SIMPSON THACHER
INSURANCE LAW ALERT
JUNE 2011

This Alert addresses decisions relating to the reimbursement of defense and settlement costs, interpretation of a "lot or batch" provision and an anti-assignment clause, and the applicability of pollution exclusions to drywall-related claims. It also discusses emerging statutory law relating to coverage for faulty workmanship under general liability policies, and interpretation of the Class Action Fairness Act. This month, we also summarize recent rulings relating to the allocation of authority between courts and arbitration panels, and the recovery of e-discovery costs under federal statutory law. Please "click through" to view articles of interest.

- ***Policyholder Who Rejects Insurer's Offer to Defend Not Entitled to Defense Cost Reimbursement***

  A Texas district court ruled that a policyholder was not entitled to reimbursement of the costs of hiring defense counsel after it rejected its insurer's offer to defend subject to a reservation of rights. *Downhole Navigator, L.L.C. v. Nautilus Ins. Co.*, No. 4:10-0695 (S.D. Tex. May 9, 2011). *Click here for full article*.

- ***Recently-Enacted South Carolina Statute Defines "Occurrence" to Include Damage Resulting from Faulty Workmanship***

  South Carolina passed legislation abrogating prior case law and stating that faulty workmanship falls within the scope of the term "occurrence" in commercial general liability policies which insure contractors for liability arising from construction-related work. S.C. CODE ANN. § 38-61-70 (2011). *Click here for full article*.

- ***Delaware Supreme Court Rules That Batch Clause Creates Ambiguity as to Definition of "Occurrence"***

  The Delaware Supreme Court ruled that a "lot or batch" provision in a commercial umbrella liability policy was ambiguous, and therefore that the insurer was required to provide a defense pending a coverage determination. *Conagra Foods, Inc. v. Lexington Ins. Co.*, 2011 WL 1599621 (Del. Apr. 28, 2011). *Click here for full article*.

- ***Loss of Cash Constitutes Property Damage under General Liability Policy, Says Louisiana Appellate Court***

  A Louisiana appellate court ruled that a diminution in bank account funds as a result of fraudulent check cashing constitutes a "loss of use of tangible property" under a general liability policy. *Innovative Hosp. Systems, LLC v. Abe's Grocery*, 2011 WL 1264601 (La. Ct. App. Apr. 6, 2011). *Click here for full article*.

- ***Louisiana Supreme Court Rules That Policy's Anti-Assignment Clause May Bar Post-Loss Assignments***

  The Louisiana Supreme Court ruled that Louisiana public policy does not preclude the inclusion in insurance policies of anti-assignment clauses relating to post-loss assignments, so long as the policy language is clear and unambiguous. *In re Katrina Canal Breaches Litig.*, 2011 WL 1774330 (La. May 10, 2011). *Click here for full article*.

- ***Federal Courts Issue Mixed Decisions on Applicability to Drywall Claims***

  Federal courts in Virginia and Florida have reached conflicting conclusions as to whether a pollution exclusion bars coverage for property damage arising out of defective drywall. *Nationwide Mut. Ins. Co. v. The Overlook, LLC*, 2011 WL 1988396 (E.D. Va. May 13, 2011); *Builders Mutual Ins. Co. v. Parallel Design & Development LLC*, 2011 WL 1988402. *Auto-Owners Ins. Co. v. American Building Materials, Inc.*, 2011 WL 1878236 (M.D. Fla. May 17, 2011). *Click here for full article*.

- ***California Appellate Court Strictly Enforces Insurer's Right to Reimbursement***

  A California appellate court ruled that an insurer may obtain reimbursement of a policy limits settlement from its policyholder even if the insurer entered into the settlement without giving the policyholder a sufficient amount of time to respond to the settlement offer. *American Modern Home Ins. Co. v. Fahmian*, 2011 WL 1334959 (Cal. Ct. App. Apr. 8, 2011). *Click here for full article*.

- ***New York District Court Gives Broad Effect to Arbitration Clause, Requiring Parties to Arbitrate Scope of Arbitration Clause***

  A federal court in New York ruled that the question of whether all reinsurers must participate in arbitration was a decision for the arbitration panel rather than the court. *Munich Reinsurance Am., Inc. v. National Cas. Co.*, 2011 WL 1561067 (S.D.N.Y. Apr. 26, 2011). *Click here for full article*.

- ***Ninth Circuit Rules That Joined Counterclaim Defendant Does Not Have Standing to Remove Case to Federal Court under Class Action Fairness Act***

  The Ninth Circuit ruled that the CAFA does not allow a party joined to an action as a counterclaim defendant to remove the case to federal court, reasoning that the term "defendant" means only the original defendant. *Westwood Apex v. Contreras*, 2011 WL 1744960 (9th Cir. May 2, 2011). *Click here for full article*.

- ***Defective Removal Notice Does Not Require Remand, Says Tenth Circuit***

  The Tenth Circuit ruled that a procedural defect in defendants' joint notice of removal did not require a remand of the case to state court. *Countryman v. Farmers Ins. Exchange*, 2011 WL 1760196 (10th Cir. May 4, 2011). *Click here for full article*.

- ***Pennsylvania District Court Awards Costs of Electronic Discovery to Prevailing Defendants***

  A federal court in Pennsylvania ruled that various e-discovery costs were recoverable under of 28 U.S.C. § 1920. *Race Tires America, Inc. v. Hoosier Racing Tire Corp.*, 2011 WL 1748620 (W.D. Pa. May 6, 2011). *Click here for full article*.

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Defense Alert:

Policyholder Who Rejects Insurer's Offer to Defend Not Entitled to Defense Cost Reimbursement

On May 9, 2011, a Texas district court ruled that a policyholder was not entitled to reimbursement of the costs of hiring defense counsel after it rejected its insurer's offer to defend subject to a reservation of rights. *Downhole Navigator, L.L.C. v. Nautilus Ins. Co.*, No. 4:10-0695 (S.D. Tex. May 9, 2011). The court reasoned that because there was no conflict of interest, Texas law did not require the insurer to fund the policyholder's choice of counsel.

After being sued in a negligence action, Downhole Navigator sought a defense from Nautilus, its general liability insurer. When Nautilus agreed to defend subject to a reservation of rights, Downhole rejected Nautilus's offer, claiming that the reservation of rights created a conflict with respect to the selection of counsel, thereby forcing Downhole to retain its own representation. In subsequent coverage litigation, the parties filed cross motions relating to Nautilus's duty to reimburse the cost of Downhole's independent counsel. The court awarded summary judgment to Nautilus.

Under Texas law, a policyholder is entitled to conduct its own defense when there is a conflict of interest between the insurer's duty to defend and its interest in avoiding coverage. No such conflict existed here, however, because as the he court explained, "[n]o finding in the [underlying] suit will control the outcome of the coverage issue." The underlying case turned on a finding of negligence, whereas the coverage issues, as framed by the reservation of rights letter, pertained primarily to the scope of various exclusions, including a professional services exclusion.

Downhole illustrates the narrowness of the conflict of interest exception to the general rule allowing an insurer to control its policyholder's defense. A

reservation of rights letter, without more, is unlikely to substantiate allegations of a conflict of interest absent a showing that the facts to be tried in the underlying case will bear directly on the ultimate issue of insurance coverage. This lesson finds further support in another recent decision, *Travelers Prop. v. Centex Homes*, 2011 WL 1225982 (N.D. Cal. Apr. 1, 2011). There, the court ruled that because the insurer's reservation of rights did not create a conflict of interest, the policyholder breached its duty to cooperate by refusing to accept insurer-appointed counsel, thereby forfeiting its right to a defense and indemnification.

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Coverage Alerts:

Recently-Enacted South Carolina Statute Defines "Occurrence" to Include Damage Resulting from Faulty Workmanship

In several previous Alerts, we have summarized decisions analyzing the question of whether faulty workmanship constitutes an "occurrence" under general liability policies. In February 2011, we highlighted a South Carolina Supreme Court decision holding that faulty workmanship was not an "occurrence" where the resulting damage was the natural and probable consequence of the negligence. *Crossman Communities of North Carolina v. Harleysville Mutual Ins. Co.*, 2011 WL 93716 (S.C. Jan 7, 2011). On May 17, 2011, South Carolina passed legislation abrogating the *Crossman* decision and stating that commercial general liability policies which insure a contractor for liability arising from construction-related work "shall contain or be deemed to contain a definition of 'occurrence' that includes … property damage or bodily injury resulting from faulty workmanship, exclusive of the faulty workmanship itself." S.C. CODE ANN. § 38-61-70 (2011). The statute, which applies to current and future coverage litigation, does not limit the exclusions from coverage that an insurer may include in a general liability policy. Similar legislation has been passed in Arkansas and Colorado, and is under consideration in Hawaii.

Delaware Supreme Court Rules That Batch Clause Creates Ambiguity as to Definition of "Occurrence"

The Delaware Supreme Court ruled that a "lot or batch" provision in a commercial umbrella liability policy created ambiguity because it defined the term "occurrence" differently than another section of the policy. In light of this ambiguity, the insurer was required to provide a defense pending a coverage determination. *Conagra Foods, Inc. v. Lexington Ins. Co.*, 2011 WL 1599621 (Del. Apr. 28, 2011).

The coverage dispute arose out of injuries caused by contaminated peanut butter manufactured by the policyholder, ConAgra. Lexington denied a defense on the ground that ConAgra had not met its retained limit for coverage under the "lot or batch" clause, which defines a batch as "a single production run at a single facility not to exceed a 7 day period" and states that all injury arising out of one batch constitutes one occurrence. The trial court held that because ConAgra had not exhausted the $5 million retained limit for any one batch (i.e., products produced over a seven day period), Lexington had no duty to defend.

The Delaware Supreme Court reversed, finding that the trial court failed to consider an alternate and equally reasonable interpretation of the policy which would trigger Lexington's defense obligations. Under the general liability provision of the policy, "occurrence" is defined as "an accident, including continuous or repeated exposure to substantially the same general harmful conditions." Under this provision, ConAgra need only satisfy a retained limit of $3 million/per occurrence. The court held that the competing presence of the "lot and batch" clause and the general liability "occurrence" definition created an ambiguity which must be resolved in favor of the policyholder for purposes of the duty to defend.

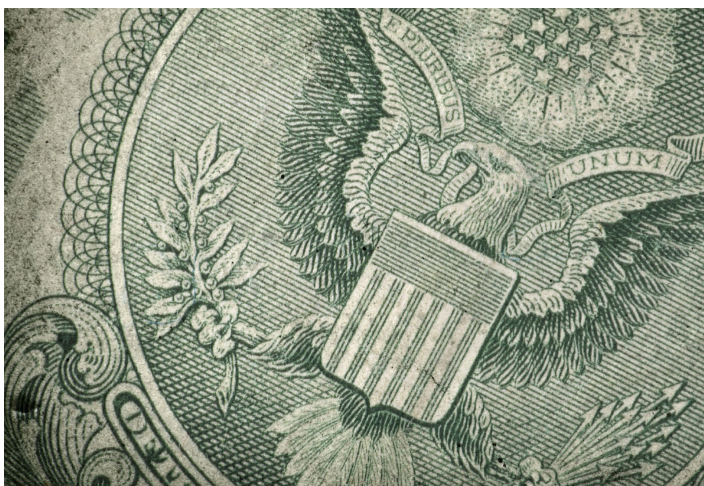
The central issue in *ConAgra*—interpretation of the term "occurrence" in connection with a "lot or batch" clause—has arisen in other bodily injury contexts, with conflicting results. Some courts have interpreted the clause to expand coverage by reducing a policyholder's deductible obligation, reasoning that the clause allows aggregation of multiple occurrences which arise from a single lot, but does not allow a single continuous occurrence to be divided up into multiple occurrences corresponding to seven-day intervals. However, batch clauses have also been interpreted in a manner that limits coverage, by precluding a policyholder from treating large numbers of personal injury claims as a single occurrence for purposes of implicating only

one deductible. While the Delaware Supreme Court's decision represents a victory for the policyholder on the duty to defend, it remains to be seen whether Lexington will be required to indemnify ConAgra—an issue that was remanded to the trial court.

Loss of Cash Constitutes Property Damage under General Liability Policy, Says Louisiana Appellate Court

A Louisiana appellate court ruled that a diminution in an account holder's bank account funds as a result of fraudulent check cashing constitutes a "loss of use of tangible property" under a general liability policy issued to the store that cashed the checks. *Innovative Hosp. Systems, LLC v. Abe's Grocery*, 2011 WL 1264601 (La. Ct. App. Apr. 6, 2011). The court reasoned that where cash is paid in exchange for a counterfeit check, the loss of cash to the account holder is tangible, and therefore within the scope of the term "property damage," defined as the "[l]oss of use of tangible property that is not physically injured."

This decision appears to cut against the weight of authority holding that economic losses do not constitute a loss of use of tangible property. Although numerous courts have held that a diminution in value may serve as a measure of damages for loss of use of tangible property, courts have generally held that an economic loss standing alone does not meet this test. *See, e.g., Generali-U.S. Branch v. Alexander*, 87 P.3d 1000 (Mont. 2004) (Complaint seeking compensation for lost payments did not allege "property damage" under general liability policy.); *Acuity v. City Concrete L.L.C.*, 2006 WL 2987717 (N.D. Ohio Oct. 17, 2006) ("[E]conomic losses do not fit the definition of property damage in the GCL policy because they are not physical injuries to tangible property.").



Louisiana Supreme Court Rules That Policy's Anti-Assignment Clause May Bar Post-Loss Assignments

Answering a question certified by the Fifth Circuit, the Louisiana Supreme Court ruled that Louisiana public policy does not preclude anti-assignment insurance clauses relating to post-loss assignments, so long as the policy language is clear and unambiguous. *In re Katrina Canal Breaches Litig.*, 2011 WL 1774330 (La. May 10, 2011).

As the Louisiana Supreme Court observed, a significant number of courts nationwide have held that even where a policy contains an anti-assignment clause, coverage for losses that have already occurred may be transferred to another company. These courts have distinguished pre-loss from post-loss assignments, reasoning that:

> [A]llowing an insured to assign the right to coverage (pre-loss) would force the insurer to protect an insured with whom it had not contracted—an insured who might present a greater level of risk than the policyholder. However, allowing an insured to assign its right to the proceeds of an insurance policy (post-loss) does not modify the insurer's risk. The insurer's obligations are fixed at the time the loss occurs, and … [t]his obligation is not altered when the claimant is not the party who was originally insured.

Although the Louisiana Supreme Court recognized the pre/post loss distinction, it held that parties were free to contractually prohibit both types of assignments for insurance proceeds. In order to prohibit post-loss assignments, however, the policy language must be explicit and unambiguous in its intent. Generalized anti-assignment provisions which prevent the assignment of the policy itself or assignment of an interest in the policy do not suffice to effectuate a ban on post-loss assignments. Although the court declined to formulate a specific test, it emphasized that policy language must be "clear and explicit" and evaluated on a policy-by-policy basis. It remains to be seen whether other courts, even those that have allowed post-loss assignments in the face of a generalized anti-assignment clause, will follow *In re Katrina* and enforce contractual provisions which specifically and explicitly bar post-loss assignments.

Pollution Exclusion Alert:

Federal Courts Issue Mixed Decisions on Applicability to Drywall Claims

In our May 2011 Alert, we noted that drywall coverage decisions were likely forthcoming in two cases pending in Virginia and Florida. Decisions have been issued in both cases and a third case, with conflicting results.

In *Nationwide Mut. Ins. Co. v. The Overlook, LLC*, No. 4:10cv69 (E.D. Va. Apr. 12, 2011), a Virginia district court had certified to the Virginia Supreme Court the question of whether a pollution exclusion was ambiguous in the context of drywall-related claims. On April 22, 2011, the Supreme Court of Virginia declined to accept the certified question, leaving the issue for district court resolution. On May 13, 2011, the district court granted partial summary judgment to Nationwide Mutual Insurance Company, ruling that the insurer had no duty to defend or indemnify a real estate developer in an underlying lawsuit brought by a homeowner alleging property damage and injuries caused by defective drywall. *Nationwide Mut. Ins. Co. v. The Overlook, LLC*, 2011 WL 1988396 (E.D. Va. May 13, 2011).

The court held that the pollution exclusion in all applicable policies squarely applied and precluded any possibility of coverage for the homeowner's drywall-related claims. The court emphasized that the pollution exclusion barred coverage for *all* underlying claims—including statutory consumer protection claims and claims of misrepresentation and failure to warn, even if such claims do not specifically allege facts relating to off-gassing of toxic chemicals. As the court explained, every claim in the complaint "implicates the defective drywall as either the basis for the claim, or the cause of the resulting damages. Thus, every claim implicates the pollution exclusion." *Overlook* is the second decision to hold that Virginia law does not limit pollution exclusions to traditional environmental contamination and applies to drywall-related claims. *See Travco Ins. Co. v. Ward*, 715 F. Supp.2d 699 (E.D. Va. 2010).

Addressing the same issue, another Virginia district court reached the opposite conclusion. *In Builders*

Mutual Ins. Co. v. Parallel Design & Development LLC, 2011 WL 1988402 (E.D. Va. May 13, 2011), the court held that a total pollution exclusion in a general liability policy was ambiguous, and must therefore be construed against the insurer for purposes of the insurer's duty to defend. Here, the applicable pollution exclusion was included in the policy via an endorsement, which replaced a previous pollution exclusion contained in the body of the policy. Although the original exclusion defined the term "pollutants," the endorsement did not. The court concluded that the absence of a definition for the term "pollutants" created an ambiguity as to whether the exclusion applied only to "traditional outdoor environmental" contamination, or to indoor drywall-related claims as well. In reaching its decision, the court declined to consider evidence submitted by Builders Mutual demonstrating that subsequent insurance policies between the parties defined "pollutants" in a manner that has been interpreted to encompass drywall-related claims. *Builders Mutual*—which cuts against two other Virginia decisions issued in this context—is a ruling that was driven by the particular facts at issue (namely, the undefined term "pollutants"). Where the term "pollutants" is defined, the *Builders Mutual* ruling will likely have little impact. However, the decision serves as a reminder that endorsement language should be carefully and thoroughly drafted, particularly where it replaces previous policy language, as courts may be unwilling to consider the latter in interpreting the former.

A Florida district court also weighed in on this issue in *Auto-Owners Ins. Co. v. American Building Materials, Inc.*, 2011 WL 1878236 (M.D. Fla. May 17, 2011). There, the court held that a pollution exclusion in a general liability policy did not preclude coverage for drywall-related property damage claims. The exclusion at issue barred coverage for damage arising out of the release of pollutants "[a]t or from any premises, site or location on which any insured or any contractors or subcontractors working directly or indirectly on any insured's behalf are performing operations." The court held the phrase "performing operations" rendered the exclusion applicable to claims arising at the time the work was being performed. Citing to an Alabama decision construing identical policy language, the court explained, "the plain language of the Pollution Exclusion limits its reach to pollutant releases at locations where the insured contemporaneously performs operations, rather than pollutant releases at locations where the insured performed operations … earlier." Because it was undisputed that the operations of the policyholder (a materials supplier) were complete at the time the drywall was delivered, and that the property damage did not occur until sometime thereafter, the court concluded that the pollution exclusion did not apply. Notably, the *Auto-Owners* ruling was based exclusively on the particular temporally-limiting language in the exclusion at issue (rather than on the meaning of the term "pollutants" or the scope of the pollution exclusion in general), and its impact on other drywall coverage cases may be limited.

Settlement Alert:

California Appellate Court Strictly Enforces Insurer's Right to Reimbursement

In previous Alerts, we have discussed an insurer's right to reimbursement of defense and/or settlement costs from a policyholder following a determination that there is no coverage under the policy. Although law in this context varies by jurisdiction, California law is clear in providing a right to reimbursement for insurers that have reserved the option of recovering such monies from their policyholders. A recent California decision gives broad effect to this principle, holding that an insurer may obtain reimbursement of a policy limits settlement from its policyholder even if the insurer entered into the settlement without giving the policyholder a sufficient amount of time to respond to the settlement offer. *American Modern Home Ins. Co. v. Fahmian*, 2011 WL 1334959 (Cal. Ct. App. Apr. 8, 2011).

The policyholder tendered his defense of a

personal injury claim to his homeowners insurer. The insurer agreed to defend subject to a reservation of rights. After evaluating the merits of the case, the insurer determined that a policy limits settlement was reasonable. The insurer notified the policyholder of its intent to settle unless the policyholder was willing to assume his own defense or waive any bad faith claims against the insurer for failure to settle. The policyholder did not respond. The insurer then settled the action and sought reimbursement from the policyholder. A lawsuit ensued, and the jury determined that (1) there was no coverage under the policy, and (2) the policyholder did not have sufficient time to reply to the insurer's settlement notification letter. In light of the latter finding, the trial court denied the insurer's request for reimbursement. The appellate court reversed.

The appellate court ruled that an insurer may obtain reimbursement from its policyholder for a policy limits settlement where a claim is determined to be outside the scope of policy coverage so long as the insurer reserved the right to do so, notified the policyholder of its intent to settle, and offered the policyholder the opportunity to assume its own defense. Because each of these requirements was satisfied here, the insurer's right to reimbursement was clear cut. In so ruling, the appellate court noted the trial court's error in imposing an additional reasonable-time-to-respond requirement. The appellate court held that the brief amount of time between the policyholder's receipt of the settlement-notification letter and the insurer's execution of the settlement agreement (only a few days) did not alter this conclusion. The appellate court observed, "a plaintiff's settlement offer might come at any time and usually contains its own time limits; therefore, a defendant and its insurer might have little or no control over the deadline to respond to that offer."

Fahmian reinforces California's strict enforcement of an insurer's right to reimbursement in the wake of a no coverage finding. However, the decision also suggests that it is sensible for insurers to timely notify policyholders of settlement offers after receiving demands from underlying plaintiffs. The court counseled that an express and "timely provision of a settlement advisement letter to the insured, after receiving the plaintiff's settlement demand" is a predicate to reimbursement.

Arbitration Alert:

New York District Court Gives Broad Effect to Arbitration Clause, Requiring Parties to Arbitrate Scope of Arbitration Clause

In recent years, courts have frequently been called upon to address the allocation of authority between courts and arbitrators. In particular, parties have disputed whether certain ancillary issues (aside from the substantive legal claims themselves) should be decided by an arbitration panel or by a court. Areas that have proven particularly tricky are those that fall somewhere in between the procedural/substantive distinction, such as the availability of class action arbitrations or the appropriateness of consolidating arbitrations. Another such dispute, one of first impression in New York, was raised in *Munich Reinsurance Am., Inc. v. National Cas. Co.*, 2011 WL 1561067 (S.D.N.Y. Apr. 26, 2011). There, the question presented was whether an arbitration

provision in a multi-party reinsurance treaty which stated that all reinsurers must "act as one party," required all reinsurers to participate in arbitration or whether arbitration could proceed in the absence of one reinsurer. Rather than answering this question itself, the court ruled that the question was one of contract interpretation and was thus for arbitrators to resolve. In reaching its decision, the court categorized the dispute as "procedural," analogizing it to disputes over whether arbitrations can be consolidated—an issue which several federal courts have relegated to arbitration panels.

Class Action Alerts:

Ninth Circuit Rules That Joined Counterclaim Defendant Does Not Have Standing to Remove Case to Federal Court under Class Action Fairness Act

In previous Alerts, we have reported on the proliferation of insurance-related class action suits. In such cases, the availability of a federal forum may be a critical factor for defendant insurers, given the often cited perception of bias among certain state courts in favor of local plaintiff classes. The passage of the Class Action Fairness Act ("CAFA") in 2005 widened the net of cases satisfying federal jurisdiction by relaxing the standards for diversity in cases involving more than 100 class members and an amount in controversy exceeding $5 million. Although applicable across the board, CAFA has particular significance in the insurance context because insurance claims often involve small amounts at stake for a large number of individual class members, which could fail to satisfy the requirements under the traditional diversity statute.

Since its enactment, circuit courts have been called up to interpret CAFA in various contexts. As reported in our September 2010 and November 2010 Alerts, the Eleventh Circuit addressed the amount in controversy requirement under CAFA, initially ruling that CAFA actions require at least one class member to allege an individual amount in controversy over $75,000, but subsequently vacating that decision and holding that the statute did not contain any such requirement. *Cappuccitti v. DirecTV, Inc.*, 623 F.3d 1118 (11th Cir. 2010).

More recently, the Ninth Circuit addressed the scope of CAFA, ruling that the statute does not allow a party joined to an action as a counterclaim defendant to remove the case to federal court. The court reasoned that the term "defendant" means only the original defendant—an interpretation consistent with decisions applying the general removal statute, 28 U.S.C. § 1441. *Westwood Apex v. Contreras*, 2011 WL 1744960 (9th Cir. May 2, 2011). The only other federal circuit court to have addressed this issue, the Fourth Circuit, reached the same conclusion. *See Palisades Collections, LLC v. Shorts*, 552 F.3d 327 (4th Cir. 2008).

Defective Removal Notice Does Not Require Remand, Says Tenth Circuit

Reversing a Colorado district court decision, the Tenth Circuit ruled that a procedural defect in defendants' joint notice of removal did not require a remand of the case to state court. *Countryman v. Farmers Ins. Exchange*, 2011 WL 1760196 (10th Cir. May 4, 2011). Plaintiffs filed a putative class action in Colorado state court alleging that the defendant insurers violated state insurance statues by refusing to pay reasonable medical expenses on automobile insurance policies. The insurers filed a joint notice of removal pursuant to CAFA within the thirty-day removal period. However, defendants inadvertently failed to include a copy of the summons served on one of the insurer defendants. This defect was cured with a supplemental filing shortly after the expiration of the thirty-day removal period. Nonetheless, the district court granted plaintiffs' motion to remand, relying on Colorado precedent holding that "a removing party's failure to adhere strictly to the unequivocal language of [the removal statute] by not including every document

served on the removing party constitute[s] a 'fatal defect' in removal procedure." The Tenth Circuit reversed. The insurers' failure to attach the summons was a *de minimis* procedural defect—and a readily curable one—that did not necessitate remand, the court held. Although Colorado decisions are not unanimous in this context, *Countryman* aligns itself with the majority of cases holding that a removing party's failure to attach the required documents to a removal notice is a curable procedural defect, rather than a fatal jurisdictional deficiency requiring remand.

Discovery Alert:

Pennsylvania District Court Awards Costs of Electronic Discovery to Prevailing Defendants

In *Race Tires America, Inc. v. Hoosier Racing Tire Corp.*, 2011 WL 1748620 (W.D. Pa. May 6, 2011), a federal Pennsylvania court addressed whether costs associated with the production of e-discovery fall within the scope of 28 U.S.C. § 1920. Section 1920 allows the assessment of costs against a losing party for, among other things, "[f]ees for exemplification and the costs of making copies of any materials where the copies are necessarily obtained for use in the case." The central issue was "how to apply these § 1920 terms to the world of electronically stored information." Endorsing a broad view of the statute, the court concluded that the following e-discovery-related costs were recoverable under § 1920: the creation of a litigation database; the scanning of documents to create electronic images; the processing and indexing of e-discovery data; the extraction of metadata fields from electronic records; and the creation of searchable and other specifically requested formats.

Although the Third Circuit has not squarely addressed this issue, *Race Tires* cited numerous opinions from other circuits in which courts have likewise awarded costs relating to the production of e-discovery (including the cost of scanning, imaging, converting and compiling electronic information). However, *Race Tires* also acknowledged several decisions in which courts have rejected requests for e-discovery costs, finding that particular tasks performed (such as converting files into searchable formats or more readable formats) were not analogous to the expenses set forth in §1920.

There appear to be no bright line rules to determine whether e-discovery costs are awardable under §1920. Rather, courts appear willing to draw fine lines in deciding whether a particular e-discovery task is the "electronic equivalent[] of exemplification and copying" and thus within the scope of the statute. Overall, resolution of disputes in this context are likely to depend on several case-specific factors, including (1) whether parties have executed a stipulation that requires production of e-discovery in certain formats (this was the case in *Race Tires*, and a factor that the court repeatedly emphasized); (2) whether costs arose from a technical task (which is more likely to be considered a § 1920 "cost"), as opposed to a "legal" task (such as document review and retrieval) traditionally conducted by attorneys or paralegals (which is less likely to be considered a § 1920 "cost"); (3) whether the costs were necessary or merely for convenience of counsel; and (4) the reasonableness of fees. The *Race Tires* decision is currently on appeal to the Third Circuit. We will monitor this and other cases and keep you apprised of noteworthy rulings in this context.

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