SIMPSON THACHER

INSURANCE LAW ALERT

MARCH 2012

This month's Alert discusses decisions relating to pro rata allocation, the interpretation of unambiguous policy provisions, and an insurer's duty to defend CERCLA-related agency directives. We also address decisions interpreting the scope of "bodily injury" and "advertising injury" in general liability policies. In addition, we summarize two recent appellate decisions in the arbitration and bankruptcy contexts. Finally, we highlight Simpson Thacher's involvement in upcoming insurance events and the Firm's recent summary judgment victory in a Wisconsin insurance litigation. Please "click through" to view articles of interest.

- ***Fourth Circuit Upholds Pro Rata Allocation for Lead Poisoning Suit***

  Applying Maryland law, the Fourth Circuit held that an insurer was required to indemnify only a pro rata portion of a judgment against its policyholder, notwithstanding that the policyholder was held jointly and severally liable for the entire judgment in the underlying lead paint-related lawsuit. *Pennsylvania Nat'l Mut. Cas. Ins. Co. v. Roberts*, 2012 WL 336150 (4th Cir. Feb. 3, 2012). *Click here for full article*

- ***New York Court of Appeals Rejects Attempt to Create Ambiguity in Policy Provision***

  The New York Court of Appeals held that Federal Insurance Company had no obligation to indemnify a settlement payment made by IBM Corporation because the settled claims were outside the scope of the operative coverage. *Federal Ins. Co. v. Int'l Business Machines Corp.*, 2012 WL 538241 (N.Y. Feb. 21, 2012). *Click here for full article*

- ***Environmental Agency Notifications Constitute a "Suit" Triggering Duty to Defend, Says Oregon Court***

  Interpreting a state statute, an Oregon court ruled that federal and local environmental agencies' communications to a policyholder relating to CERCLA liability constituted a "suit" for purposes of triggering general liability insurers' defense obligations. *Century Indem. Co. v. Marine Grp., LLC*, 2012 WL 259988 (D. Or. Jan. 27, 2012). *Click here for full article*

- ***Class Action Suit Against Nutritional Supplements Manufacturer Does Not Allege "Bodily Injury," Says Texas Court***

  A Texas court ruled that an insurance company had no duty to defend claims of false advertising and deceptive practices against a drug manufacturer because the complaint did not allege "bodily injury" within the meaning of the insurance policy. *CSA Nutraceuticals GP, LLC v. Chubb Custom Ins. Co.*, No. 3:10-CV-02155-F (N.D. Tex. Jan. 30, 2012). *Click here for full article*

- ***Second Circuit Reverses Vacatur of Arbitration Award, Finding No Basis for Disqualifying Arbitrators***

  The Second Circuit reversed a lower court ruling vacating an arbitration award in a reinsurance dispute and found that two arbitrators should not be disqualified for "evident partiality." *Scandinavian Reinsurance Co. Ltd. v. St. Paul Fire & Marine Ins. Co.*, 2012 WL 335772 (2d Cir. Feb. 3, 2012). *Click here for full article*

- ***California Court Requires General Liability Insurer to Defend Mattel Suit Pursuant to Advertising Injury Provision***

  In a dispute arising out of the longstanding Bratz doll litigation, a California federal court ruled that allegations of misappropriation against MGA Entertainment fell within the scope of a general liability policy's advertising injury provision, and therefore that the insurer had a duty to defend the claims. *MGA Entm't, Inc. v. Hartford Ins. Grp.*, No. ED CV 08-0457 (C.D. Cal. Jan. 27, 2012). *Click here for full article*

- ***Simpson Thacher Wins Summary Judgment for Insurers***

  A Wisconsin court awarded partial summary judgment to Simpson Thacher clients AIU Insurance Company, Lexington Insurance Company and National Union Fire Insurance Company of Pittsburgh, PA in litigation brought by The Coca-Cola Company and Cleaver Brooks, Inc. *Cleaver-Brooks, Inc. v. AIU Ins. Co.*, No. 11CV10292 (Wis. Cir. Ct. Milwaukee County Feb. 21, 2012). *Click here for full article*

- ***New Jersey Court Denies Debtor's Claims for Insurance Proceeds from Liquidated Insurer***

  A New Jersey appellate court affirmed the denial of claims for insurance proceeds that W.R. Grace & Co. contended were owed by a liquidated insurer on account of asbestos claims filed in Grace's bankruptcy case. *Comm'r of Ins. v. Integrity Ins. Co./W.R. Grace & Co.*, 2012 WL 75097 (N.J. Super. Ct. App. Div. Jan. 11, 2012). *Click here for full article*

- ***STB News Alerts***

  Click here for information on Simpson Thacher's involvement in insurance-related organizations and events.

Allocation Alert:

Fourth Circuit Upholds Pro Rata Allocation for Lead Poisoning Suit

Applying Maryland law, the Fourth Circuit held that an insurer was required to indemnify only a pro rata portion of a judgment against its policyholder, notwithstanding that the policyholder was held jointly and severally liable for the entire judgment in the underlying lead paint-related lawsuit. *Pennsylvania Nat'l Mut. Cas. Ins. Co. v. Roberts*, 2012 WL 336150 (4th Cir. Feb. 3, 2012). The court explained that the insurer's indemnification obligations were determined solely by the policy language—which limited coverage to injury or damage that occurred "during the policy period"—and not by reference to the theory of tort liability in the underlying litigation. In addition, the court held that a pro rata approach was appropriate even though the underlying litigation involved multiple tortfeasors. The court stated: "[t]here is nothing in Maryland law to indicate it would abandon the pro rata approach and commitment to contractual language when multiple tortfeasors are involved." Although some jurisdictions apply a "joint and several" approach to allocating indemnity costs, Maryland, like the majority of other jurisdictions, follows a pro rata approach to allocation. *See* September 2011 Alert (pro rata allocation under Minnesota law); October 2011 Alert (pro rata allocation under Vermont law); January 2012 Alert (pro rata allocation under New York law).

The court also sided with the insurer on two related issues. First, the court held that the starting point for allocation was the birth date of the child who suffered lead poisoning injuries. The tort plaintiff urged the use of a later start date, which would have resulted in a larger insurance recovery. Rejecting this argument, the court noted the plaintiff had "changed her tune" by arguing in the underlying trial that the injuries began at birth, but then arguing in the insurance litigation that the injuries did not occur until later. Second, the court held the insurer responsible for a twenty-two month period of coverage, rather than a twenty-four month period, based on the policyholder's sale of the property two months before the policy's expiration. Under the terms of the policy, coverage extended only to premises owned, rented, or occupied by the original policyholder. In addition, the policy contained a non-assignment clause, prohibiting the transfer of coverage without written consent of the insurance company. In light of these two provisions, the court concluded that coverage had terminated upon the sale of the property.

This edition of the Insurance Law Alert was prepared by Mary Beth Forshaw (mforshaw@stblaw.com/212-455-2846) and Michael D. Kibler (mkibler@stblaw.com/310-407-7515).

POLICY CONSTRUCTION ALERT:

New York Court of Appeals Rejects Attempt to Create Ambiguity in Policy Provision

Affirming an appellate court decision, the New York Court of Appeals held that Federal Insurance Company had no obligation to indemnify a settlement payment made by IBM Corporation because the settled claims were outside the scope of the operative coverage. *Federal Ins. Co. v. Int'l Business Machines Corp.*, 2012 WL 538241 (N.Y. Feb. 21, 2012).

The underlying complaint alleged that certain amendments to IBM's benefit plans violated ERISA. IBM ultimately settled the action and sought reimbursement from Federal, its excess insurer. Federal argued that its policy did not provide coverage because the claims against IBM were outside the scope of the policy's "Wrongful Act" provision. The policy defined a "Wrongful Act" as "any breach of the responsibilities, obligations or duties by an Insured which are imposed upon a fiduciary of a Benefit Program by [ERISA]." Federal argued that this provision provides coverage only where IBM is acting as an ERISA fiduciary. Because the underlying complaint did not allege that IBM acted in this role, the court held that the provision did not apply. In so ruling, the court rejected IBM's argument that the undefined term "fiduciary" in the policy should be given its plain, ordinary meaning, rather than the specific meaning associated with an ERISA fiduciary.

Federal provides strong support for insurers defending against claims of ambiguity. The court rejected the notion that subsequent policy language revisions indicate prior ambiguity. ("Because the [ ] policy is sufficiently clear on its face, we decline to speculate about Federal's choice to revise its own policy."). The court also refused to find ambiguity on the basis that policy language could arguably have been clearer in expressing the parties' intent, noting:

> It is simply not the case that because the challenged provision could have been worded differently, it is ambiguous and must be construed in IBM's favor. There are often many ways of effectively conveying the same meaning and the question is not simply whether the insurer could have phrased the provision differently. Rather, the issue is, in light of the reasonable expectations of the average policyholder, whether the provision, as written, is sufficiently clear and precise such that there is no room for reasonable disagreement about the scope of coverage.

DEFENSE ALERT:

Environmental Agency Notifications Constitute a "Suit" Triggering Duty to Defend, Says Oregon Court

Interpreting the definition of "suit" contained in an Oregon environmental statute, an Oregon district court ruled that federal and local environmental agencies' communications to a policyholder relating to

CERCLA liability constituted a "suit" for purposes of general liability insurers' defense obligations. *Century Indem. Co. v. Marine Grp., LLC*, 2012 WL 259988 (D. Or. Jan. 27, 2012).

Over a two-year period, the EPA and a local environmental agency exchanged communications with the policyholder relating to its potential liability for CERCLA response costs. The correspondence notified the policyholder of the investigation of a certain site, requested information, and ultimately identified the policyholder as a potentially responsible party with respect to clean up costs. The policyholder, in turn, sought defense and indemnification from its insurers. The insurers denied a defense, arguing that there was no "suit" that triggered their defense obligations.

Citing to the Oregon Environmental Cleanup Assistance Act, the court concluded that the correspondence at issue constituted a "suit." Under the statute, "suit" in a general liability policy is deemed to include administrative proceedings and actions, and encompasses an "action or agreement" by the EPA that "directs, requests or agrees that an insured take action with respect to contamination." Or. Rev. Stat. 465.480(1)(a), (2)(b) (2009). The court concluded that the totality of the agency communications—which alleged potential liability under CERCLA and directed the policyholder to participate in the allocation of liability and damages—imposed legal obligations upon the policyholder which "combined to achieve the [ ] 'suit' equivalent."

Significantly, the Oregon statute allows for parties to agree contractually to a more restrictive definition of "suit," stating that the statutory definition "do[es] not apply if the application of the rule results in an interpretation contrary to the intent of the parties." Or. Rev. Stat. 465.480(7). Parties seeking to benefit from this exclusion are advised to draft clear and explicit language given Oregon's broad interpretation of the term "suit" in *Century Indemnity* and other analogous cases.

Coverage Alert:

Class Action Suit Against Nutritional Supplements Manufacturer Does Not Allege "Bodily Injury," Says Texas Court

A federal court in Texas ruled that an insurance company had no duty to defend claims of false advertising and deceptive practices against a drug manufacturer because the complaint did not allege "bodily injury" within the meaning of the insurance policy. *CSA Nutraceuticals GP, LLC v. Chubb Custom Ins. Co.*, No. 3:10-CV-02155-F (N.D. Tex. Jan. 30, 2012).

In the underlying suit, plaintiffs alleged that CSA engaged in false and misleading advertising and business practices in order to induce plaintiffs to purchase a diet supplement, leading to plaintiffs' economic loss. Plaintiffs sought monetary damages and/or restitution of CSA's "wrongfully earned profits." Chubb argued, and the court agreed, that such allegations fell outside the scope of "bodily injury." The court explained that the crux of the complaint was that plaintiffs were deceived into purchasing CSA's products and thus financially harmed—not that plaintiffs suffered any bodily harm as a result of using the products. In addition, the court held that even assuming the complaint could be construed to

allege mental anguish, such emotional injury, standing alone, would be insufficient to establish "bodily injury" under the terms of the policy and applicable state law.

CSA Nutraceuticals comports with other decisions holding that allegations of economic harm (even where arising from an allegedly harmful product) do not constitute "bodily injury" for the purposes of insurance coverage. *See Medmarc Cas. Ins. Co. v. Avent Am., Inc.*, 612 F.3d 607 (7th Cir. 2010) (general liability insurer had no duty to defend class action suit alleging baby bottle contamination because suit sought economic damages based on loss of use, rather than bodily injury) (discussed in September 2010 Alert).

Arbitration Alert:

Second Circuit Reverses Vacatur of Arbitration Award, Finding No Basis for Disqualifying Arbitrators

In our April 2010 Alert, we discussed a New York district court ruling vacating an arbitration award in a reinsurance dispute on the basis that two arbitrators were disqualified for "evident partiality." *Scandinavian Reinsurance Co. Ltd. v. St. Paul Fire & Marine Ins. Co.*, 732 F. Supp. 2d 293 (S.D.N.Y. 2010). Last month, the Second Circuit reversed the ruling. The Second Circuit found no basis for disqualifying the arbitrators and remanded the case with instructions to confirm the arbitral award. *Scandinavian Reinsurance Co. Ltd. v. St. Paul Fire & Marine Ins. Co.*, 2012 WL 335772 (2d Cir. Feb. 3, 2012).

The district court held that disqualification was warranted because two members of an arbitration panel had failed to disclose their simultaneous participation in an arbitration involving similar legal issues, a common witness and a party with significant business ties to one of the parties in the instant arbitration. The Second Circuit disagreed, finding that the arbitrators' overlapping service (and their failure to disclose it) did not, without more, constitute "evident partiality." In so finding, the court distinguished between concurrent arbitral service in two arguably similar proceedings and a more "material relationship," such as a family connection or an ongoing business arrangement with a party or law firm. In addition, the Second Circuit held that none of the other commonalities between the two arbitrations (similar legal issues, a shared witness, and a business relationship between two parties) suggested bias sufficient to warrant disqualification. The court stated: "the fact that one arbitration resembles another in some respects does not suggest to us that an arbitrator presiding in both is somehow therefore likely to be biased in favor of or against any party."

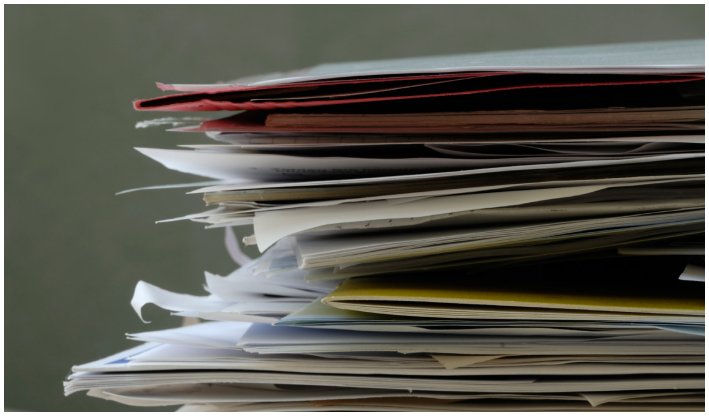
The Second Circuit's ruling illustrates the strong deference afforded to the arbitral process and arbitral awards, and the limited scope of federal court review in this context. Parties seeking to disqualify arbitrators on the basis of "evident partiality" can face a high burden. As the Second Circuit noted, the issue of arbitrator bias turns on case-specific factors, including: (1) the extent and character of the arbitrator's personal and/or pecuniary interest in the proceedings; (2) the directness of the relationship between the arbitrator and the party s/he allegedly favors; (3) the connection of that relationship to the arbitrator; and (4) the temporal proximity of the relationship and the arbitration. Decisions on arbitrator disqualification are far from consistent. In past Alerts, we have discussed numerous rulings on both sides of the fence. *Compare Trustmark Ins. Co. v. John Hancock Life Ins. Co.*, 631 F.3d 869 (7th Cir. 2011) (March 2011 Alert); *Trustmark Ins. Co. v Clarendon Nat'l Ins. Co.*, 2010 WL 431592 (N.D. Ill. Feb. 1, 2010) (March 2010 Alert); *Arrowood Indem. Co. v. Trustmark Ins. Co.*, No. 3:03-CV-1000 (D. Conn. Feb. 2, 2010) (April 2010 Alert) (denying motions to disqualify) *with Benjamin, Weill & Mazer v. Kors*, 116 Cal. Rptr. 3d 677 (1st Dist. 2010), *vacated*, 195 Cal. App. 4th 40 (1st Dist. 2011) (December 2010 Alert); *Alim v. KBR Halliburton*, 2011 WL 61868 (Tex. Ct. App. Jan. 10, 2011) (February 2011 Alert) (granting motions to disqualify).

ADVERTISING ALERT:

California Court Requires General Liability Insurer to Defend Mattel Suit Pursuant to Advertising Injury Provision

In a dispute arising out of the longstanding Bratz doll litigation, a California federal court ruled that allegations of misappropriation against MGA Entertainment fell within the scope of a general liability policy's advertising injury provision, and therefore that the insurer had a duty to defend the claims. *MGA Entm't, Inc. v. Hartford Ins. Grp.*, No. ED CV 08-0457 (C.D. Cal. Jan. 27, 2012).

In the underlying lawsuit, Mattel initially asserted claims of disparagement, trade libel and misrepresentation against MGA Entertainment. In a previous ruling, the court held that such allegations fell within the scope of "advertising injury" under the relevant policies, and thus triggered the insurer's defense obligations. Since this opinion was issued, Mattel filed an amended pleading which eliminated the disparagement and trade libel claims and alleged that MGA Entertainment "targeted and recruited" Mattel employees in order to access confidential and propriety information. MGA Entertainment's insurer argued that because the amended complaint did not include the allegations upon which the court previously relied in finding a duty to defend, the duty to defend no longer existed. The court disagreed. The court held that the amended complaint still contained allegations that gave rise to a duty to defend under the advertising injury provision. In particular, the amended complaint alleged that MGA Entertainment obtained and misappropriated Mattel's marketing and advertising strategies—conduct that fell squarely within an advertising injury provision, the court concluded.



Although the court based its duty to defend ruling primarily on the allegations in the amended complaint, the court also noted that under California law, an insurer's defense obligations may be triggered by extrinsic facts known to the insurer. Here, a previous order constituted such extrinsic evidence, the court reasoned, because the order held that a material issue of fact existed as to whether MGA Entertainment misappropriated Mattel's marketing slogans and advertising campaigns.

In reaching its decision, the court relied on *Hyundai Motor Am. v. Nat'l Union Fire Ins. Co.*, 600 F.3d 1092 (9th Cir. 2010), discussed in our May 2010 Alert. In *Hyundai*, the court interpreted an identically-worded advertising injury provision to trigger defense obligations for a complaint alleging that the insured had misused the claimant's marketing methods.

LITIGATION ALERT:

Simpson Thacher Wins Summary Judgment for Insurers

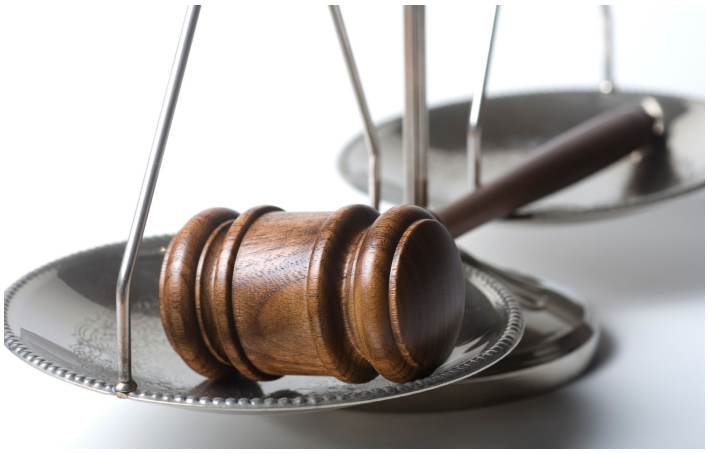
On February 21, 2012, a Wisconsin court awarded partial summary judgment to Simpson Thacher clients AIU Insurance Company, Lexington Insurance Company and National Union Fire Insurance Company of Pittsburgh, PA in litigation brought by The Coca-Cola Company and Cleaver Brooks, Inc. *Cleaver-Brooks, Inc. v. AIU Ins. Co.*, No. 11CV10292 (Wis. Cir. Ct. Milwaukee County Feb. 21, 2012). The court held that a draft settlement agreement was not an enforceable contract, finding that the parties did not intend to be bound by the agreement. In so

ruling, the court held that Simpson Thacher had successfully established that plaintiffs' course of conduct demonstrated that no contract had been formed. In a separate ruling, the court denied Coke and Cleaver Brooks' partial summary judgment motion seeking to enforce a term sheet. The insurers are represented by Simpson Thacher partners Mary Beth Forshaw and Bryce Friedman.

Bankruptcy Alert:

New Jersey Court Denies Debtor's Claims for Insurance Proceeds from Liquidated Insurer

A New Jersey appellate court affirmed the denial of claims for insurance proceeds that W.R. Grace & Co. ("Grace") contended were owed by a liquidated insurer on account of asbestos claims filed in Grace's bankruptcy case. *Comm'r of Ins. v. Integrity Ins. Co./ W.R. Grace & Co.*, 2012 WL 75097 (N.J. Super. Ct. App. Div. Jan. 11, 2012). Grace submitted proofs of claim against the insolvent insurer's liquidator, together with supporting documentation consisting of Grace's plan of reorganization, an estimation of Grace's asbestos liabilities prepared by an expert retained by Grace in connection with its bankruptcy case, and other plan-related submissions. The liquidator denied Grace's claims based on, *inter alia*, a New Jersey statute prohibiting the allowance of contingent claims against an insolvent insurer. *See* N.J. Stat. Ann. 17:30C-28a ("No contingent claim shall share in a distribution of the assets of an [insolvent] insurer" except where "(1) [s]uch claim becomes absolute against the insurer on or before the last day fixed for filing of proofs of claim ….''). A special master agreed with the liquidator, finding it "undisputed that Grace's claims do not have fixed liability, have not been either settled or adjudicated, and thus the amount which Grace will have to pay is not definite or determinable, but



estimated." On appeal, the Superior Court affirmed, holding that there is no precedent to support the proposition that the liquidator should "earmark funds to cover contingent and future claims against Grace—a step that has no statutory support" and would be contrary to New Jersey case law. In so ruling, the court rejected Grace's contention that its claims were not contingent because the identity of the underlying asbestos claimants was known and the claims would have been asserted but for Grace's bankruptcy and the automatic stay. The court held that the value of the claims at issue "has not been fixed by actual payment, settlement, final judgment or a claims resolution procedure approved by the federal bankruptcy court."

STB News Alerts:

On March 3, Mary Kay Vyskocil spoke at the American Bar Association's "Insurance Coverage Litigation Committee CLE Seminar" in Tucson, Arizona. Mary Kay discussed current and emerging reinsurance issues.

On April 24, Bryce Friedman will be speaking at an HB Litigation Conference entitled "Food, Drug and Medical Device Litigation Forum" in Minneapolis, Minnesota. Bryce will participate in a panel discussing the preservation of privilege in the context of insurance litigation arising from food, drug and medical device claims.

Simpson Thacher has been an international leader in the practice of insurance and reinsurance law for more than a quarter of a century. Our insurance litigation team practices worldwide.

Barry R. Ostrager
(212) 455-2655
bostrager@stblaw.com

Mary Kay Vyskocil
(212) 455-3093
mvyskocil@stblaw.com

Andrew S. Amer
(212) 455-2953
aamer@stblaw.com

David J. Woll
(212) 455-3136
dwoll@stblaw.com

Mary Beth Forshaw
(212) 455-2846
mforshaw@stblaw.com

Andrew T. Frankel
(212) 455-3073
afrankel@stblaw.com

Lynn K. Neuner
(212) 455-2696
lneuner@stblaw.com

Seth A. Ribner
(310) 407-7510
sribner@stblaw.com

Chet A. Kronenberg
(310) 407-7557
ckronenberg@stblaw.com

Linda H. Martin
(212) 455-7722
lmartin@stblaw.com

Bryce L. Friedman
(212) 455-2235
bfriedman@stblaw.com

Michael D. Kibler
(310) 407-7515
mkibler@stblaw.com

Michael J. Garvey
(212) 455-7358
mgarvey@stblaw.com

Tyler B. Robinson
+44-(0)20-7275-6118
trobinson@stblaw.com

George S. Wang
(212) 455-2228
gwang@stblaw.com

Deborah L. Stein
(310) 407-7525
dstein@stblaw.com

Elisa Alcabes
(212) 455-3133
ealcabes@stblaw.com

"[Simpson Thacher's insurance litigation group consists of] excellent tacticians and litigators with broad industry connections."

— Chambers USA 2011
(quoting a client)

UNITED STATES

New York
425 Lexington Avenue
New York, NY 10017
+1-212-455-2000

Houston
2 Houston Center
909 Fannin Street
Houston, Texas 77010
+1-713-821-5650

Los Angeles
1999 Avenue of the Stars
Los Angeles, CA 90067
+1-310-407-7500

Palo Alto
2550 Hanover Street
Palo Alto, CA 94304
+1-650-251-5000

Washington, D.C.
1155 F Street, N.W.
Washington, D.C. 20004
+1-202-636-5500

EUROPE

London
CityPoint
One Ropemaker Street
London EC2Y 9HU
England
+44-(0)20-7275-6500

ASIA

Beijing
3919 China World Tower
1 Jian Guo Men Wai Avenue
Beijing 100004
China
+86-10-5965-2999

Hong Kong
ICBC Tower
3 Garden Road, Central
Hong Kong
+852-2514-7600

Tokyo
Gaikokuho Jimu Bengoshi Jimusho
Ark Mori Building
12-32, Akasaka 1-Chome
Minato-Ku, Tokyo 107-6037
Japan
+81-3-5562-6200

SOUTH AMERICA

São Paulo
Av. Presidente Juscelino Kubitschek, 1455
São Paulo, SP 04543-011
Brazil
+55-11-3546-1000