OHRENSTEIN & BROWN, LLP

SUMMER 1996

INSURANCE NEWSLETTER

NEW YORK WORKERS' COMPENSATION REFORM PLAN PASSED BY LEGISLATURE

On July 13, 1996, the New York State Legislature passed a comprehensive workers' compensation reform plan (the "Act") which will have a very significant impact on the defense of lawsuits brought by employees injured on the job. Governor Pataki was expected to sign the Act around the time this issue went to press. The following is a summary of the changes effected by the new law.

The major provisions of the Act would:

- **Limit third-party actions against employers to cases involving "grave injuries"**

An injured worker who is collecting workers' compensation from his or her employer cannot sue the employer in a separate action. The employee can, however, sue another party, such as an equipment manufacturer, landlord or general contractor. Under the 1972 Court of Appeals ruling in *Dole v. Dow*, the entity sued by the employee can then bring a third-party action against the employer for contribution and/or indemnification. For example, the manufacturer of a textile cutting machine can implead the plaintiff's employer on the theory that the employer modified the machine or failed to properly supervise the plaintiff.

The Act essentially repeals *Dole v. Dow* to prohibit third-party actions against employers except in two narrow situations.

First, a third-party action may be brought where the plaintiff has sustained narrowly defined "grave injuries". Grave injuries, as defined in the law, include:

a. death;

b. permanent and total loss of use or amputation of an arm, leg, hand or foot;

c. paraplegia/quadriplegia;

d. total and permanent blindness or deafness;

e. permanent and severe facial disfiguration;

f. brain injury resulting in permanent total disability;

g. loss of multiple fingers or toes;

h. loss of nose or an ear; and

i. loss of index finger.

Second, a defendant may still bring a third-party action (irrespective of the severity of the injury) against an employer "based upon a provision in a written contract entered into prior to the accident or occurrence by which the employer had expressly agreed to contribution to or indemnification of the claimant or person asserting the cause of action for the type of loss suffered." For example, a general contractor will be able to implead an employer/sub-contractor based upon an indemnity and/or hold harmless provision in their contract running in favor of the general contractor relating to injury claims by the sub-contractor's employees.

- **Amend the CPLR so that the culpable conduct of the employer will not be considered in determining the equitable share of each defendant's liability**

Section 1601 of the Civil Practice Law and Rules addresses the situation where a verdict is rendered in favor of a plaintiff in an action involving two or more tortfeasors who are jointly held liable. Traditionally, if the liability of a defendant was found to be 50% or less of the total liability assigned to all persons liable, the liability of such a defendant

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to the claimant for non-economic loss (i.e. pain & suffering) would not exceed that defendant's "equitable share." The equitable share was determined in accordance with the relative culpable conduct of each person causing or contributing to the total liability for non-economic loss whether a party or not. Previously, therefore, under Section 1601 the conduct of culpable entities not named in the lawsuit would be considered in determining each party's equitable share. Section 1601 is now amended to the extent that the culpable conduct of a non-party employer paying workers' compensation will not be considered by the jury in determining the equitable share of total liability unless the plaintiff has sustained a "grave injury", as previously defined.

In practice, the defendant in most cases will be unable to either implead the employer or to benefit from a deduction for the equitable share of fault of the employer as an "empty chair".

ANALYSIS

The reform of New York's workers' compensation system will have both positive and negative ramifications for general liability insurers and workers' compensation carriers. Clearly, there will be fewer costly third-party lawsuits brought against insureds in their capacity as employers. Until now, New York was one of the few states which allowed unlimited third-party lawsuits against an injured party's employer. At the same time, however, insureds such as general contractors and manufacturers will no longer be able to "pass through" liability to a plaintiff's employer in all third-party lawsuits, thereby increasing the costs of defending and insuring these insureds. Ironically, in one scenario, an insured employer would benefit from the new law by escaping from potential third-party liability, but would also suffer a detriment in another case when the same insured is precluded from impleading a plaintiff's employer.

We anticipate that there will be significant litigation with respect to whether the new law applies to cases which are currently in suit, but where the defendants have not yet interposed third-party actions. (The Act ambiguously states that it "shall take effect immediately", but does not otherwise address this issue.) Further, as with the automobile no-fault law's definition of "serious

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injury", the definition of "grave injury" will spawn a great deal of litigation.

Further, it is our view that it will now be more difficult to involve the workers' compensation carrier in settlement negotiations and to persuade the workers' compensation carrier to waive or compromise the workers' compensation lien, which is often an important element of a settlement package. The statute may have other wide ranging impacts upon setting reserves, underwriting decisions, and insurance policy drafting.

We have recommended and continue to recommend the following:

1. Review all pending lawsuits to ascertain whether the employer is a potential third-party defendant. If so, a third-party action should be commenced as soon as possible against the employer in advance of the act being signed into law by the Governor.

2. Insureds such as manufacturers, landlords and contractors should consider requiring entities with whom they contract to include in their agreements hold harmless andindemnification clauses in their favor. A third-party action for contribution and indemnification against an employer would then be permitted, even in cases where the plaintiff has not sustained a "grave injury". On the other hand, insureds whose employees are likely to be injured while working for others would want to avoid entering into such contracts. Particular attention should be paid to invoices, purchase orders and the like which often contain "hidden" indemnity clauses.

3. In cases where the insured is a third-party defendant/employer who has not contractually agreed to indemnify the defendant and the plaintiff has not suffered a "grave" injury, the viability of a motion to dismiss the claim should be considered. ❧

JUAREZ REVISITED: VIOLATIONS OF LOCAL LAW 1 REQUIRING REMOVAL OR COVERING OF LEAD PAINT DO NOT CONSTITUTE NEGLIGENCE PER SE

In our Summer, 1995 edition of the INSURANCE NEWSLETTER, we reported on a decision of keen interest to multiple dwelling property owners, managers and their insurers, concerning the standard of liability imposed under New York City's "Local Law 1" for injuries to infants caused by lead paint poisoning (Administrative Code § 27-2013[h][1]). In *Juarez v. Wavecrest Management Team, Ltd.*, 212 A.D.2d 38, 627 N.Y.S.2d 620 (1st Dep't 1995), the New York's Appellate Division, First Department held that a landlord's common law duty of care was supplanted by Local Law 1, which provides that an owner of a multiple dwelling "shall remove or cover . . . any paint or other similar surface-coating material" containing excessive amounts of lead. In so finding, the court concluded that while a violation of Local Law 1 did not impose absolute or "strict" liability upon an owner, such violation did constitute negligence *per se*. See *Violations of Local Law Class Filing Lead Paint as Hazardous Held Not to Impose Absolute Liability*, OHRENSTEIN & BROWN INS. NEWSLETTER, SUMMER 1995 at 3.

In an unanimous opinion dated July 2, 1996, the New York Court of Appeals reversed the Appellate Division's decision in Juarez, holding that the element of "notice" required at com-mon law must still be satisfied in order to establish an owner's negligence and resulting liability for injuries caused by lead paint. In *Juarez v. Wavecrest Management Team, Ltd.*, ___ N.Y.2d ___, 1996 WL 365903 (July 2, 1996), the New York Court of Appeals observed that Local Law 1 "abrogated" the common law "only to extent indicated by the clear import of its enactment . . ." As such, it found upon reviewing New York City's regulatory scheme that the absence of language in Local Law 1 charging landlords with a duty of inspection was "particularly telling," and supported its conclusion that the law provides for "constructive notice" of a hazardous lead condition where a landlord has knowledge that a child resides in an apartment.

The Court further noted that a landlord may be deemed to have constructive notice of a lead condition where it is authorized to enter an apartment. Such notice would arise, explained the Court, where the landlord has retained in its lease the right to enter the interior of an apartment to inspect the premises. Likewise, the Court remarked that a landlord may be charged with constructive notice under Local Law 1 itself, which confers landlords with a right of entry to inspect and repair lead conditions. Under such circumstances, the Court wrote that although Local Law 1 does not impose on landlords "a continuous and affirmative duty to

inspect for the residence of children," a landlord would be deemed to have notice if it learns that the apartment is occupied by an infant.

The chief lessons of *Juarez* can thus be stated in practical terms as follows: While a violation of Local Law 1 is not negligence per se, if a landlord has reason to know that a child under 7 occupies an apartment, the landlord must take reasonable steps to remedy any hazardous lead condition. As a result of the right of entry conferred upon a landlord by the terms of a lease or by Local Law 1, the landlord will be charged with constructive notice of any hazardous lead paint condition in an apartment. ❧

CLAIMS FOR "UNINTENDED" INJURIES RESULTING FROM SEXUAL ASSAULTS EXCLUDED BY INTENTIONAL ACTS EXCLUSION

In *Travelers Ins. Co. v. Stanton*, ____ A.D.2d ____, ____ N.Y.S.2d ____, 1996 WL 431188 (3d Dep't Aug. 1, 1996), and *Pistolesi v. Nationwide* Mut. Fire Ins. Co., ____ A.D.2d ____, 644 N.Y.S.2d 819 (3d Dep't 1996), the New York's Appellate Division, Third Department held that allegedly "unintended" injuries resulting from sexual assaults are inherently related to the intentional acts the cause them; and that regardless of the subjective intent of the insured, such injuries flow "directly and immediately" from the sexual misconduct. Accordingly, claims arising from such conduct fall outside the scope of coverage under policy provisions excluding coverage for intentional acts committed by an insured.

In *Pistolesi*, the trial court rendered a decision declaring that the insurer was obligated to defend the insured pursuant to a homeowner's policy in connection with an action where it was alleged that the insured subjected the plaintiff in that action to sexual battery, including non-consensual sexual intercourse. Previously, the insurer had disclaimed coverage on the basis that no "occurrence," within the meaning of the policy, had resulted from the insured's conduct, because the injuries were not the result of an "accident." In addition to specifying coverage only for injuries resulting from "an accident," the policy provided an express exclusion for injuries "expected or intended by the insured."

Reversing the trial court, the Appellate Division noted, "[t]he critical issue is not whether the sexual assault was an intentional act, but whether the harm that resulted to the victim . . . could have been other than harm 'expected or intended by the insured.'" In reaching its determination, the court reasoned that neither the existence nor lack of allegations relating to negligence or unintentional injuries would control. Additionally, the court rejected the argument that the victim's injuries could constitute "unintended" results warranting coverage where, for example, the insured was mistaken as to the victim's lack of consent.

Relying, in part, on the New York Court of Appeals decision in *Allstate Ins. Co. v. Mugavero*, 79 N.Y.2d 153, 581 N.Y.S.2d 142 (1992), the court held that the existence of the insurer's duty to defend in cases involving sexual assault depends upon whether the victim's injuries are "inherent in the nature of the insured's sexual assault and constitute harm 'which flows directly and immediately from [the insurer's] intentional act . . .'" (In Mugavero, the Court of Appeals held that harm to children who had been sexually assaulted must be viewed as intentional despite the possibility that the insured lacked the subjective intent to cause the harm in question.)

Applying this standard, the Appellate Division held that the physical and emotional injuries alleged "[c]learly constitute the type of harm that could only have flowed directly and immediately from the insured's intentional sexual assault . . . ." Further, the court ruled that the harm caused was, as a matter of law, inherent in the nature of the insured's intentional act. Therefore, the court found, the exclusion for intentional acts was applicable and the insurer owed no duty of indemnification to the insured. Lastly, the court noted that its decision was also supported by recognizing the consequences of permitting an insured to commit an intentional act of this nature while transferring the responsibility for his misdeed on to the shoulders of other insureds in the form of higher premiums.

Similarly, in *Travelers*, the Appellate Division revisited this issue after the insurer's motion seeking a declaration that it owed no duty to indemnify an insured for damages assessed against him in a civil action for sexual battery was denied. The underlying action involved claims against the Village of Trumansburg and one of its police officers who had allegedly forced the victim to a remote area

where he forced her to engage in sexual relations. On appeal, the officer argued that the trier of fact could have determined that he honestly but incorrectly believed that the sexual contact would not injure the victim and that, therefore, any injuries arising from such contact could be "unintentional."

Without referencing the language in the policy, the court, relying on *Pistolesi*, stated "[I]t is now well settled that where harm to the victim is inherent in the nature of the act performed, whatever injuries result are, as a matter of law, intentionally caused." Explaining this principle, the court stated, "[I]t is utterly immaterial that defendant may have incorrectly believed that his sexual overtures were unobjectionable . . . " and that the defendant's "[i]ntent to cause the injury is legally inseparable from his intent to commit the tortious act." ❧

FEDERAL APPEALS COURT VACATES INJUNCTION AGAINST ENFORCEMENT OF NEW YORK EXCESS INSURANCE LAW

The United States Court of Appeals for the Second Circuit has vacated and remanded a district court opinion which held that New York's Excess Insurance Law indirectly regulated and unlawfully discriminated against out-of-state risk retention groups. See *Federal Judge Enjoins Enforcement of New York Excess Insurance Law*, OHRENSTEIN & BROWN INS. NEWSLETTER, Spring 1995 at 5. The Court of Appeals held that the district court's grant of summary judgment to the out-of-state risk retention group was incorrect since the district court did not make sufficient factual findings on the issues of indirect regulation or discrimination against the out-of-state risk retention group ("RRG"). The case, *Preferred Physicians Mutual Risk Retention Group v. Pataki*, 85 F.3d 913 (2d Cir. 1996), arises from a challenge to New York's Excess Insurance Law ("EIL") brought by a RRG chartered under Missouri law.

An RRG is similar to a mutual insurance company; persons who are engaged in activities that have a similar exposure to liability may join together to form an insurance company to share such liability. RRGs operate pursuant to a federal statute, the Liability Risk Retention Act ("LRRA"). The purpose of this act was to permit groups of similarly situated insured's to obtain economies of scale through buying insurance on a group basis, and to permit such groups also to self-insure through risk retention groups, and thus not be subject to the ups and downs of the insurance industry cycle. An RRG, upon being licensed to do business in its state of domicile, may do business in all states without being required to obtain additional licenses. The domiciliary state of an RRG may regulate its formation and operation, but the other states in which the RRG operates may only regulate it in a limited manner. The LRRA makes RRGs exempt from any state law which (1) regulates, directly or indirectly, the operation of a RRG or (2) otherwise discriminates against the RRG.

At issue in this case was a provision in New York's EIL which allows physicians and dentists with hospital admitting privileges to obtain a layer of excess insurance coverage at no additional premium, but only if their primary insurance is issued by a New York licensed insurer. Since Preferred Physicians Mutual Risk Retention Group ("Preferred") is exempt from New York's licensure requirements pursuant to the LRRA, its coverage did not satisfy the EIL's eligibility requirements, and thus its insureds were ineligible for the free layer of excess insurance coverage.

Preferred claimed that New York's EIL regulates and discriminates against Preferred in violation of the LRRA. Although the district court granted Preferred's motion for summary judgment, the Second Circuit Court of Appeals vacated the entry of summary judgment, on the ground that material issues of fact existed.

The parties agreed that the EIL constitutes a subsidy to insurers licensed in New York who sell insurance to EIL eligible physicians who are also in the market for excess insurance. The district court had held that the subsidy constituted a "powerful incentive, bordering on compulsion, to out-of-state RRGs to receive New York accreditation."

The Second Court, however, found that it was ambiguous whether the subsidy amounted to unlawful indirect regulation of the RRG. The appeals court stated that the value of the subsidy could be counterbalanced by the fact that the RRG was exempt from the majority of New York's insurance regulations. In addition, the value of the benefit conferred by the EIL was found to depend upon the

importance to physicians of the excess coverage provided. While it might be of significant value to those physicians who would purchase excess insurance in any event, the value to those physicians who would not have otherwise purchased the excess coverage was of a lesser amount. The record below, said the Second Circuit, was unclear as to the impact of the EIL upon Preferred and thus it was unclear if the EIL constituted indirect regulation of the RRG.

The appeals court stated, "the mere existence of a competitive advantage to regulated insurers conferred by a New York State statute does not necessarily amount to indirect regulation." The court concluded that summary judgment should not have been granted to Preferred on these grounds.

With respect to the issue of unlawful discrimination against the RRG, the Second Circuit stated that it was unclear whether the EIL violated the LRRA's prohibition against discrimination. The court addressed the issue of discrimination by stating that "discrimination against a particular class is not proven merely by a showing that the class is a part of a larger group that suffers some competitive disadvantage." The district court's finding, according to the Second Court was premised solely on the conclusion that RRGs (as well as surplus lines and other unlicensed insurers) are injured by EIL. The court found that it was unclear from the record whether the EIL was enacted with discriminatory intent against RRGs. Such a finding would prove discrimination under the LRRA. The court also found that the district court record did not reveal with any certainty that Preferred suffered a disparate impact under the EIL or that it suffered discrimination.

It remains to be seen whether Preferred will on remand be able to develop a factual record sufficient to show that (1) the EIL unlawfully regulates the RRGs by giving an unfair advantage to licensed insurers and (2) whether Preferred can show that EIL had a disparate impact upon the RRG and, further, unlawfully discriminated against the RRG. ❧

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