “common origin,” namely the failure of DuPont to implement and enforce a company-wide environmental policy.

The Court of Appeals rejected Travelers’ argument that the separate occurrences at different times and places constituted a “series of” occurrences having a “common origin.” The Court stated that reinsurance contracts did not allow occurrences, however remote in place or time, to be treated as a single loss. The Court further noted that Travelers could have aggregated the claims if the occurrences had a spacial and temporal relationship to one common origin, which was not the case here. In this case, the acts of pollution occurred over

decades and on different sites. Since treatment of each site as a separate loss failed to pierce the retention level under the reinsurance contracts, summary judgment was properly granted in favor of the reinsurers.

Travelers alternately argued that even if summary judgment was properly granted as to whether the polluted sites could be aggregated into a single loss, the reinsurance contracts had a “follow the fortunes” clause which obligated reinsurers to cover all payments made by Travelers to its insureds pursuant to settlements or judgments. However, the Court held that this clause could not supercede the language of the policy since it would bind reinsurers to indemnify a reinsured whenever it paid a claim, regardless of the contractual language defining loss. ✎

—*Mari Grace Sacro*

SECOND CIRCUIT COURT OF APPEALS HOLDS THAT EMPLOYMENT CLASSIFICATION DOES NOT SERVE TO LIMIT COVERAGE OF CGL POLICY

In *Mount Vernon Fire Ins. Co. v. Belize NY, Inc.*, 277 F.3d 232 (2d Cir. 2002), the United States Court of Appeals for the Second Circuit addressed the issue as to whether a commercial general liability policy’s classification listing constituted a limitation of coverage for bodily injury and property damage. Citing to *Cont’l Cas. Co. v. Rapid-American Corp.*, 80 N.Y.2d 640, 652, 609 N.E.2d 506,512, 593 N.Y.S.2d 966, 972 (1993), which requires that exclusions for coverage must be set forth clearly and unmistakably, not be subject to any other reasonable interpretation and fit the particular case, the appellate panel held that the policy lacked any language limiting coverage to “carpentry” and concluded that the language of the proposed limitation was by no means “clear and unmistakable.” The rationale of the court’s decision was the premise that if an insurer was able to limit its policy coverage through the classifications listing, the insured would not be alerted to the limitation, permitting insurers to argue for limitations by invoking “stand-alone words of classification” not otherwise referred to in a policy. The court further held that if the insurer wanted to limit the coverage based upon classifications, it could have done so specifically.

On June 15, 1995 Mount Vernon issued a commercial general liability policy to Belize, a general construction company. Among other things, the policy's first page, entitled "Policy Declarations" classified the "Form of Business" as "Corporation" and the "Business Description" as "Carpentry" and indicated that Belize was afforded commercial liability insurance in the amount of \$1,000,000 per occurrence and \$2,000,000 in the aggregate. Two classes were listed under "Premium Computation" on the Declarations Page: "Carpentry-Interior-001" and "Carpentry-001." No further mention of these terms were made in the policy.

In 1994 Belize was hired by LEMA International, Ltd., a general contractor, to perform the demolition work, which Belize subcontracted to others, in connection with a renovation project in a building housing a religious group known as United House of Prayer for all People of the Church on the Rock of the Apostolic Faith. Thereafter, Belize was hired by LEMA to assist in the supervision of LEMA's subcontractors and to make sure that the subcontractors were properly performing their assignments and completing them according to LEMA's time chart. In 1995, LEMA ceased to be the general contractor and Belize was informed to submit its invoices to LMA International, Ltd., which had replaced LEMA as the general contractor.

On December 8, 1995, during the course of the renovation work, a person entered into the United House building, shot several people and then started a fire before committing suicide. Seven people died and several others were injured.

In 1996, an action was commenced against Belize on behalf of one of the individuals who had died as a result of the fire. It was alleged that (1) Belize was negligent, careless and reckless; (2) the sprinkler was unlawfully shut off; and (3) LMA had "bricked over, eliminated and/or made inoperable, one or more means of ingress and egress to the premises."

Pointing to "assertions regarding Belize's potential involvement" in the renovation project, Mount Vernon commenced a declaratory judgment action alleging that it was not required to defend or indemnify Belize for liability arising out of the performance of work at the construction site. Mount Vernon argued that Belize was not engaged in carpentry work at the time of the December 8, 1995 incident

and that only liabilities created as a result of Belize's carpentry work were covered under the policy. Mount Vernon contended that at the time of the incident, Belize was acting in a supervisory capacity and therefore any liabilities Belize incurred were not covered by the policy.

Granting summary judgment, the District Court held that the policy did not provide a limitation of coverage based on the business classifications found within the Policy Declarations. The District Court's rationale was based on the fact that Mount Vernon failed to include "clear and unmistakable language" limiting the insurance risk to carpentry, as required by New York law. The Second Circuit affirmed, holding that the policy lacked any language limiting coverage to "carpentry" and concluded that the language of the proposed limitation was by no means "clear and unmistakable." ❖

—*Joann Scifo*

IN DETERMINING COVERAGE FOR NEGLIGENT SUPERVISION CLAIM UNDER ERRORS AND OMISSIONS POLICY, COURT LOOKS TO CONDUCT OF INSURED RATHER THAN ITS EMPLOYEE

New York's Appellate Division, Second Department, addressing an issue of first impression, has held that the intentional act exclusion contained in an errors and omissions policy issued to a school district did not apply to permit the insurer to disclaim coverage for the district's alleged negligent hiring and supervision of a teacher later accused of sexually abusing students. In a decision that could have a broad impact on insurers, the court indicated that to deny coverage where the risk insured against sets in motion a chain of events resulting in an excluded act, would "frustrate the reasonable expectations of the insured."

In *Watkins Glen Central School District v. National Union Fire Ins. Co. of Pittsburgh, Pa.*, 286 A.D.2d 48, 732 N.Y.S.2d 70 (2d Dep't 2001), Watkins Glen Central School District commenced an action against National Union seeking defense and indemnification under an errors and omissions policy, in connection with an action where it was alleged that the school district was negligent in connection with its hiring, supervision, and retention of a teacher, Gary Serlo.

Serlo was reportedly convicted in Pennsylvania in 1974 of sex crimes he committed in the course of his prior employment as an elementary school teacher. Despite a lengthy gap in his teaching employment history, the school district hired Serlo in 1984, allegedly without conducting an adequate background check. Then, at subsequent times during his employment with the school district, Serlo had allegedly been the subject of complaints of sexual misconduct with students, which the district allegedly failed to aggressively investigate.

At all pertinent times, the school district was insured under a school leaders errors and omissions policy underwritten by National Union. When the school district was served with the complaint in the underlying action, it looked to National Union for defense and indemnification under the errors and omissions policy. National Union disclaimed coverage, however, pursuant to a policy exclusion for claims arising out of assault and battery, and bodily injury and emotional distress.

The Appellate Division explained that New York generally employs a “but for” test that looks to the nature of the underlying conduct to determine whether a certain occurrence is covered or excluded from coverage. Where a negligent supervision claim is based on an intentional act of an insured, the exclusion for intentional acts would apply.

In the instant matter, however, the court found that while Serlo unquestionably committed intentional acts, it was the school district to whom National Union owed a duty of defense and indemnification, not Serlo. The negligent hiring and supervision of Serlo by the district was an act that fell squarely within the errors and omissions policy provided by National Union. ❖

—*Elizabeth Lauriello Nuemann*

INSURERS ORDERED TO PAY PAST AND FUTURE DISABILITY BENEFITS IN A LUMP SUM FOR BAD FAITH

A Supreme Court, New York County judge, has affirmed a jury verdict that ordered a number of insurers (collectively referred to by the court as “First Unum”) to pay past and future disability benefits and attorney fees because they acted in bad faith by repudiating an insured’s policy.

In *Wurm v. Continental Insurance Company of Newark, New Jersey et al.*, 2001 WL 1263363, 2001 N.Y. Slip Op. 40155(U) (N.Y.Sup., Sept. 5, 2001) plaintiff, a dentist, sustained spinal injuries resulting from a horseback riding accident. The disability policy issued to her by First Unum policy entitled her to lifetime monthly benefits if she became totally and permanently disabled from practicing dentistry.

Although First Unum began paying benefits to Dr. Wurm following her accident, the insurer continued to investigate her claim. She was placed under surveillance at least 15 times. Moreover, one of the insurer’s claims supervisors posed as a patient and attempted to schedule a dental appointment. Despite a report from a claims examiner who wrote, “we do not have sufficient medical documentation to withhold benefits”, the company continued its investigation and, after Ms. Wurm was paid \$400,000, denied her future benefits.

After being instructed that a finding of bad faith was permissible if First Unum “evidenced a reckless or gross disregard for its policy obligation, or was disingenuous or dishonest in its failure to carry out the contract,” the jury returned a verdict of \$3.4 million—a combination of \$708,726 for past benefits, roughly \$1.8 million for future benefits, \$258,000 for pre-judgment interest and attorney’s fees amounting to 30% of the total verdict. The jury verdict was reported to be the first to award future benefits in a lump sum to a plaintiff for a determination of bad faith.

First Unum asked the trial judge, Emily Jane Goodman to set aside the verdict, arguing that the jury was incorrectly instructed on how to decide the bad faith charge and jury should not have heard evidence on plaintiff’s claims for future damages, bad faith, deceptive trade practices and punitive damages. Justice Goodman, who noted that the jury, in fact, favored First Unum on deceptive trade practices and punitive damages, rejected both arguments – a fact, she wrote, that contradicted First Unum’s assertion that her instructions created sympathy for Dr. Wurm. ❖

—*Nicole Fox*


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