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Phone: +1 646 783 7100 | Fax: +1 646 783 7161 | customerservice@law360.com

4 Key Insurance Rulings You May Have Missed This Summer

By **Jeff Sistrunk**

Law360 (August 30, 2019, 7:11 PM EDT) -- Several important insurance opinions flew under the radar this summer, including a Delaware court's decision that a government investigation notice triggers an insurer's duty to defend its policyholder and a Pennsylvania appellate court's ruling that a carrier must defend claims that an insured's faulty repair work damaged someone else's property.

Here, Law360 breaks down four recent insurance rulings that attorneys should know.

Conduent State Healthcare v. AIG Specialty Insurance Co.

Ruling on an issue of first impression under Delaware law, a state judge held June 24 that a policyholder is entitled to defense coverage when it receives a notice from a government agency indicating it is under investigation for potential wrongdoing.

Superior Court Judge Mary M. Johnston denied a motion to dismiss filed by two AIG units, which had sought a ruling that they have no duty to cover policyholder Conduent State Healthcare's costs to respond to a 2012 notice from the Texas attorney general's office known as a civil investigative demand, or CID. The demand alerted Conduent, the claims administrator for Texas Medicaid's orthodontics program, that the state was investigating possible Medicaid fraud by the company.

In a subsequent lawsuit, the Lone Star State's attorney general claimed that Conduent processed $1.1 billion in orthodontic claims for Medicaid patients that weren't medically necessary. Conduent ultimately resolved the claims for $235.9 million, in the largest Medicaid-related settlement in the state's history.

Conduent claimed in a suit filed in March that its insurers should be responsible for covering the costs of its response to the Texas attorney general's CID, certain suits filed by health care providers and the action brought by the state. The company argued that the insurers' duty to defend was triggered when the CID was issued, but AIG countered the CID does not constitute a claim, which must allege "a wrongful act" by Conduent.

Judge Johnston said in her opinion that, while substantial case law backed both sides' arguments, she was more persuaded by Conduent's contention that the CID constitutes a covered insurance claim.

"The court is not persuaded that investigating an alleged unlawful act by the insured is different from

actually alleging an unlawful act," Judge Johnston wrote. "This is a distinction without a difference."

The decision will bolster policyholders' efforts to obtain coverage for government probes, said Jassy Vick Carolan LLP partner William Um.

"The Conduent case takes away the legal fiction that these government investigations are innocuous just because they don't contain formal allegations of wrongdoing," Um said.

Conduent is represented by Robin L. Cohen and Keith McKenna of McKool Smith PC and Jennifer C. Wasson and Carla M. Jones of Potter Anderson & Corroon LLP.

The AIG units are represented by John L. Reed and Matthew Denn of DLA Piper and Robert S. Harrell of Mayer Brown LLP.

The case is Conduent State Healthcare LLC v. AIG Specialty Insurance Co. et al., case number N18C-12-074, in the Superior Court for the State of Delaware.

Pennsylvania Manufacturers Insurance Co. v. Pottstown Industrial Complex

On July 22, a Pennsylvania appeals court clarified the state's law and found that a policyholder can secure defense coverage for claims arising from its alleged faulty workmanship, provided that the purportedly shoddy work damaged a third party's property.

A panel of the Pennsylvania Superior Court reversed a trial court's ruling that Pennsylvania Manufacturers Indemnity Co. has no duty to defend its policyholder, landlord Pottstown Industrial Complex LP, in a negligence action brought by a tenant.

The tenant, florist supplies company The Pride Group Inc., claimed that Pottstown Industrial's failure to properly repair its building's roof led to interior flooding four times between 2013 and 2016, ruining $700,000 worth of Pride's inventory.

In the ensuing coverage dispute, PMIC argued that, because Pride's suit concerned Pottstown Industrial's own purportedly deficient work, it did not allege an accidental "occurrence" under the terms of the landlord's commercial general liability policy. The insurer cited the Pennsylvania Supreme Court's 2006 decision in Kvaerner Metals v. Commercial Union Insurance and another midlevel state appellate panel's subsequent ruling in Millers Capital Insurance v. Gambone Brothers Development, which established that a policyholder's faulty workmanship generally does not qualify as an occurrence.

The trial court agreed with PMIC's interpretation of the two cases and ruled in its favor, but the Superior Court panel disagreed.

Under Kvaerner and Millers Capital, a claim stemming from a policyholder's shoddy work doesn't allege an occurrence "where the only property damaged is the product or property that the insured supplied or on which it worked" or the damages being sought "are for the insured's failure to deliver the product or perform the service it contracted to provide," the opinion said. In Pottstown Industrial's case, by contrast, the tenant is seeking compensation for the loss of its own property, the panel noted.

"Holding that such claims are covered by a CGL policy is consistent with the rationale of Kvaerner that the term 'occurrence' must not be interpreted so broadly that it converts the policy into a performance

bond, as this construction does not provide coverage for loss of the value of the insured's performance," the panel said. "Rather, it construes the policy as providing insurance for a risk that CGL policies are intended to cover, damage that the insured causes to another person's property."

Pottstown Industrial is represented by Meghan Katherine Finnerty and Jay M. Levin of Offit Kurman PA.

PMIC is represented by Geoffrey Stetson Gavett of Gavett Datt & Barish PC and George Elias Saba of Law Offices of George E. Saba Jr. LLC.

The case is Pennsylvania Manufacturers Insurance Co. v. Pottstown Industrial Complex LP et al., case number 3489 EDA 2018, in the Superior Court of Pennsylvania.

Nationwide Mutual Insurance Co. v. Arnold

The Pennsylvania Superior Court also had the opportunity to consider the scope of a rarely litigated policy exclusion when it ruled on July 11 that Nationwide Mutual Insurance Co. must defend a Pennsylvania Department of Transportation whistleblower in a suit alleging that he falsely accused a contractor of overcharging the agency.

A panel of the appellate court agreed with a trial court that Nationwide cannot deny coverage for the underlying suit against its insured, PennDOT engineer August Arnold, by invoking a "business pursuits" exclusion in his personal umbrella policy for liabilities "arising out of" his work.

Arnold acted as a whistleblower in a U.S. government action against several agency contractors. One of those companies, CMC Engineering, won summary judgment in the whistleblower case and then sued Arnold and his attorney, Jon Pushinsky, claiming the engineer falsely accused CMC of fraudulent conduct.

According to the insurer, if Arnold had not been working for PennDOT, he would not have been able to act as a whistleblower. But the Superior Court found that, while Arnold's employment at PennDOT allowed him to gather evidence of the contractors' alleged fraud, those activities were not related to his actual job responsibilities. As a result, CMC's suit doesn't fall under the business pursuits exclusion, and Nationwide must fund Arnold's defense, the panel said.

"At bottom, CMC's allegations challenge Arnold's personal conduct, not actions he took or events that transpired in the context of his employment," the panel held. "We decline to construe the 'business pursuits' exclusion so broadly that coverage is precluded for allegations with any nexus whatsoever to an insured's work."

Lowenstein Sandler LLP partner Lynda Bennett said that, while the decision is noteworthy because it provided rare guidance on the business pursuits exclusion, its analysis could also be applied to disputes over a number of other policy exclusions.

"A lot of the court's decision centers around this 'arising out of' language, which you see in a lot of exclusions," Bennett said. "There is a potential for this case to have broader reach because the court narrowly interpreted what this language means."

Arnold is represented by William H. Knestrick III of Neighborhood Attorneys LLC.

Nationwide is represented by John A. Anastasia and Joseph B. Mayers of The Mayers Firm LLC.

Pushinsky is represented by Patrick J. Wolfe Jr. of Narducci Moore Fleisher Roeberg & Wolfe LLP.

The case is Nationwide Mutual Insurance Co. v. Arnold et al., case number 1208 WDA 2018, in the Superior Court of Pennsylvania.

UBS Financial Services of Puerto Rico v. XL Specialty Insurance Co.

Right before the Fourth of July holiday, the First Circuit issued a splashy opinion affirming a lower court's ruling that UBS AG units cannot tap into $20 million in insurance coverage to defray costs associated with scores of claims that investors lost billions of dollars because UBS manipulated Puerto Rico's municipal debt bond market.

Applying a broad interpretation of a common policy exclusion, a panel of the federal appellate court upheld U.S. District Judge Francisco Besosa's February 2018 ruling granting summary judgment to primary and excess insurers for UBS Financial Services Inc. of Puerto Rico and UBS Trust Co. of Puerto Rico.

The panel agreed with the district judge's conclusion that a "specific litigation" exclusion in the insurers' policies clearly bars coverage because the claims at issue share a number of allegations with certain earlier matters concerning UBS' purported misleading statements regarding closed-end funds holding Puerto Rican municipal debt.

UBS told the First Circuit that the district judge's analysis flouted the standard set forth by the appeals court's 2005 decision in Federal Insurance Co. v. Raytheon, which dealt with a similar specific litigation exclusion and held that the "relevant facts" in a present claim must "substantial[ly] overlap" with those in an earlier claim for the exclusion to apply. According to UBS, while the claims for which it is seeking coverage include some references to a pair of past actions, they are largely rooted in distinct allegations of wrongdoing not at issue in those earlier matters.

But the First Circuit was unswayed, saying the exclusion at the heart of the Raytheon case was less restrictive than the one involved in the matter at hand. Moreover, the panel said, UBS accepted a broader specific litigation exclusion after extensive negotiations with its insurers, and it cannot now rewrite the exclusionary language.

"Aware of the breadth of the unchanged exclusion, UBS nevertheless agreed to purchase the policy as it read," the panel said. "Therefore, we see no reason to depart from the negotiated plain text of the provision."

UBS is represented by Robert T. Smith, Rajesh R. Srinivasan, Michael I. Verde, David L. Goldberg, Tenley Mochizuki and Philip A. Nemecek of Katten Muchin Rosenman LLP and Jaime E. Toro-Monserrate and Nayda I. Perez Roman of Toro Colon Mullet Rivera & Sifre PSC.

XL Specialty is represented by Kimberly M. Melvin, Cara Tseng Duffield, John E. Howell and Karen L. Toto of Wiley Rein LLP. Hartford Fire is represented by Joshua D. Weinberg of Shipman & Goodwin LLP. Axis is represented by Michael R. Goodstein and James M. Young of Bailey Cavalieri LLC. The insurers are also jointly represented by Francisco E. Colón-Ramírez of Colón Ramírez LLC.

The case is UBS Financial Services Inc. of Puerto Rico et al. v. XL Specialty Insurance Co. et al., case number 18-1148, in the U.S. Court of Appeals for the First Circuit.

--Additional reporting by Sarah Jarvis. Editing by Kelly Duncan and Brian Baresch.