ReedSmith

The business of relationships.SM

ESSEX COURT CHAMBERS

BARRISTERS

Bermuda Form Mock Arbitration - Index to Legal Authorities

09 June 2015

IN THE MATTER OF A BERMUDA FORM ARBITRATION

BETWEEN

WELLBEING HOSPITAL INC.

Claimant

-and-

FAIRPLAY INSURANCE CO. LTD.

Respondent

INDEX TO LEGAL AUTHORITIES

1	(English) Arbitration Act 1996, section 34
2	*Winterthur Swiss Insurance v AG (Manchester) Ltd.* [2006] EWHC 839 (Comm) (extract)
3	*Isidore Rosen & Sons Inc. v Security Mutual Insurance Company* 31 N.Y.2d 342 (NY 1972)
4	*Luria Bros & Co v Alliance Assurance* 780 2d 1082 (2d Cir 1986)
5	*PepsiCo v Continental Casualty* 640 F Supp 656 (SDNY 1986)
6	*International Ins Co v Newmont Mining Co* 800 F. Supp 1195, 1196-7 (SDNY 1992)
7	*Vigilant Ins Co v Bear Stearns Co* 855 NYS 2d 45 (NY2008)

TAB 1

Arbitration Act 1996

CHAPTER 23

First Published 1996
Reprinted 2001

(6) The decision of the court on the question of jurisdiction shall be treated as a judgment of the court for the purposes of an appeal.

But no appeal lies without the leave of the court which shall not be given unless the court considers that the question involves a point of law which is one of general importance or is one which for some other special reason should be considered by the Court of Appeal.

The arbitral proceedings

General duty of the tribunal.

33.—(1) The tribunal shall—

(a) act fairly and impartially as between the parties, giving each party a reasonable opportunity of putting his case and dealing with that of his opponent, and

(b) adopt procedures suitable to the circumstances of the particular case, avoiding unnecessary delay or expense, so as to provide a fair means for the resolution of the matters falling to be determined.

(2) The tribunal shall comply with that general duty in conducting the arbitral proceedings, in its decisions on matters of procedure and evidence and in the exercise of all other powers conferred on it.

Procedural and evidential matters.

34.—(1) It shall be for the tribunal to decide all procedural and evidential matters, subject to the right of the parties to agree any matter.

(2) Procedural and evidential matters include—

(a) when and where any part of the proceedings is to be held;

(b) the language or languages to be used in the proceedings and whether translations of any relevant documents are to be supplied;

(c) whether any and if so what form of written statements of claim and defence are to be used, when these should be supplied and the extent to which such statements can be later amended;

(d) whether any and if so which documents or classes of documents should be disclosed between and produced by the parties and at what stage;

(e) whether any and if so what questions should be put to and answered by the respective parties and when and in what form this should be done;

(f) whether to apply strict rules of evidence (or any other rules) as to the admissibility, relevance or weight of any material (oral, written or other) sought to be tendered on any matters of fact or opinion, and the time, manner and form in which such material should be exchanged and presented;

(g) whether and to what extent the tribunal should itself take the initiative in ascertaining the facts and the law;

(h) whether and to what extent there should be oral or written evidence or submissions.

(3) The tribunal may fix the time within which any directions given by it are to be complied with, and may if it thinks fit extend the time so fixed (whether or not it has expired).

TAB 2

Status: Positive or Neutral Judicial Treatment

Winterthur Swiss Insurance Company, The National Insurance & Guarantee Corporation Limited v AG (Manchester) Limited (In Liquidation), Rowe Cohen (A Firm), Ashington Denton (A Firm)

Case No: 05/613

High Court of Justice Queen's Bench Division Commercial Court

12 April 2006

[2006] EWHC 839 (Comm)

2006 WL 1288361

Before : Mr Justice Aikens

Date: 12th April 2006, Hearing dates: 19th, 20th and 23rd January 2006

Representation

Mr C Hollander QC and Mr Tim Lord (instructed by Richards Butler , Solicitors, London) for the Claimants.

Mr B Patten (instructed by Henmans , Solicitors, Oxford) for the Second Defendants.

Ms S Carr QC and Mr J Smith (instructed by Bond Pearce LLP , Solicitors, Exeter) for the Group Two Panel Solicitor Defendants.

Mr J Fenwick QC , Mr T Lowe and Mr B Hubble (instructed by Kennedys , Solicitors, London) for the Group One Panel Solicitor Defendants.

Mr C Phipps (instructed by Berrymans Lace Mawer , Solicitors, London) for the Group Four Panel Solicitor Defendants.

Approved Judgment

Mr Justice Aikens :

I. The Background to the litigation

1 This litigation concerns "After the Event" legal expenses insurance. This type of insurance was introduced with the reduction in the availability of legal aid for many types of civil claim and with the introduction of Conditional Fee Agreements for litigation. The second claimant, ("NIG") underwrote "After the Event" legal expenses insurance ("ATE policies") in connection with a litigation funding scheme operated by the first defendant. The first defendant was formerly called The Accident Group Limited. It then changed its name to AG (Manchester) Limited. The company has been in liquidation since 15 January 2004. In these proceedings the company has been called "TAG". The ATE insurance scheme run by TAG has been called "the TAG Scheme".

2 By a written agreement dated 1 July 2001, NIG appointed TAG as its agent. NIG effectively delegated to TAG the underwriting and claims handling of ATE policies. The TAG Scheme was marketed to the public as a "no win, no fee" scheme, which would finance the litigation of claims

64 In order to deal with these issues it may help to state some general propositions about "legal professional privilege", its scope and when it can be exercised or not.

What is "legal professional privilege"?

"Legal professional privilege", which is often referred to simply as "privilege", is recognised as a fundamental human right granted by the common law. [22] The right is given to citizens or other legal entities that obtain legal advice from a lawyer. In B v Auckland District Law Society [23] Lord Millett described "privilege" as " *a right to resist the compulsory disclosure of information* ". The corollary of this right of the client is the duty of the lawyer to keep confidential and not to disclose to others information that is covered by legal professional privilege. The right to resist the compulsory disclosure of information can be exercised in litigation or other adversarial legal processes, such as arbitration. But the right to resist the compulsory disclosure of information is not confined to such processes. Generally speaking, information that is covered by legal professional privilege cannot be subject to any order for compulsory production to another at all, unless there is an express statutory power, or one by implication, that requires it. [24]

66 The cases have noted that this right to resist the compulsory disclosure of information is confined to information relating to legal advice, as opposed to information and advice given and received in other confidential relationships such as between a patient and his doctor or an accountant and his client. [25] I mention below the rationale for this rule only applying in relation to legal advice, as opposed to other confidential relationships.

67 The cases have developed a distinction between two sub — types, or "sub — heads" [26] of "legal professional privilege". In the earliest cases the privilege from compulsory production was confined to information (principally documentary) that was created where legal proceedings were in contemplation. That type of legal professional privilege has become known today as "litigation privilege". But, in two landmark cases in 1833, Lord Brougham LC held that legal professional privilege extended to communications where legal advice was sought and given when no litigation was contemplated. [27] That sub — type of legal professional privilege has become known today as "legal advice privilege".

68 The rationale for the first sub — type (ie. "litigation privilege") rests, in modern terms, on the principles of access to justice, the proper administration of justice, a fair trial and equality of arms. Those who engage in litigation or are contemplating doing so may well require professional legal advice to advance their case in litigation effectively. [28] To obtain the legal advice and to pursue adversarial litigation [29] efficiently, the communications between a lawyer and his client and a lawyer and a third party and any communication brought into existence for the dominant purpose of being used in litigation must be kept confidential, without fear that what is said or written might be disclosed. Therefore those classes of communication are covered by "litigation privilege". [30]

69 The rationale for the second sub — type of privilege, (ie. "legal advice privilege"), is that it advances the rule of law. [31] Citizens, corporations and other legal entities need to know what the law is so that they can decide what they can and cannot do and so manage their affairs according to law. If a citizen or corporation is to obtain advice on his legal rights and obligations, the lawyer consulted must be given all the relevant facts so as to give effective advice. Many cases have concluded that all the relevant facts will not necessarily be given unless they are imparted in confidence to the lawyer and the lawyer is under a duty to keep that information and his advice confidential. To protect that confidentiality and so advance the rule of law, the cases have developed the rule that communications between lawyers and clients [32] that are generated even when no litigation is contemplated, will not be subject to compulsory production, unless a statutory power expressly or by implication requires it. [33] But "legal advice privilege" does not extend to communications obtained from third parties that are to be shown to the lawyer for the purpose of obtaining legal advice. [34]

70 In the present case issues on legal advice privilege arise only at the pre — ATE Policy stage. Mr Hollander is prepared to accept, if necessary, that the vetting by Rowe Cohen and the Panel Solicitors before the ATE Policies were issued will be subject to "legal advice privilege". But he

submits that legal advice at that stage was being sought by NIG to see whether an ATE Policy should be issued. Therefore if there is privilege in communications to Rowe Cohen and the Panel Solicitors by the potential TAG Claimant and the legal advice given by them, the privilege must be that of the insurer, NIG.

The scope of "litigation privilege"

"Litigation privilege" extends, in time, to information (which must include information stored in electronic form as well as in documentary form) which is produced either during the course of adversarial (as opposed to inquisitorial or investigative) litigation, or when such litigation is in contemplation. The privilege obviously covers legal advice given by a lawyer to his client for the purposes of such existing or contemplated litigation. It also extends to communications between the lawyer and his client and the lawyer and third parties, provided that those communications are made for the sole or dominant purpose of obtaining legal advice or conducting that litigation. [35] In deciding whether a communication is subject to "litigation privilege", the court has to consider objectively the purpose of the person or authority that directed the creation of the communication. [36]

In what circumstances might a person be unable to exercise a right to assert Legal Professional Privilege over communications that would otherwise be covered by that right?

The general rule, applicable to both sub — types of legal professional privilege, is that a communication that is protected by the privilege continues to be protected for ever, unless the privilege is waived by the client, who alone has the right to waive privilege. No one can waive privilege on his behalf unless the client's consent has been given: " *once privileged, always privileged* ". Moreover, if the client refuses to waive his right to maintain privilege, for whatever reason or for none, that refusal cannot be questioned or investigated by the court. [37] Although Lord Nicholls of Birkenhead said in the Derby Magistrates' case that he was " *instinctively unattracted* " to a rule that a client can insist on maintaining privilege, when the client no longer has any interest in asserting it and where the non — disclosure would prejudice a third party, the law remains " *once privileged, always privileged* ". [38] Moreover, the privilege remains absolute, unless the privileged communication is itself the means of carrying out a fraud. [39]

73 A client can consent to privileged communications being made available generally for disclosure. In that case the privileged nature of the communications is lost completely. But a client can also agree to produce privileged communications for a limited purpose only. If that happens, the privileged nature of those communications is not lost completely. The client can assert the right not to produce the same communications for any purpose outside the limited purpose for which he agreed to produce the communications. [40]

74 I must consider next the situation where privileged documents or communications either have been or will be created and the person in the position of the client agrees, by contract or otherwise, with a third party, to grant that party access to such privileged communications. In Brown v Guardian Royal Exchange Assurance PLC [41] there was an express term in the contract for a solicitor's professional indemnity insurance that where solicitors or other expert advisers were employed in relation to a claim against the insured, then " *the Insurers ... may require the solicitors' reports to be submitted directly to them* ". The Court of Appeal held that this term in the insurance was crucial. It meant that if solicitors were appointed to deal with a claim against the insured solicitor, then the insurers were entitled to see communications from both the insured and third parties to and from solicitors employed in relation to a claim against the insured, provided that the communications concerned the subject matter of the claim against the insured. [42] It seems to follow that the person who has the right to exercise privilege must be entitled to agree with a third party to give that person access to privileged communications. The agreement might be general or for specified purposes. That will depend on the correct construction of the agreement. [43] Once the assent to access is given to a third party, then in general the right to privilege cannot be re-asserted as against that party, except with agreement. However, where the agreement to give access to privileged communications is founded on a joint or common interest between the person in the role of client and another, as it was in Brown's case , then it would appear that if the joint or common interest ends, eg. when an actual conflict of interest

arises, then the right to have access to privileged information that is created thereafter by or on behalf of the client, will end. [44]

75 That leaves the question of whether someone other than the third party to whom the right of access is given is entitled to claim a right of access to privileged communications, eg. by claiming it is an assignee of the third party's rights. That is a major issue in this application, because Winterthur claims the right of access to communications that are privileged in its position as assignee of NIG. I will deal with it below.

"Common Interest" privilege

The concept of "common interest" privilege derives from *Jenkyns v Bushby* , [45] a decision of Kindersley V-C. He held that a case for the opinion of counsel, prepared in relation to separate litigation for the benefit of the predecessor in title to the defendant in the action, but after the present dispute had arisen, was privileged from production in the later action. The concept was developed in the *Court of Appeal's decision in Buttes Gas and Oil Co v Hammer (No 3)* . [46] Brightman LJ expressed the proposition of law to which he gave assent in this way:

> "... if two parties with a common interest and a common solicitor exchange information for the dominant purpose of informing each other of the facts, or the issues, or advice received, or of obtaining legal advice in respect of contemplated or pending litigation, the documents or copies containing that information are privileged from production in the hands of each". [47]

77 In *Guinness Peat Properties Ltd v Fitzroy Robinson Partnership* , [48] the defendants in the action had, as insureds, written a letter report to their insurers about a claim made against them by the plaintiffs. The Court of Appeal held that the letter had been brought into existence at the instance of the insurers in order to obtain legal advice or to assist in the conduct of litigation. Solicitors for the defendants had inadvertently allowed the plaintiffs' solicitors to inspect the letter and it was referred to in the plaintiffs' expert's report. The Court of Appeal upheld the judge's decision to grant an injunction to restrain the plaintiffs from using the letter further and ordering them to return all copies to the defendants. Slade LJ noted that although it was the insurers that had caused the letter to be created, it was the defendant insured that now claimed that it was covered by "litigation privilege". He held, following the statement of the law of Brightman LJ in the Buttes Gas case , that the document was privileged in the hands of the defendant insured. [49]

78 These cases demonstrate that where a communication is produced by or at the instance of one party for the purposes of obtaining legal advice or to assist in the conduct of litigation, then a second party that has a common interest in the subject matter of the communication or the litigation can assert a right of privilege over that communication as against a third party. The basis for the right to assert this "common interest privilege" must be the common interest in the confidentiality of the communication. The cases I have referred to concerned applications for production of communications to a third party, which were resisted. They assume that the communications concerned will be covered by one or other sub — type of legal professional privilege in the hands of the party that caused the communication to be produced in the first place. That type of situation, where a second party resists the application of a third party for production of communications, has been called "using common interest privilege as a shield". [50]

79 However, it is not this use of common interest privilege that arises in the present applications. The submission of Mr Hollander is that NIG (and Winterthur) can rely on "common interest privilege as a sword". [51] That type of common interest privilege is established by such cases as Cia Barca de Panama SA v George Wimpey & Co Ltd , [52] and Commercial Union Assurance Co plc v Mander . [53] The principle is that if party B has a sufficiently common interest in communications that are held by party A, then party B can obtain disclosure of those communications from party A even though, as against third parties, the communications would be privileged from production by virtue of legal professional privilege. In Svenska Handelsbanken v Sun Alliance and London Insurance PLC , [54] Rix J (as he then was) held that "common interest privilege as a sword" could be asserted in relation to both "litigation" privilege and also "legal advice" privilege. I respectfully agree.

80 The questions of what type of relationship between the two parties can give rise to a "common

interest" in the communication concerned has been considered in a number of cases. Amongst the types of relationship that can give rise to a "common interest" are those of insured and insurer and insurer/reinsured and reinsurer. [55] The cases have refused to be prescriptive about the circumstances in which the two parties will have a sufficient "common interest" in the particular communications concerned. The issue has to be decided on the facts of the individual case.

81 Two cases deal with the time at which the common interest in the privileged communication must exist in order to permit the exercise of "common interest privilege as a sword". In Cia Barca v Wimpey , Bridge LJ formulated the principle on the basis that the two parties (A and B in my example) have a common interest in the communication at the time the relevant communication was created. [56] It will not matter that, subsequently, the two parties (A and B) fall out. [57] That analysis was followed by Moore — Bick J (as he then was) in Commercial Union v Mander . [58] It therefore appears to follow that, at least in cases of "common interest as a sword", once a communication is subject to common interest privilege, then it will always remain so.

82 With that introduction of the legal principles, I consider the five issues for decision that I have set out above.

VI. Are any pre — ATE Policy documents in the hands of the Panel Solicitors referred to in the Schedule to the Outline Argument submitted by the Panel Solicitors subject to any form of "legal professional privilege"; if so, what form?

83 Both "legal advice privilege" and "litigation privilege" are claimed in relation to pre — ATE Policy communications. Logically it seems sensible to consider first "litigation privilege", because that can cover not only communications between the client and his lawyer, but also third parties and the lawyer. In so far as the relevant pre — ATE Policy communications might be subject to "litigation privilege", three questions arise. First, at the time that the relevant communications were created, was litigation contemplated? Secondly, were the communications created for the dominant purpose of obtaining legal advice for that litigation or in aid of that litigation? Thirdly, under the direction of which person or entity, objectively speaking, were those communications created; that of the putative TAG Claimant, or the putative ATE insurer, NIG?

84 Insofar as "legal advice privilege" is asserted, the major question is: at whose direction were communications produced that went to Rowe Cohen or a Panel Solicitor? Was "the client" at that stage NIG or the potential TAG Claimant? A secondary question might arise if the answer to the first question is: "the potential ATE claimant". That is, was the communication to Rowe Cohen or the Panel Solicitor from the potential TAG Claimant, as "the client", or from a third party.

85 Mr Hollander submits that there was, in effect, a condition precedent to an ATE Policy being issued. That was that the potential claim had been properly vetted. Until it had been, there could be no question of pursuing a claim through litigation. So, before the ATE Policy was issued, litigation was not contemplated and no communications could have been produced with the dominant purpose of obtaining legal advice as to contemplated litigation or in aid of such litigation. He relies on the House of Lords' decision in Jones v Great Central Railway Company . [59] The House held that letters written by a trade union member to his union so as to provide evidence to see whether it would provide him with legal assistance to bring a claim for wrongful dismissal were not covered by legal professional privilege.

86 Miss Carr submits that "litigation privilege" applies to the pre — ATE Policies, in particular the key documents, which are the Claim Application Form and the AIL Questionnaire. In her submission there was a "unified" purpose in completing these pre — ATE Policy documents, because the process of obtaining the ATE Policy was an intrinsic part of the litigation process. In this regard, Miss Carr relies on the wording of what was dubbed by TAG agents as the "Second Aid Pack"; these packs were handed to TAG Claimants, "outside the supermarket", as it were. The packs suggest that information provided will go to a solicitor. Miss Carr also relies on the wording of the TAG Service Agreement and Declaration, in particular declarations 9 and 12, with the references to "my claim" (ie. that of the potential TAG Claimant); "my case"; "my solicitor" and "my application for a policy". Miss Carr submits that the whole process, considered objectively, is in aid of litigation.

87 Miss Carr relies on the analysis of the Court of Appeal in Re Highgrade Traders Ltd. [60] In that

TAB 3

Isadore Rosen & Sons, Inc., Appellant, v. Security Mutual Insurance Company of New York, Respondent

[NO NUMBER IN ORIGINAL]

Court of Appeals of New York

31 N.Y.2d 342; 291 N.E.2d 380; 339 N.Y.S.2d 97; 1972 N.Y. LEXIS 942

November 1, 1972, Argued
December 6, 1972, Decided

PRIOR HISTORY: *Rosen & Sons* v. *Security Mut. Ins. Co. of N. Y.*, 37 A D 2d 829.

Appeal from an order of the Appellate Division of the Supreme Court in the First Judicial Department, entered October 26, 1971, which (1) reversed, on the law, an order of the Supreme Court at Special Term (Ivan Warner, J.), entered in Bronx County, denying a motion by defendant for summary judgment; (2) granted the motion, and (3) dismissed the complaint.

DISPOSITION: Order reversed, with costs, and the case remitted to Supreme Court, Bronx County, for further proceedings in accordance with the opinion herein.

CORE TERMS: insurer, insured, settlement, general contractor, notice, summary judgment, contractor, final payment, unreasonable delay, notified, negligence claim, subcontractor, triable, policy provisions, coverage, issue of fact, unreasonably delayed, work performed, vice-president, permission, covering, exerted, exact, roof, general rule, denial of liability, evidentiary facts, withholding, adjust, failure to act

HEADNOTES

Insurance -- settlement of negligence claim -- consent of insurer -- insurance policy covering claim due to alleged negligence of plaintiff and naming plaintiff as insured provided that insured should not voluntarily make payment on any risk -- general contractor and plaintiff, subcontractor, reached settlement in which balance earned by plaintiff was paid -- motion by defendant insurance company in action on said policy for summary judgment properly denied -- triable issue of fact presented as to whether defendant insurance company unreasonably delayed action on negligence claim where it had notice of claim and knew of economic pressure exerted by general contractor and as to whether certain provisions of policy against settlement without insurer's permission in writing were waived.

One of the terms of the agreement between plaintiff, subcontractor for an apartment construction project, and the general contractor was that the general contractor would provide liability insurance for plaintiff covering property damage caused by plaintiff's operation. Defendant insurance company issued a policy in which plaintiff was named as an insured. In the course of construction, the general contractor claimed that plaintiff had negligently caused damage of $ 15,648. This was a covered risk under the policy. There was owing to plaintiff from the general contractor about $ 80,000 as final payment for work performed. A settlement was reached between the two in which the balance of the amount earned by plaintiff was paid. The policy provided that the insured shall not "voluntarily make any payment" on any risk within the obligation of the policy;

and that no action shall lie against the insurer until the amount of the insured's obligation "shall have been finally determined". In this action against the insurer for recovery under the terms of the policy, Special Term properly denied a motion by defendant for summary judgment. A triable issue of fact is presented on the issue whether defendant unreasonably delayed taking action on the negligence claim against plaintiff under circumstances where it had notice of the claim and knew or ought to have known of economic pressure for settlement exerted by the general contractor, also its insured, in such fashion as to waive the provisions of its policy against settlement by the insured without its permission in writing.

COUNSEL: *Frederick Cohen, David Morgulas* and *Albert Foreman* for appellant. I. Appellant was not required to subject itself to a judgment in favor of Dayton as seemingly required by paragraph 10 of the policy of insurance. (*Kennelly* v. *London Guar. & Acc. Co.*, 184 App. Div. 1; *Meridian Trading Corp.* v. *National Auto. & Cas. Ins. Co.*, 45 Misc 2d 847; *Jesse E. Kahn, Inc.* v. *Driscoll Co.*, 1 Misc 2d 405; *Broadway Realty Co.* v. *Lawyers Tit. Ins. & Trust Co.*, 226 N. Y. 335; *Bushey & Sons* v. *American Ins. Co.*, 237 N. Y. 24; *Gerka* v. *Fidelity & Cas. Co.*, 251 N. Y. 51; *Hartol Prods. Corp.* v. *Prudential Ins. Co.*, 290 N. Y. 44; *Bronx Sav. Bank* v. *Weigandt*, 1 N Y 2d 545.) II. Respondent's delay in disclaiming liability under the policy estops it from asserting the "no action" clause as a bar to this action. The issue of estoppel is a factual question which cannot be resolved on a motion for summary judgment. (*Matter of Vanguard Ins. Co.* v. *Polchlopek*, 18 N Y 2d 376; *Cardinal* v. *State of New York*, 304 N. Y. 400; *Matter of Empire State Sur. Co.*, 214 N. Y. 553; *Berger Bros. Elec. Motors* v. *New Amsterdam Cas. Co.*, 178 Misc. 1053, 267 App. Div. 333, 293 N. Y. 523; *Mitchell* v. *Lindstrom*, 12 A D 2d 813; *Weissblum* v. *Glens Falls Ins. Co.*, 31 Misc 2d 132, 40 Misc 2d 964; *O'Dowd* v. *American Sur. Co. of N. Y.*, 3 N Y 2d 347; *Ashland Window & Housecleaning Co.* v. *Metropolitan Cas. Ins. Co. of N. Y.*, 269 App. Div. 31.) III. Respondent's liability under the policy of insurance was absolute. It was bound to protect both appellant and Dayton from both "legal liability" and "contractual liability." (*Levine* v. *Shell Oil Co.*, 28 N Y 2d 205; *Kurek* v. *Port Chester Housing Auth .*, 18 N Y 2d 450; *Fuller Co.* v. *Fischbach & Moore*, 7 App. Div. 33; *Madawick Contr. Co.* v. *Travelers Ins. Co.*, 307 N. Y. 111; *Mattera* v. *Mack Trucks*, 38 Misc 2d 256.)

Lazarus I. Levine and *I. Sidney Worthman* for respondent. I. Notice is not an issue in this action. In view of the unambiguous terms and conditions of the policy and by reason of the concession made by plaintiff, the instant action is not maintainable against defendant by reason of the breach by plaintiff, as an additional insured, of the terms and conditions of the subject policy of insurance. (*Kennelly* v. *London Guar. & Acc. Co.*, 184 App. Div. 1; *Meridian Trading Corp.* v. *National Auto. & Cas. Ins. Co.*, 45 Misc 2d 847.) II. Appellant has failed to demonstrate any basis for its claim that respondent is estopped from asserting the "no action" clause in the subject policy of insurance as a bar to this action. (*Indig* v. *Finkelstein*, 23 N Y 2d 728; *Holdridge* v. *Town of Burlington*, 32 A D 2d 581; *Steingart Assoc.* v. *Sandler*, 28 A D 2d 801.)

JUDGES: Chief Judge Fuld and Judges Scileppi and Gibson concur with Judge Bergan; Judge Breitel dissents and votes to affirm in a separate opinion in which Judges Burke and Jasen concur.

OPINION BY: BERGAN

OPINION

[*344] [**381] [***98] Plaintiff was the masonry subcontractor for an apartment construction project in which Dayton Construction Co., Inc. was the general contractor. One of the terms of the agreement between them was that the prime contractor would provide for plaintiff liability insurance covering, among other things, property damage caused by plaintiff's operation. The premium for this coverage was to be paid by plaintiff.

[*345] Defendant Security Mutual Insurance Company of New York issued a general "wrap-up" policy to Dayton in which plaintiff was named as an additional insured. In the course of construction Dayton claimed that plaintiff had negligently caused damage of $ 15,648 to the roof which had been installed by another subcontractor, and demanded payment in this amount.

At the time the general contractor pressed plaintiff for payment of the claimed roof damage, there was owing to plaintiff from the general contractor about $ 80,000 as final payment for work performed. Plaintiff's affidavit in the record shows the general contractor "refused to make final payment, unless it was reimbursed for the damage which it claims plaintiff caused".

[***99] There was withheld from the amount owed plaintiff the $ 15,648 which the general contractor claimed and this resulted in a settlement between the two in which the balance of the amount earned by plaintiff was paid. The affidavit of plaintiff's president asserts that plaintiff "had no choice but to make its own settlement with the general contractor".

This action is against the insurer for recovery under the terms of the policy. It is clear that damage due to the negligence of plaintiff in the course of its work was a covered risk. The insurer asserts a defense under two provisions of the policy. One provision is that the insured shall not "voluntarily make any payment" on any risk within the obligation of the policy; and the other is that no action shall lie against the insurer unless the insured shall have complied fully with all the terms of the policy, nor until the amount of the insured's obligation "shall have been finally determined either by judgment * * * or by written agreement of the insured, the claimant and the company."

Defendant's motion for summary judgment has been granted by the Appellate Division, reversing the Special Term, on the ground the policy provisions had not been complied with and there was no triable issue. The Special Term had been of opinion there was a factual issue. The answer alleges that defendant had not been given notice of the damage as soon as practicable; that it was not notified "of the pendency of said claim" and that "the first notice of the alleged claim" was the service of the summons and complaint on the defendant.

[*346] Plaintiff undertook to show in opposition to the motion for summary judgment that the company had been advised of the damage for which it covered plaintiff; that defendant's failure to act and the pressure resulting from the withholding of the large amount due for work performed compelled plaintiff to agree to the offset for damage; that the resulting settlement was not "voluntary" within the intention of the policy; and that the need for the insurer to join into a written agreement of settlement was waived.

Defendant examined the plaintiff's president Philip Rosen before trial and it was partly on the basis of this examination, referred to in an affidavit of defendant's vice-president, that defendant's motion for summary judgment was made. This testimony disclosed that plaintiff resisted the claim for damage by the general contractor but "They were holding a lot of my money for a long time, and this is something that I was more or less forced to go into."

[**382] When the deduction was made by the general contractor, a release was given to plaintiff and on the examination before trial Mr. Rosen [***100] testified he could not recall "after" such release what he did about notifying defendant of the claim. The affidavit of the defendant's vice-president in support of the motion reiterates in terms what the answer alleges: "that neither the plaintiff nor anyone in its behalf gave notice to the defendant nor was [it] consulted with reference to the payment".

Plaintiff's opposing affidavit, by Mr. Rosen, takes sharp issue with this statement. He says: "When the claim was made against the plaintiff, plaintiff notified the defendant, but defendant did absolutely nothing to adjust or otherwise process the claim. The net result was that when the time for final payment came, the general contractor refused to make final payment, unless it was reimbursed for the damage which it claims plaintiff caused, and which damage, if any, was covered under defendant's insurance policy." The affidavit added that the defendant would neither "assert nor deny" its "coverage" and that plaintiff was placed in an "untenable position" because of the large amount of money being held up "because defendant remained completely inactive under its insurance policy". He added that defendant did not "care how much of plaintiff's money was being tied up, it merely sat back and waited".

[*347] Defendant's vice-president made a reply affidavit addressed to this, in which he said "I note * * * that it is claimed that the plaintiff notified the defendant of the claim being made" for damage to the roof. He adds this significant statement: "Whether this is so or not is not in issue on this motion."

This on its face, and seen against the specific statements in Mr. Rosen's affidavit, seems an admission that what defendant asserted in its answer, "that neither the plaintiff nor anyone in its behalf gave notice to the defendant", is wrong; and that notice of it was in fact given. Whether defendant knowingly sat idle with notice of the claim asserted by the coinsured general contractor and with knowledge of the pressure that could be brought from that relationship, is another matter and not resolved by the affidavits.

Nor is the exact sequence of events conclusively

shown. At one point in the examination before trial plaintiff's president indicated that he did not know of the "exact amount" of the claim until the final settlement with the general contractor was due, and at another that he did not recall what was done "after" the release in notifying the insurance company of the claim; but at other points in the record he is unequivocal in stating the insurer had timely notice of the nature of the claim and the risk of liability (aside from the exact amount); and did nothing about it until the general contractor squeezed him into settlement.

[***101] The New York rule is that where an insurer "'unjustifiably refuses to defend a suit, the insured may make a reasonable settlement or compromise of the injured party's claim, and is then entitled to reimbursement from the insurer, even though the policy purports to avoid liability for settlements made without the insurer's consent'" (*Matter of Empire State Sur. Co.*, 214 N. Y. 553, 563, opn. per Seabury, J., restated in *Cardinal* v. *State of New York*, 304 N. Y. 400, 410).

But the insurer's obligation to act in good faith for the insured's interests may be breached in other ways than by refusing or neglecting to defend a suit. It may be breached by neglect and failure to act protectively when the insured is compelled to make settlement at his peril; and unreasonable delay by the insurer, in dealing with a claim, may be one form of refusal to perform which could justify settlement by the insured.

[*348] [**383] This seems the general rule: "The provision against settlement by insured cannot be taken advantage of by insurer, where it unreasonably delays to take any action, after notice of the claim" (45 C. J. S., Insurance, § 937, subd. b, p. 1072; see *Home Ind. Co.* v. *Snowden*, 223 Ark. 64; *Interstate Cas. Co.* v. *Wallins Creek Coal Co.*, 164 Ky. 778).

The Supreme Court of Nebraska, in *Otteman* v. *Interstate Fire & Cas. Co.* (172 Neb. 574), dealt with a problem closely similar to the one now here. The insurer over a period of seven months failed to act on the insured's report and subsequent inquiries about a claim within the policy. The insured settled the claim without the insurer's consent and was allowed to recover against the insurer notwithstanding a policy provision against settlement by the insured and a provision requiring the written consent of the insurer.

The court noted as a general rule in "All jurisdictions" that a "denial of liability" relieves the insured from the obligation not to settle (172 Neb., at p. 579). The opinion equated an unreasonable delay in acting to denial of liability.

The conclusion was: "We have no hesitancy in finding that the evidence amply discloses an unreasonable delay on the part of the defendant in processing the plaintiff's claim. We further find that such delay amounted to a denial of coverage and constituted a waiver of any right to insist on the policy provision regarding defense or settlement" (p. 583). The decision in *Interstate Cas. Co.* v. *Wallins Creek Coal Co.* (*supra*) was cited as a leading authority on the effect of unreasonable delay in taking any action. (See, also, Appleman, Insurance Law and Practice, Vol. 7A, § 4714.)

[***102] A triable issue of fact is presented in the present case on the issue whether defendant unreasonably delayed taking action on the negligence claim against plaintiff under circumstances where it had notice of the claim and knew or ought to have known of economic pressure for settlement exerted by the general contractor, also its insured, in such fashion as to waive the provisions of its policy against settlement by the insured without its permission in writing.

The order should be reversed and the motion for summary judgment denied, with costs.

DISSENT BY: BREITEL

DISSENT

[*349] Breitel, J. (dissenting). The dissenters do not dispute the rules of law stated on behalf of the majority. Disagreement, narrow but crucial, relates only to the failure of plaintiff to set forth on this motion for summary judgment the evidentiary facts establishing that it is able to prove that it gave defendant insurer notice of the claim made upon it by the contractor.

As quoted in the majority opinion all that plaintiff has ever said on this score is that: "When the claim was made against the plaintiff, plaintiff notified the defendant, but the defendant did absolutely nothing to adjust or otherwise process the claim." Any notification was denied by defendant. Plaintiff never stated the time when the notice was given, the content of the notice, the manner in which it was given, the place where given, or

to whom. Particularly important would be the content of the notice, assuming that it was ever given. To advise the insurer that the contractor was asserting a claim generally would mean nothing, unless the details of the claim were described. Nor would the insurer know unless it were told that the contractor was withholding moneys due. Nor would the insurer be on notice to pursue an adjustment within a given time span unless it were also told what the time demands were by the contractor and what were the time and money pressures on plaintiff. All these essentials are omitted. [**384] To top it off, plaintiff does not describe the response it received to the undescribed notice it gave at an unspecified time and place to an undesignated person. The bare conclusory assertion would not suffice as a particular under a demand for a bill of particulars, let alone as evidentiary facts required to defeate a motion for summary judgment (*Ehrlich* v. *American Moninger Greenhouse*, 26 N Y 2d 255, 259; *Kramer* v. *Harris*, 9 A D 2d 282, 283).

Accordingly, I dissent and vote to affirm the grant of summary judgment.

TAB 4

LURIA BROTHERS & COMPANY, INC., OGDEN METALS INC., OGDEN CORPORATION and LURIA INTERNATIONAL DIVISION, Plaintiffs-Appellants, Cross-Appellees, v. ALLIANCE ASSURANCE CO., LTD., COMMERCIAL UNION ASSURANCE CO., ASSMIJ NIEUW ROTTER DAM, EAGLE STAR INSURANCE COMPANY, LONDO & HULL MARITIME INSURANCE COMPANY, URBAINE UAP, ASSICUR-AZIONI D'ITALIA, LA BELGIQUE S.A., ASSURANCES ABELLE-PAIX, MUTUAMAR-SOCIETA DE ASS. PER AZIONI, LEVANTE, COMAR, SIAT (SOCIETA ITALIANA ASSICURACIONI TRASPORTI), RIUNIONE ADRIATICA, SICURTA FRA ARMATORI, TOKIO FIRE & MARINE INS. CO., LTD., TAISHO MARINE & FIRE INS. CO., LTD., NEUCHATELOISE COMPAGNE SUISSE, EUROPA, ASSURANCES GENERALES de FRANCE, L'ASSURANCES LIEGEOISE, BOREAS, PACIFIC EMPLOYERS INSURANCE CO., AMERICAN INTERNATIONAL UNDERWRITERS, ITALIA ASSICURAZIONI KEMPER, LANGUEDOC SOCIETE d'ASSURANCAS, CORNHILL INSURANCE CO., LTD., SCOTTISH LION INS. CO., LTD., DE VADERLANDSCHE, PHOENIX CONTINENTAL S.A., L'ALSACIENNE, BLOCK SEA & BALTIC GENERAL INS. CO., LTD., LE MONDE, S.A.A.G. 1857 BRUXELLES, RIUNIONE ADRIATICA, L'INDEPENDANCE, PROVIDENTIA, ATLAS, ALLIANZ, and any and all underwriters subscribing to Marine Liability Policy numbered 3110 and Mari Excess Liability Policy numbered 3111, CITY INSURANCE COMPANY, Defendants-Appellees, Cross-Appellants

Nos. 85-7002, 85-7004, 85-7028

UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

780 F.2d 1082; 1986 U.S. App. LEXIS 21742; 1986 AMC 1539

April 29, 1985, Argued
January 10, 1986, Decided

PRIOR HISTORY: [**1] Cross-appeals from a judgment of the United States District Court for the Southern District of New York, Charles L. Brieant, Judge, awarding plaintiffs $210,186.63, representing, with adjustments not relevant on this appeal, $1,025,000.00 indemnity to plaintiffs against defendants under two liability insurance policies plus $89,708.14 in reimbursed legal fees, less an offset for restitution of $900,000.00 by plaintiffs to defendants based on the rescission, ordered sua sponte by the court, of an agreement between plaintiffs and defendants.

DISPOSITION: Reversed as to restitution; affirmed in all other respects.

CORE TERMS: underwriter's, vessel's, cargo, voyage, giorgis, restitution, settlement, shipowner's, indemnity, gratia, liability policies, henrijean, scrap, charterer, telex, coverage, turnings, loading, insurer, potential liability, sinking, indemnify, claimant's, assured, void, nondisclosure, legal expenses, cross-appeal, uninsured, warranties

COUNSEL: Patrick V. Martin, New York, New York (Douglas R. Burnett, Hill, Rivkins, Carey, Loesberg, O'Brien & Mulroy, New York, New York, of Counsel) for Plaintiffs-Appellants, Cross-Appellees.

Richard E. Repetto, New York, New York (John A.V. Nicoletti, James P. Krauzlis, Donovan Maloof Walsh & Kennedy, New York, New York, of Counsel), for Defendants-Appellees, Cross-Appellants.

JUDGES: Van Graafeiland and Pratt, Circuit Judges, and Morris E. Lasker, Senior District Judge for the Southern District of New York, sitting by designation.

OPINION BY: PRATT

OPINION

[*1084] PRATT, [**2] Circuit Judge:

This case arises out of the sinking of a cargo ship on the high seas with the loss of all crew members and passengers. The issues, of course, are over money: to what extent shall plaintiffs Luria Brothers & Company, Inc., et al., hereinafter collectively referred to as "Luria", who were charterers of the ill-fated vessel, recover from defendants Alliance Assurance Co., Ltd. et al., hereinafter collectively referred to as "underwriters", for financial burdens resulting from the loss and the events leading up to it. Luria, having settled with the cargo owners and the personal representatives of those who lost their lives in the sinking, sought in the court below indemnity from the underwriters for the settlement payments made and for attorneys fees incurred in the settled cases. The underwriters denied any obligation to Luria.

The district court, after a nonjury trial, found Luria to be entitled to the claimed indemnity. But, for reasons soon to be explained, it also *sua sponte* ordered restitution to the underwriters of a $900,000 *ex gratia* payment they had earlier made to Luria.

Luria appeals from the order of restitution. The underwriters cross-appeal from [**3] [*1085] the award to plaintiffs of indemnity and legal fees.

BACKGROUND

Luria, an international dealer in scrap metal, regularly charters vessels to export the scrap. In connection with its export business, Luria purchased various insurance policies to cover its liability as a charterer and loading stevedore ("liability policies") as well as possible loss or damage to its cargo ("cargo policies"). Frank B. Hall & Co. of New York, Inc., ("Hall"), a New York insurance broker, placed and serviced these policies for Luria through Luria's Belgian broker, Henrijean & Cie of Brussels ("Henrijean").

Three insurance policies are relevant here: the primary liability policy, H/L 3110, the first excess liability policy, H/L 3111, and the cargo policy, H/L 3222. J. Haenecour & Co. of Brussels and Antwerp ("Haenecour") acted as underwriting agent and lead underwriter on behalf of the underwriters who subscribed to one or more of the three policies. As lead underwriter Haenecour was entrusted with authority to deal with all matters of rating, conditions, and settlement of claims in connection with the policies.

In July 1979 Luria entered into a time charter with Evimeria Compania Naviera, [**4] S.A., Panama, ("shipowner"), owner of a 17-year-old bulk carrier, Agios Giorgis. Under the terms of the charter party, Luria could employ the vessel to carry "scrap, excluding motor blocks and including turnings which, if loaded shall be chemically treated."

On August 22, 1979, the Agios Giorgis commenced loading 14,586 long tons of Luria's metal turnings at the port of Chicago. Luria admits that the cargo was loaded against the advice of its loading inspector, without being chemically treated, and that the vessel sailed with the turnings temperature in excess of permitted regulations. Further, Luria concedes that this resulted in breach of certain warranties in the cargo and liability policies that rendered coverage on those policies null and void for the voyage from Chicago to Newark, New Jersey.

On September 17, 1979, the vessel arrived at New Haven, Connecticut, to load additional scrap cargo on top of the turnings. The next day a fire was discovered in the turnings in the No. 5 hold of the vessel. Since the port of New Haven is devoted primarily to the discharge and storage of petroleum products, the harbor master ordered the burning Agios Giorgis to leave New Haven to avert [**5] potential disaster. She did so, and arrived at Luria's terminal at port Newark, New Jersey, on September 22. In these few days, the fire had spread throughout all of the vessel's holds, and despite attempts to extinguish the fire, temperatures eventually reached in excess of 1100 degrees fahrenheit.

After discussions among Luria, the shipowner, and other parties, it was decided to discharge all the turnings and scrap, an operation that was completed on November 9, 1979.

While the discharge was proceeding, representatives of Luria, Hall, Henrijean, and Haenecour met in Belgium in October. All present conceded that in view of the breach of warranties, the policies did not cover Luria's liability for loss and discharge of the cargo, for consequent delays, for damage to the vessel, or for possible third-party claims. Nevertheless, Luria requested from the underwriters an *ex gratia* payment -- a voluntary contribution not required by the policies -- to help Luria bear the loss.

In support of its request, Luria specifically dwelt upon the extensive business relationship between the parties over the past twenty years and suggested that it could direct additional future insurance [**6] business at profitable rates to the underwriters, if Haenecour would make the requested *ex gratia* payment. Although no agreement to make such a payment was reached at the October meeting, Haenecour told Luria to come back with a business proposition at a future meeting.

After discharge of the cargo and cleanup of the vessel, Luria decided to send the [*1086] Agios Giorgis on a second voyage, this time to Japan with a cargo of heavy scrap from port Newark. Luria had a good reason to send the vessel to Japan since repairs for the damage caused by the fires, for which Luria was liable to the shipowner, could be had more cheaply in Japan.

Luria sought liability coverage for the voyage, and Henrijean negotiated a limited reinstatement of insurance with Haenecour on a new policy; on November 13, the reinstatement was made subject to "no aggravation of risk" by the proposed addendum to the charter party that would cover the second voyage.

Three days later, Luria and the shipowner formally agreed, by executing the addendum to the existing charter party, to employ the Agios Giorgis for the second scrap voyage to Japan. The shipowner warranted that "the vessel [was] in class [**7] ready to commence loading". Henrijean reviewed the addendum and forwarded it to the underwriters on November 26, 1979.

Loading of the scrap for the second voyage was completed on November 29, 1979, and the vessel set sail for Japan the following day. On board was a crew of 27, including the captain's wife, infant son, and three other members of his family. The vessel passed through the Panama Canal, bunkered at Los Angeles, and continued across the Pacific.

On January 7, 1980, the vessel M/S Nichirin Maru received an urgent distress call from the Agios Giorgis, reading in relevant part: "Indicate crack at hold No. 5 stop water under control stop * * * please attend master." The Nichirin Maru hastened to aid the vessel and sighted the Agios Giorgis the following day. The Agios Giorgis advised that she intended to continue her voyage under the escort of the Nichirin Maru, that she had sustained two large cracks in the plates at her No. 5 hold, that she was listing from four to five degrees, and that her pumps had the sea water coming through the cracks under control.

Several hours later, the Agios Giorgis sent a distress message indicating that one crack had enlarged to between [**8] four and five feet. But after the Nichirin Maru indicated the next day that it must soon abandon escort due to diminishing bunkers and supplies, the Agios Giorgis responded that conditions on the damaged vessel had stabilized and authorized the cessation of rescue efforts. The Nichirin Maru then altered her course and returned to Japan.

The following day, the vessel Hoegh Miranda received an emergency distress signal from the Agios Giorgis. As the Hoegh Miranda sped to assist, the Agios Giorgis informed her that water was rushing into two holds and that the vessel was beginning to list toward the right. At that time the winds were blowing up to full gale force, the sea was stormy, and the waves had reached a height of ten meters. A short time later, in the early hours of January 11, while within sight of the Hoegh Miranda, the Agios Giorgis sank, leaving no survivors.

About one month later, on February 7, 1980, with knowledge that the Agios Giorgis had sunk, representatives of Luria, Hall, Henrijean, and Haenecour met again in Belgium. Following that meeting representatives of Henrijean and Haenecour met alone and agreed to a final figure of $900,000 for the *ex gratia* payment [**9] to Luria. Their agreement was embodied in a telex summary of the meeting dated February 8, 1980, sent by Henrijean to Haenecour, who approved and confirmed the agreement in a telex also dated February 8. The first telex read, in pertinent part, as follows:

> re: Luria -- open cover 3222
>
> hereunder agreement was reached on 7 February 1980 during meeting held in antwerp being understood that leader of cover is only engaging his own line and that we have to convince each and every co-underwriters [sic] to follow the same commercial approach. * * *
>
> referring to * * * "aegis [sic] giorgis" (voyage Chicago to port Newark) the breach of warranties spelled out in open cover render coverage null and void. however, in view of long standing relationship, it was agreed, subject to here-above [*1087] remark, to contribute into assureds losses within the scope of the open cover as follows:
>
> 1) cargo contribution- 35 pct of dlrs 2 million or dlrs 700.00 less return premium.
>
> 2) charterers liability contribution: dlrs 200.000 less return premium
>
> total contribution: dlrs 900.000 ot [sic] being understood that:
>
> -- there will be on supplementary contribution whatsoever out [**10] of all aegis [sic] giorgis * * * casualties resulting from the fires.
>
> * * *
>
> henrijean will develop best possible efforts to convince co-unds and/or reinsurers to follow same settlement and we hope toreport [sic] to you favorably as soon as possible.

The telex was forwarded to Hall, and then to Luria, which did not respond to Hall's invitation to state anything in the telex at variance with Luria's understanding.

In August 1981 Luria was served with a third-party complaint by the shipowner in an action brought on behalf of the underwriters for the sunken cargo. In September 1981 a wrongful death action seeking total damages of $9,400,000 against Luria and others was filed in the Southern District of New York on behalf of the estates and relatives of 22 of the 27 men, women, and children who had perished on the Agios Giorgis.

Luria sent the summonses and complaints in the death and cargo actions to Hall. By telex dated October 7, 1981, Hall informed Henrijean of the pendency of the actions and requested that he inform the underwriters and ask them to confirm appointment of counsel to "protect all interests".

On October 14, Henrijean replied:

> we refer [**11] to your telex of 7 October, we have informed the leading underwriters, who are declining liability in view of the agreement with the assured of 7 February 1980 * * *.

The cargo action was settled, and while Luria did not contribute to the settlement, it did incur pre-settlement legal expenses of $30,224.

In the wrongful death action the parties reached a final settlement in February 1983, to which Luria contributed $1,217,656.50. In return for its contribution, Luria received full releases from the death claimants and from the shipowner, as well as an indemnity from the shipowner's P & I Club for any future claims by the estates of the nonsuing decedents. Luria also incurred $59,485 in legal expenses in this action.

In May 1983 Luria brought the instant suit for indemnity against the underwriters who had subscribed to liability policies 3110 and 3111. Following trial, the district judge issued a 62-page "Findings and Conclusions and Order" in which he first addressed "the extent, if at all, to which Luria was under a legal liability to the death claimants with whom it settled". As discussed below in more detail, this question was central to Luria's suit for if Luria [**12] faced no potential liability from the death claimants, then the underwriters did not have to indemnify Luria for its contribution to the settlement. The court found that Luria was potentially liable to the death claimants, that the policies covered this type of liability, and that the underwriters, therefore, were required to indemnify Luria for the settlement.

The court then addressed whether Luria's claim was barred by the agreement under which the *ex gratia* payment was made. The underwriters argued that Luria's acceptance of the $900,000 *ex gratia* payment, pursuant to the provisions under which it was paid, precluded any indemnification for liability arising out of the sinking on the second voyage. However, the court reasoned that:

> It is inconceivable that a businessman of Mr. Haenecour's sophistication would have agreed to a $900,000 *ex gratia* payment toward Luria's losses from the first voyage, if the question of the insurer's [*1088] liability for potentially staggering indemnification on the second voyage remained an open one. Similarly, it is unlikely, and indeed impossible, that Luria would have consented to receive approximately 25% indemnity on [**13] its cargo losses for the first voyage, for which it, having breached the policy warranties, knew it was entitled to receive nothing, if it had been aware that by doing so, it would later be claimed to have released the insurers from any responsibility for indemnity against immense and undetermined third-party claims arising out of the sinking on the second voyage.
>
> The effect and scope of the disputed provision in the February 8th telex presents a fundamental ambiguity. In the total absence of any persuasive evidence establishing that the parties enjoyed a shared understanding of this ambiguous clause, the Court is led to conclude, and I find, that no enforceable contract was created at the time of the February conference * * *. [footnote omitted].

The district court then found that since Luria "apparently" had not directed the additional promised business to the underwriters, a promise the court thought was composed of "precatory words * * * too vague * * * to constitute consideration for the *ex gratia* payment, and its purposes for making the agreement were frustrated. Even though the underwriters had never requested return of the payment, the court concluded that [**14] "equity requires that the underwriters be made whole by restoration of the amount of the *ex gratia* payment," deemed the pleadings amended on this point to conform to the proof, pursuant to Fed. R. Civ. P. 15, and offset the $900,000 *ex gratia* payment against the indemnity required of the insurers.

The court also awarded Luria reimbursement for legal expenses incurred in defense of the wrongful death and cargo actions.

Finally, the district court rejected the underwriters' claim that the amount of indemnity should be reduced by the value of an additional benefit Luria had received under the settlement between the shipowner and Luria -- a release from its previously agreed-to liability to the shipowner for damage to the vessel caused by the turnings fire.

On appeal, Luria contends that: 1) the district court abused its discretion by *sua sponte* ordering restitution of the $900,000 to the underwriters, 2) the underwriters were not entitled to any restitution, 3) there was consideration for the $900,000 payment, and 4) the trial court erred in finding the February 7 agreement unenforceable.

On its cross-appeal, Alliance argues that the district court erred: 1) in failing [**15] to hold as a matter of law that the liability policies on the trans-Pacific voyage were void *ab initio* on account of Luria's failure to disclose facts material to the risk; 2) in finding coverage under the liability policies for the type of potential liability assigned to Luria; 3) in awarding Luria legal costs of defending claims arising out of the sinking; and 4) in not reducing the indemnity award by the amount of Luria's uninsured liabilities on the first voyage that were released by the shipowner in the settlement agreement. Finally, Alliance urges that if the district court erred in holding the February 7 agreement null and void, it further erred by failing to apply the agreement's terms and conditions which released the underwriters from the obligation to indemnify Luria.

We agree that the district court erred by ordering restitution, and we reverse that part of the judgment without prejudice to the bringing of another suit by Alliance or the other underwriters for restitution of the *ex gratia* payment. In view of this disposition, we need not address Luria's other claims. We reject each of the arguments raised by Alliance on its cross-appeal.

DISCUSSION

A. [**16] *Luria's Appeal.*

Under Fed. R. Civ. P. 15(b), "when issues not raised by the pleadings are tried by [*1089] express or implied consent of the parties, they shall be treated in all respects as if they had been raised in the pleadings." In such a case, failure to amend the pleadings to conform them to the evidence and raise these issues does not affect the result of the trial, Fed. R. Civ. P. 15(b), although the trial judge may allow such an amendment, even after judgment, either upon motion of any party, *id.*, or *sua sponte*, 6 C. Wright & A. Miller, *Federal Practice and Procedure* § 1493, at 461 (1971).

Regardless of whether the pleadings are amended, however, the crucial test is whether the parties have consented to litigation of the issue; it must have been tried by their express or implied consent. Fed. R. Civ. P. 15(b); *Browning Debenture Holders' Committee v. DASA Corp.*, 560 F.2d 1078, 1086 (2d Cir. 1977).

Here, it is clear that the issue of restitution was not tried by the *express* consent of the parties. In essence, counsel for the underwriters urge otherwise by claiming that they had pled the February 7 agreement as an affirmative [**17] defense and that the court did no more than treat the affirmative defense as a counterclaim. The answer included in the appendix, however, contains no reference whatsoever to the February 7 agreement.

In any event, whether parties have implicitly consented to the trial of an issue not presented by the pleadings depends on whether they recognized that the issue had entered the case at trial. 6 C. Wright & A. Miller, *supra* § 1493, at 462. Usually, consent may be implied from failure to object at trial to the introduction of evidence relevant to the unpled issue. *Usery v. Marquette Cement Manufacturing Co.*, 568 F.2d 902, 906 (2d Cir. 1977).

Some evidence introduced at trial here arguably was relevant to the question whether there should be a rescission and restitution, e.g., the terms of the agreement and the different interpretations given the agreement by the parties. But, it would appear that the primary purpose for introducing the terms of the agreement and the parties' differing interpretations was to determine whether the underwriters had to indemnify Luria for its contribution to the settlement. That such evidence, relevant to both pled and unpled issues, [**18] was introduced without objection does not imply consent to trial of the unpled issues, absent some obvious attempt to raise them. *McLean-Behm Steel Erectors, Inc. v. Occupational Safety and Health Review Commission*, 608 F.2d 580, 582 (5th Cir. 1979); *see Browning Debenture Holders' Committee*, 560 F.2d at 1086. And it is hard to find such an attempt when the questions of rescission and restitution were not even mentioned, let alone discussed below, until the district court issued its decision.

At a post-judgment, rule 52 hearing, the district court stated:

> I told you time and again during this trial that it looked to me as if the $900,000 and the purposes for it were totally frustrated and you ought to address yourself to it. I am afraid on some of those occasions I did not tell you on the record but I am sure I mentioned it at least once and I know I told you a couple of other times.

After a careful review of the trial transcript, we have found no instance where the trial judge made such a comment on the record. Assuming he did so off the record, such a comment was insufficient to warn Luria that the trial judge was considering [**19] restitution of the payment, relief that the underwriter had not even requested. Under the circumstances, therefore, it is not fair to infer that Luria had consented to trial of the issue of restitution.

Moreover, we think that the district court's action prejudiced Luria. The underwriters who contributed to the $900,000 payment fall into three categories: 1) the defendant liability underwriters; 2) the nonparty cargo underwriters; and 3) the defendant liability underwriters, who also subscribed to the cargo policy. Luria argues that:

> Each of the twelve non-party cargo underwriters had to specifically agree to a contribution to the *ex gratia* payment [*1090] and did not act through the lead underwriter clause. * * * This was in sharp contrast to the issue of the declination of coverage by the party underwriters under the charterer liability policies 3110 and

> 3111. These underwriters acted through the lead underwriter. This distinction was fundamental in the formulation of pre-trial discovery by Luria. * * * Had Luria been apprised of the possibility of a recission of the *ex gratia* payment agreement, it would have certainly insisted upon depositions of the individual [**20] underwriters and discovery of their files.

Although we express no opinion as to the merits of Luria's argument, Luria should have been entitled, through normal pretrial discovery, to explore this and other possible defenses to restitution. The absence of any opportunity to do so constitutes sufficient prejudice to warrant reversal for that part of the district court's order granting restitution of the $900,000 payment. *See International Harvester Credit Corp. v. East Coast Truck*, 547 F.2d 888, 890-91 (5th Cir. 1977) (improper to order rescission of contract under Rule 15(b) when rescission not raised in the pleadings or at trial); *cf. Rosenwald v. Vornado, Inc.*, 70 F.R.D. 376, 377 (E.D. Pa. 1976) (court denied post-trial motion to amend pleadings to add a counterclaim when matter was not admitted into evidence and plaintiffs did not have an opportunity to present a defense to the counterclaim).

We recognize the district judge's concern for the possible injustice if, indeed, the parties' intentions for the February 7 agreement were as he speculated. We therefore leave open the opportunity for the underwriters, some of whom were not formal [**21] parties to this action, to pursue the matter of restitution in a separate action.

B. *Alliance's Cross-Appeal* .

On its cross-appeal Alliance has asserted five major arguments, none of which is persuasive.

1. *Luria's Nondisclosure of Material Facts*. Alliance contends that the district court erred as a matter of law in failing to hold the liability policies void *ab initio* on account of Luria's failure to disclose facts material to the covered risk.

When first informed of the pendency of the cargo and the death actions against Luria, the underwriters did not raise a nondisclosure defense, but instead informed Luria that they "declined liability in view of the agreement with the assured of 7 February 1980." By failing to raise the nondisclosure defense until several years later, long after they originally had denied liability on another ground, the underwriters waived the defense. It is settled that "when one specific ground of forfeiture is urged against the claim, and a refusal to pay is based upon a specific ground, all other grounds are waived." 16C Appleman & Appleman, *Insurance Law and Practice*, § 9260, at 393 (1981); *see General Accident Insurance Group v. Cirucci*, 46 N.Y.2d 862, 863-64, 414 N.Y.S.2d 512, 514, 387 N.E.2d 223 (1979); [**22] *Appell v. Liberty Mutual Insurance Co.*, 22 A.D.2d 906, 255 N.Y.S.2d 545, 547 (2d Dep't 1964); *The Anthony D. Nichols*, 49 F.2d 927, 930 (S.D.N.Y. 1931).

The underwriters claim that they did not learn of the unseaworthy condition of the vessel until April 1983 and, since they had no knowledge in October 1981 of the facts giving rise to the nondisclosure defense, they insist that they could not have waived the nondisclosure defense by their original denial on other grounds at that time.

It is true that an insurer cannot waive a defense by asserting another defense as grounds for declination if it had no knowledge of the facts giving rise to the unasserted defense. *See Ginsburg v. Pacific Mut. Life Ins. Co. of California*, 89 F.2d 158, 160 (2d Cir.), *cert. denied*, 302 U.S. 708, 82 L. Ed. 546, 58 S. Ct. 27 (1937). But, at the time the underwriters here initially declined liability, they knew that the vessel had experienced severe fires in the holds with temperatures in excess of 1100 degrees fahrenheit, and had later sunk. They also had commissioned an earlier survey by the London Salvage Association, [*1091] [**23] which indicated that there had been extensive damages to the vessel from the fire, and that repairs had been deferred until arrival in Japan.

Finally, their argument here is belied by their own action. The February 7 agreement provided, in part, that "there will be no supplementary contribution whatsoever out of all aegis [sic] giorgis * * * casualties *resulting from the fires*." [emphasis added]. This part of the agreement is what the underwriters must have had in mind when they declined liability in 1981, since the remainder of the agreement provides no possible basis for avoiding liability. It follows that when they declined liability, the underwriters must have though that the fire had weakened the vessel to the point of making it

unseaworthy. It strains our credulity when they now argue that they didn't learn the ship was unseaworthy until 1983.

In any event, even if the underwriters did not have actual knowledge of the facts giving rise to the misrepresentation defense in 1981 when they declined liability on other grounds, the circumstances were more than adequate to put them on notice that Luria had not disclosed the unseaworthy condition of the vessel when it sought [**24] insurance for the second voyage. Hence, they had constructive knowledge and this alone was sufficient. 16C Appleman & Appleman, *Insurance Law and Practice* § 9260, at 394 & n.11 (1981); *see Zeldman v. Mutual Life Insurance Co. of New York*, 269 A.D. 53, 53 N.Y.S.2d 792, 794 (1st Dep't 1945) (insurer normally does not waive rights unless acting with actual knowledge of the facts; constructive knowledge, however, may be sufficient if insurer disregards circumstances putting it on notice).

2. *Coverage Under the Policy*. The underwriters next argue that the district court erred in finding coverage under the liability policies for the type of potential liability it assigned to plaintiffs in finding indemnity for the settlement.

When an insurer declines coverage, as here, an insured may settle rather than proceed to trial to determine its legal liability. *Bunge Corp. v. London and Overseas Insurance Co.*, 394 F.2d 496, 497, (2d Cir.), *cert. denied*, 393 U.S. 952, 89 S. Ct. 376, 21 L. Ed. 2d 363 (1968). In order to recover the amount of the settlement from the insurer, the insured need not establish actual liability to the party [**25] with whom it has settled "so long as * * * a potential liability on the facts known to the [insured is] shown to exist, culminating in a settlement in an amount reasonable in view of the size of possible recovery and degree of probability of claimant's success against the [insured]." *Damanti v. A/S Inger*, 314 F.2d 395, 397 (2d Cir.) *cert. denied*, 375 U.S. 834, 11 L. Ed. 2d 64, 84 S. Ct. 46 (1963).

On the facts known to Luria at the time of settlement, Luria had potential liability to the death claimants. The district court found it probable that a trial jury would have concluded that the unseaworthiness of the vessel caused the sinking and the earlier fire was a concurrent cause of the sinking. While it is generally true that "a time charterer assumes no liability flowing from the unseaworthiness of the vessel", *Klishewich v. Mediterranean Agencies, Inc.*, 302 F. Supp. 712, 713 (E.D.N.Y. 1969), a time charterer may be held liable for foreseeable damage to others resulting from loading and storage of cargo, *see, e.g., In re Skibs A/S Jolund*, 250 F.2d 777, 787 (2d Cir. 1957), *cert. denied*, 356 U.S. 933, 2 L. Ed. 2d 763, 78 S. Ct. 772 (1958). [**26] Here, even though Luria, as charterer, might ordinarily have owed no legal duty to the seamen for the unseaworthiness of the vessel, we detect no error in the finding below that a jury might well have found that Luria's disregard of explicit standards for such cargo presented a foreseeable danger of combustion within the cargo of untreated turnings, with Luria under a duty of care to those who foreseeably might have been injured as a result of its negligence, *see petition of Kinsman Transit Company*, 338 F.2d 708, 722 (2d Cir. 1964), and thus obligated to ascertain that the damages caused by the fire had been repaired adequately before loading the vessel for departure on the second voyage.

[*1092] Under the circumstances, where Luria, though a time charterer, actively participated in exposing third parties to an inherently dangerous condition that it helped create, the possibility for joint liability, along with the shipowner, for damages to these third parties was high. Thus, the district court amply demonstrated Luria's potential liability.

Further, one need only read the first section of both liability policies to determine that they encompassed this [**27] type of liability. Those sections read in pertinent part:

> Charterers Liability.
>
> This insurance to cover the liability whether legal or contractual of the Assureds insofar as they are interested in the shipment of ferrous and/or nonferrous scrap including turnings * * *.

Luria's potential liability for its failure "to ascertain that the damages caused by the fire had been repaired adequately before loading" the scrap for the second voyage, falls within the broad scope of Luria's insurance against liability "insofar as [it is] interested in the shipment of * * * scrap".

3. *Payment of Legal Expenses by Alliance*. The underwriters object to the award of legal fees to Luria,

arguing that under the terms of the liability policies, payment of such expenses was contingent upon the underwriter's consent. The pertinent language of the policies provides that:

> This insurance to cover the liability * * * of the Assureds * * * including * * * all legal expenses and/or costs incurred in defending claims whether founded or unfounded subject to the notification and acquiescence of the underwriters * * *.
>
> * * *
>
> Costs [excluding expenses for salaried employee [**28] and retainer counsel] incurred by the Assured shall be payable by the underwriters only if underwriters hereon give written consent to the incurring of such costs in respect of any particular claim, suit or proceeding * * *.

As a matter of common sense, once the underwriters had disclaimed all liability, Luria had no need thereafter to obtain their approval for legal expenditures. Since, as we have shown above, the underwriters were liable for indemnification, they were also liable for Luria's reasonable legal fees in defending and settling the underlying claims.

4. *Reducing the Indemnity Award by the Amount of Luria's Released Uninsured Liabilities.* The underwriters point out that the fires on the Chicago to Newark voyage had caused extensive damage to the vessel's hull, that by agreement with the shipowner, Luria was liable for the cost of repairs, and that Luria had no insurance coverage for this liability since the warranties of the insurance policies had been breached. They reason that this "uninsured contractual liability" of Luria was released in the overall settlement agreement to which the shipowner and Luria were parties, and they conclude that "underwriters [**29] cannot be required to indemnify Luria for the amounts expended to release itself from any uninsured liability" and that they should therefore be credited with the value Luria received as a result of the release of its uninsured liabilities to the shipowner.

At a post-trial hearing, the district court noted that since under admiralty law the shipowner's claim against Luria sank with the ship the release did not affect "the allocation of the settlement * * * between the owner and charterer at all, so I really think that there is no monetary value that can be assigned to that." Similarly, in the "Findings and Conclusions and Order" the court found that "to attribute any monetary value to this release or indemnity, on the present record, would be speculative and unjustified." We find no error in the court's conclusion.

5. *The Effect of the February 7 Agreement.* The underwriters argue that if, as Luria contends in attacking restitution, the district court erred by holding the February agreement null and void, then it further erred by failing to apply those terms of that agreement that release the underwriters from the obligation to indemnify Luria. This argument fails, however, [**30] because [*1093] the February 7 agreement, even if valid, would not have released the underwriters.

In making this argument, the underwriters rely on that part of the February 7 telex which stated that "there will be no supplementary contribution whatsoever out of all aegis [sic] giorgis * * * casualties resulting from the fires." This statement, however, must be read in the context of an earlier paragraph in the telex which began with the words "Referring to * * * Aegis [sic] Giorgis (voyage Chicago to Newark)", words which limit the impact of the agreement to the vessel's first voyage and have no effect on the later voyage across the Pacific.

CONCLUSION

On Luria's appeal, that portion of the district court's order requiring restitution of the $900,000 payment is reversed without prejudice to another action by the underwriters for restitution. In all other respects the district court's order is affirmed.

TAB 5

PEPSICO, INC., Plaintiff, v. CONTINENTAL CASUALTY COMPANY, Defendant

No. 85 Civ. 5518-CLB

UNITED STATES DISTRICT COURT FOR THE SOUTHERN DISTRICT OF NEW YORK

640 F. Supp. 656; 1986 U.S. Dist. LEXIS 23831; 1988-1 Trade Cas. (CCH) P68,079

June 23, 1986, Filed

SUBSEQUENT HISTORY: On Motion for Clarification July 30, 1986.
On reconsideration by, Clarified by, Motion denied by, in part, 07/30/1986

DISPOSITION: The court granted the motion for partial summary judgment, as defendant did not show that there was no possible factual basis on which it might be obligated to indemnify, but denied the motion in part, as partial costs were those of plaintiff, and not its insured officers and directors; the court denied defendant's motion to dismiss.

CORE TERMS: settlement, indemnification, dishonesty, antitrust, insured, coverage, insurance policy, indemnify, insurer, Wrongful Acts, class action, public policy, duty to pay, final judgment, contemporaneous, defending, dishonest, customer, by-law, summary judgment, unreasonably, Insurance Law, fraud claims, policy definition, burden of proving, obligated to pay, final adjudication, good faith, reimbursement, accounting

COUNSEL: [**1] Ronald S. Rolfe, Louis M. Solomon, Jonathan D. Thier, Lawrence M. Rolnick, Cravath Swaine & Moore, for Plaintiff.

Nancy Barton, Dennis Block, Weil Gotshal & Manges, Stewart Ross, Cathy Simon, Ross, Dixon & Masback, for Defendant.

JUDGES: Brieant, J.

OPINION BY: BRIEANT

OPINION

[*657] MEMORANDUM & ORDER

Brieant, J.

Plaintiff PepsiCo, Inc. ("PepsiCo") brought this action against defendant Continental Casualty Company ("Continental") to recover money paid to settle litigation on behalf its officers and directors; it also asserts claims against Continental for fraud and antitrust violations. Continental had issued a policy insuring PepsiCo's directors and officers from certain claims against them. PepsiCo now seeks an interpretation of the underlying policy agreement in the form a partial summary judgment motion. Continental has moved to dismiss various portions of the complaint.

PepsiCo announced to the public in November 1982 that it had discovered "accounting irregularities" in several of its international operations, including Mexico [*658] and the Philippines. Employees in those countries had falsified accounts to improve the apparent performance of their operations. PepsiCo [**2] consequently had to restate its consolidated earnings for 1978-1981 and the first three quarters of 1982.

Predictably, several suits under well-known Rule 10b-5 were filed against PepsiCo, its directors and officers, its accounting firm, Arthur Young & Co., and a former officer, Richard Ahern, alleging a "fraud on the market" because of the false financial statements. These suits were consolidated before then Judge Abraham D. Sofaer of this district. The consolidated amended complaint alleged violations on the part of all defendants of Section 10 of the 1934 Securities Act as well as a common law claim for fraud and reckless and negligent misrepresentation. On August 23, 1984, Judge Sofaer certified a class for the Securities Act claim.

In February, 1983 the Securities and Exchange Commission also initiated an investigation into the circumstances of the PepsiCo false financials to determine whether PepsiCo or its directors and officers had violated any of the federal securities laws. As part of this investigation the S.E.C. interviewed PepsiCo officers and managers and partners and employees of Arthur Young & Co. The S.E.C. subsequently charged PepsiCo with violations of certain [**3] anti-fraud and reporting provisions of the Securities Act. Mr. Ahern was indicted by a Federal Grand Jury and pled guilty to criminal charges of fraud. He was sentenced in April 1984.

On March 4, 1985 attorneys for PepsiCo, its inside directors and its outside directors reached a tentative settlement agreement with class plaintiffs' counsel. PepsiCo counsel approached Continental seeking its approval of the proposed settlement. When they were unable to reach an accord on the settlement because of time pressures, PepsiCo and Continental entered into a non-waiver agreement. By this agreement Continental obtained the right to review the settlement after the fact but without losing its right under the policy to object to the reasonableness of the settlement.

The Class Action parties entered into a stipulation of settlement on March 15, 1985 and Judge Sofaer approved the settlement as fair, reasonable and adequate on April 26, 1985, after having expressed himself as "shocked, quite surprised at the amount." (Ex. F. Simon affidavit at 10). Under the terms of the settlement, PepsiCo paid $22,067,754 into a Settlement Fund. In exchange, plaintiffs in each of the actions released all defendants [**4] from liability. All of plaintiffs' claims against all defendants, including the non-certified common law or state law claims were dismissed with prejudice.

The Directors and Officers Liability Policy at issue here covered the period July 28, 1981 to July 28, 1984. After extending that coverage for thirty days, PepsiCo and Continental agreed to a new policy for the period August 27, 1984 to August 27, 1987. Both policies included a provision permitting either party to cancel the policy unilaterally. Pursuant to that provision, Continental cancelled the 1984-1987 policy effective June 29, 1985.

PepsiCo Motion for Summary Judgment

By its motion for partial summary judgment PepsiCo has asked this Court to make the following four interpretations of the underlying policy. First, that Continental had a contemporaneous duty to pay the defense costs to the directors and officers as they incurred them. Second, that nothing in the directors and officers policy and no public policy precludes reimbursement to PepsiCo for the settlement and defense costs. Third, that Continental cannot pro rate its payments on the directors and officers insurance policy according to relative degrees of [**5] liability as between the insured and other defendants including the corporation. Fourth, if Continental is permitted to make some allocation according to degree of fault, then it should bear the burden of proving liability on the part of the corporation itself and Arthur Young.

[*659] *Contemporaneous Duty to Pay Defense Costs*

The parties agreed at the time the policy was issued that a "loss" should include the cost of defending legal actions brought against directors and officers for "Wrongful Acts." The policy definition of Loss states that,

> "Loss shall mean any amount which the Directors and Officers are legally obligated to pay for which they are not indemnified by the Company, or for which the Company may be required or permitted by law to pay as indemnity to the Directors and Officers, for a claim or claims made against them for Wrongful Acts, and shall include . . . amounts incurred in the defense of legal actions, claims or proceedings and appeals therefrom . . ." para. III.(d) of Policy, Ex. 1 to Rolfe Affidavit.

The "Wrongful Acts" covered by this policy do not include all tortious acts. According to the policy definition, "Wrongful Acts" means [**6] "any actual or alleged error or misstatement or act or omission or neglect or breach of duty by the Directors and Officers in the discharge of their duties . . . or any other matter *not excluded by the terms and conditions of this policy* claimed against them solely by reason of their being officers and directors of the Company." Para. III.(c). of Policy, Ex 1 to Rolfe Affidavit (emphasis added). The policy excludes coverage for any payments "brought about or contributed to by the dishonesty of the Directors or Officers." The policy will cover, however, the costs of defending the directors and officers against alleged dishonesty "*unless a judgment or other final adjudication* thereof adverse to the directors and officers shall establish that acts of active and deliberate dishonesty committed by the Directors and Officers with actual dishonest purpose and intent were material to the cause of action so adjudicated." para. IV.(b)(5) of Policy, Ex. 1 to Rolfe Affidavit (emphasis added).

Continental contends that it is not liable for immediate payment to PepsiCo for the directors and officers legal fees because Paragraph VI of the Policy provides that "no costs, charges or expenses [**7] shall be incurred without Underwriters' consent." Continental argues that it could not pay the directors' and officers' legal fees until the conclusion of the litigation because there remained the possibility that a final adjudication would include a finding that the directors or officers had been materially dishonest. Paragraph VI includes a declaration that Continental will pay the amounts due except as limited by the exclusions listed in Paragraph V of the policy.

Although this language would have entitled Continental to reimbursement of payments for the defense costs of directors and officers adjudicated as dishonest, it does not excuse Continental from its obligation to pay the defense costs as they are incurred. First, under the policy, entry of final judgment is not a prerequisite to payment of defense costs. The policy definition of loss includes amounts incurred in the defense of all allegations of wrongdoing and dishonesty. Thus, the duty to pay defense costs essentially applies to all legal actions against the directors arising out of their status as such. Continental promised to pay "on behalf of" the directors and officers "all loss which [they] shall become legally [**8] obligated to pay." para. I(a) to Policy, Ex. 1 to Rolfe Affidavit. Thus, once the "loss" or attorneys fees were incurred by the directors and officers, C.N.A.'s responsibility to reimburse the directors and officers attached.

A similar directors and officers policy was also interpreted recently to require contemporaneous payments of defense costs. *Okada v. M.G.I.C.*, 608 F. Supp. 383 (D. Hawaii 1985). In that case, shareholders of a bankrupt savings and loan sued the directors and officers claiming that their negligence caused the collapse of the institution. As in this case, that policy did not impose a "duty to defend" upon the insurer although the definition of loss included "defense costs." The Court explained that,

> "the absence of policy language explicitly imposing a duty to defend does not [*660] mean that the policy does not require the insurer to pay defense costs. Like liability arising from a judgment or settlement, attorneys fees are compensable losses under [the policy definition]. The only difference is that such fees come due earlier than any possible adverse judgment." *Id.* at 385.

Second, a liability insurer has a duty to pay all defense [**9] costs until it can confine its duty to pay only on those claims it has insured the policy holders against. *Shapiro v. American Home Assurance Company*, 616 F. Supp. 906, 913 (D. Mass. 1985). Continental could excuse itself from the contemporaneous duty only if it could establish as a matter of law that there was no possible factual basis on which it might be obligated to indemnify the directors and officers. *Villa Charlotte Bronte, Inc. v. Commercial Union*, 64 N.Y.2d 846, 848, 487 N.Y.S.2d 314, 476 N.E.2d 640 (1985). Here Continental was obligated to pay incurred defense costs unless a final judgment found "material dishonesty" by the directors or officers. Continental has conceded that even if a final judgment had been entered such a conclusion was highly unlikely. Continental consequently had an obligation under the Policy to pay the directors' and officers' defense costs as they were incurred.

The Terms of the Policy and Public Policy

A class was certified against defendants only on the federal claim that they had violated Section 10(b) of the

Securities Exchange Act, 15 U.S.C. § 78j(b) and SEC Rule 10(b)-5. Liability under those provisions requires that plaintiffs [**10] prove intentional or reckless misconduct on the part of defendants. Continental claims as its seventh affirmative defense that a finding of liability on these claims would fall within the dishonesty exclusion of the Policy (para. IV.b.5), and it should therefore not be held responsible to insure the directors and officers on the claims. Continental also asserts that indemnification against such charges is contrary to "public policy."

Insofar as concerns defense costs, this argument adds nothing. Under the terms of the policy, Continental agreed to pay all costs for defending and settling claims for actual and *alleged* Wrongful Acts. The exclusion for "dishonesty" attaches only after a "final judgment or other final adjudication" implicates the directors. Such a finding is no longer possible in this case. The class action claims have been dismissed with prejudice and although the S.E.C. investigation resulted in charges against PepsiCo, none were asserted against any of its directors or officers. Continental cannot now put the directors and officers other than Ahern on trial to determine whether or not they were, in fact, dishonest to the point that the policy will not cover them.

[**11] The policy at issue here is critically different from the one at issue in *Stargatt v. Avenell*, 434 F. Supp. 234 (D. Del. 1977), cited by defendant. The insurance company in that case was permitted to contend that the directors' and officers' dishonesty barred reimbursement under the policy. That policy's dishonesty exclusion, however, was unconditional and did not predicate its applicability upon a "final judgment or other final adjudication." *Compare Id.* at 242-242, *with* para. IV.(b)(5) of Policy, Ex. 1 to Rolfe Affidavit.

Public policy also does not bar reimbursement of the defense and settlement costs. Continental agreed to reimburse PepsiCo for such payments whenever PepsiCo "may be required or permitted by law" to indemnify its directors and officers. Continental suggests that Delaware Corporation Law bars corporate indemnification of settlements involving alleged Rule 10-(b)(5) violations, and that even if it does permit indemnification for such claims, a genuine issue of material fact remains as to whether the PepsiCo directors' indemnification decision was procedurally flawed.

Continental refers to the Delaware Corporation Law, § 145, which provides when, [**12] and under what conditions, a corporation may indemnify its directors and officers. Section 145(a), for example, permits indemnification when a director or officer "acted in good faith and in a manner he reasonably [*661] believed to be in or not opposed to the best interests of the corporation." Section 145(d) establishes the appropriate manner for making the determination that the director or officer "has met the applicable standard of conduct." PepsiCo's failure to satisfy these procedures or even to make an evaluation of the directors and officers actions is made irrelevant by the fact that these provisions are not exclusive conditions for indemnification. The statute itself makes clear that these are simply "fall back" provisions which a Delaware corporation may or may not adopt. Section 145(f) of the Delaware Code states that "the indemnification provided by this section shall not be deemed exclusive of any other rights to which those seeking indemnification may be entitled under any by-law, agreement, vote of stockholders or disinterested directors or otherwise . . ." The Delaware Supreme Court has applied this section literally, holding that "the corporation can . . . grant [**13] indemnification rights beyond those provided by the statute." *Hibbert v. Hollywood Park, Inc.*, 457 A.2d 339, 344 (Del. 1983).

PepsiCo has adopted a by-law that broadens its ability to indemnify its directors and officers. The pertinent section provides that,

> "unless the Board of Directors shall determine otherwise, the Corporation shall indemnify, to the full extent permitted by law, any person made . . . a party to an action, suit or proceeding, whether civil, criminal, administrative or investigative by reason of the fact that he . . . is or was a director, officer or employee of the Corporation . . . against expenses (including attorney's fees), judgments, fines and amounts paid in settlement actually and reasonably incurred by him in connection with such action, suit or proceeding." PepsiCo By-Laws § 3.07. Ex. 9 to Rolfe Affidavit.

This By-Law makes indemnification of PepsiCo directors and officers the rule rather than the exception. PepsiCo has, therefore, supplanted the "backstop"

provisions included in Del. Corp. Law §§ 145 (a), (b). The procedures detailed in § 145 (d) apply only when a corporation indemnifies pursuant to those backstop provisions. The [**14] simple vote of the Board of Directors, according to the corporation's By-Laws, was a procedurally correct method of indemnifying the directors. Accordingly, no further discovery pursuant to Fed. R. Civ. P. 56(f) on this issue is necessary.

Allocation

PepsiCo argues that Continental should reimburse the corporation the full amount of the settlement costs (up to the policy limit) because the directors and officers insured by Continental remain jointly and severally liable for the entire amount. Continental contends that despite the unitary nature of the claims, the directors' and officers' risk of liability was minimal relative to the risk facing PepsiCo and Arthur Young. It contends that some allocation must be made among the defendants. Alternatively, Continental has amended its answer to include its demand that it be allowed to insist upon contribution from PepsiCo and Arthur Young as joint tortfeasors. According to Continental, it would be unfair that PepsiCo and Arthur Young, neither of which are insured by Continental, should "free ride" on the directors and officers insurance policy.

The policy clearly provides that it covers only the directors and officers of PepsiCo, [**15] not the corporation and not its accounting firm. *See* Policy paras. I.(a), I.(b), Ex. 1 to Rolfe Affidavit. The policy provides for payments to PepsiCo only for the amount it indemnifies the defendant directors and officers.

Our Court of Appeals, applying New York law, has permitted insurance companies the right to apportion payments on a lump sum settlement according to who was or was not insured. In *H.S. Equities, Inc. v. Hartford Accident and Indemnity Co.*, 661 F.2d 264 (2d Cir. 1981) the insurer, Hartford, had issued a blanket brokers bond which insured H.S. Equities for "any loss through any dishonest, fraudulent or criminal act of any of its Employees." Hartford had also agreed to indemnify the [*662] costs of defending against an insurable claim. Two H.S. Equities customers sued the company and one of its agents for violations of the Federal Securities Laws and for breaches of common law fiduciary duty. The two customers ultimately settled their claims against H.S. Equities and the agent for a lump sum settlement of $130,000. Hartford refused to pay the full settlement amount "on the ground that there was no evidence of [the agent's] dishonesty." *Id.* at 267. [**16] H.S. Equities sued to recover on the insurance policy. The District Court found that the settlement "conclusively established" the insurance company's liability under the Bond for the part of the settlement attributable to the claims covered by the insurance policy. The Court of Appeals reversed this aspect of the District Court's holding; it ruled that such a settlement constituted only "presumptive evidence" of the insurance company's liability. The case was accordingly remanded to the district court to make the appropriate finding. The Court of Appeals affirmed, however, the District Court's conclusion that one half of the settlement amount was attributable to alleged transgressions on the part of H.S. Equities, which was not insured by Hartford. *Id.* at 272.

PepsiCo contends that *H.S. Equities* differs from the instant case because the class action complaint in this case involved claims of joint and several liability against all the defendants. Paragraph VI of the Policy provides, however, that, "no costs, charges, or expenses shall be incurred, or settlements made, without Underwriters' consent, such consent not to be unreasonably withheld." C.N.A. has not yet approved [**17] the settlement. The parties agreed to a "non-waiver" agreement that provided that Continental would not object to the settlement at the time it was proposed but retained its right to object to the settlement if it later determined that it was not "reasonable".

Continental has now made clear that it finds the settlement is reasonable as a whole. (Tr. 16-17). It objects, however, that the amount is unreasonable if it is considered a measure of the directors' and officers' liability. Continental would have been within its rights to make this sort of objection under the Policy prior to the settlement; because of the non-waiver agreement it may raise these same objections now. Continental has not insured the Corporation or Arthur Young, both of which benefitted from the settlement. It is extremely unlikely that the directors and officers would have agreed to a settlement, the costs of which they would be expected to pay in toto. It is equally unlikely that Continental would have approved such a settlement. Allocation of responsibility according to the relative exposures of the respective parties to the class action litigation is therefore appropriate.

Although jointly and severally liable [**18] to the

plaintiffs, joint tortfeasors may demand contribution from each other, even in a securities fraud case. *See, e.g., Sirota v. Solitron*, 673 F.2d 566 (2d Cir.) *cert. denied*, 459 U.S. 838, 74 L. Ed. 2d 80, 103 S. Ct. 86 (1982). These allocations are often made, albeit only as approximations, according to some notion of relative fault. *See McLean v. Alexander*, 449 F. Supp. 1251 (D. Del. 1978). *rev'd on other grounds*, 599 F.2d 1190 (3d Cir. 1979). The allocation of risk in this case does not appear to present any special complexity or difficulty.

This court concludes, therefore, that the Policy requires the parties to allocate the settlement costs between those amounts attributable to the directors and officers and those attributable to PepsiCo and its accountants. Evidence of a good faith settlement of the underlying litigation, however, creates a presumption that the costs are covered by the policy. *See H.S. Equities*, 661 F.2d at 269. Continental must accordingly bear the ultimate burden of proving what amount of the settlement cost should be excluded from the policy coverage.

MOTIONS TO DISMISS

Anti Trust Claim

PepsiCo's antitrust claim, Count [**19] IX of its complaint, asserts that Continental [*663] has failed to deal with it in good faith with respect to this insurance policy. The complaint lists the following specific harms:

> "CNA has engaged in one or more of the following acts, among others:
>
> (a) it has unreasonably and unjustifiably denied coverage of PepsiCo's claims;
>
> (b) it has unreasonably and unjustifiably delayed in honoring PepsiCo's claims, thereby holding PepsiCo's money and earning interest on that money at rates higher than the legal rate;
>
> (c) it has unreasonably and unjustifiably asserted grounds for noncoverage that do not have any basis in fact or in law, that are contrary to public policy, and that constitute malicious, wanton, and wrongful denials made in gross disregard of PepsiCo's rights;
>
> (d) it has made false and misleading representations concerning the coverage afforded by its policies;
>
> (e) it has set the terms and conditions upon which it would deal with PepsiCo;
>
> (f) it has wrongfully threatened to attempt to rescind the CNA Policies should PepsiCo press its claim for coverage under them; and
>
> (g) it has wrongfully cancelled the 1984-1987 Policy, thereby [**20] refusing to deal with PepsiCo." para. 39, Complaint at 15.

PepsiCo contends that Continental's behavior is part of a conspiracy among Continental and other insurance companies, underwriters and their agents directed against PepsiCo and other policy holders. Complaint at para. 40. This conspiracy, according to the complaint, is a *per se* violation of the Antitrust laws and may have "the effect of enabling CNA (a) to monopolize or attempt or conspire to monopolize, (b) unreasonably restrain trade and competition in and (c) substantially lessen competition in the market for the purchase or sale of D&O liability insurance or in one of more lines of commerce within that market." Complaint, para. 42.

Continental has moved to dismiss this antitrust claim for failure to make sufficient allegations of anti-competitive effects. The list of wrongs alleged in para. 39 of the complaint are simply alleged business torts and do not amount to antitrust violations. An antitrust claim must allege some injury to competition, not simply to a competitor or customer. *Brunswick v. Pueblo Bowl-O-Mat*, 429 U.S. 477, 488, 50 L. Ed. 2d 701, 97 S. Ct. 690 (1977). Although PepsiCo has made some [**21] allegations of this sort, Continental describes those allegations as conclusory assertions.

A conspiracy not to honor contracts does not necessarily describe an anti-competitive arrangement. As the late Judge Friendly explained, "combining an assertion of general antitrust violation with a claim of injury from breach of contract or tort does not automatically make the latter a claim arising under the antitrust laws." *Salerno v. American League of*

Professional Baseball Clubs, 429 F.2d 1003, 1004 (2d Cir. 1970); *see also U.N.R. v. Continental Insurance Co.*, 607 F. Supp. 855, 861 (N.D. Ill. 1984).

The Supreme Court, however, has made clear that insurance companies may be called upon to answer complaints brought under the antitrust laws where those complaints allege "boycotts or other refusals to deal." Such boycotts are not limited to those that have competitors as targets. Rather, the term "boycott" in this context includes refusals to deal in cases where the target is a customer of some or all of the conspirators. *St. Paul Fire & Marine Insurance Co. v. Barry*, 438 U.S. 531, 542, 57 L. Ed. 2d 932, 98 S. Ct. 2923 (1977).

PepsiCo has alleged a concerted refusal to deal [**22] on the part of Continental and some or all of its competitors. Paragraph 40 of the Complaint, which makes a conspiracy allegation, incorporates by reference all of Paragraph 39 of the Complaint. As already quoted above, subsection (g) of that paragraph alleges a "refusal to deal." This claim therefore survives defendant's motion to dismiss. Whether it can be supported by credible evidence remains to be seen.

[*664] *Fraud Claims*

PepsiCo's complaint includes several claims of fraud and mispresentation in Counts VII, VIII and X. Rule 9(b), Fed. R. Civ. P. requires plaintiffs to state their allegations of fraud with particularity. Continental argues that PepsiCo has failed to provide it with adequate notice of the fraud claims as required by Rule 9(b).

PepsiCo's complaint as pleaded does not satisfy the Rule 9(b) requirements. The basic outline of PepsiCo's fraud claims is relatively straightforward and simple, viz. that Continental is attempting to disavow its insurance contract with PepsiCo and that it may never have intended to honor the agreement from the outset. As pleaded, the fraud allegations easily satisfy the basic Rule 8 requirements. Rule 9(b), however, imposes [**23] a higher standard on fraud pleadings. Courts have generally interpreted the particularity command as requiring a party to plead the circumstances surrounding the fraud, including the "time, place and contents of the false representation, as well as the identity of the person making the misrepresentation and what he obtained thereby." *Robertson v. National Basketball Association*, 67 F.R.D. 691, 697 (S.D.N.Y. 1975); *see also Todd v. Oppenheimer Co.*, 78 F.R.D. 415, 420-421 (S.D.N.Y. 1978).

PepsiCo did not need to include the name of the individual who wrote the fraudulent statements as long as it can allege that Continental adopted them. It has failed, however, to state when and where the statements appeared in any of the claims alleging fraud. The portions of Count X that allege fraud, subsections (a) and (f), do not identify what statements, documents, or policy provisions included knowing misrepresentations. Counts VII and VIII and Count X, subsections (a) and (f) are dismissed without prejudice. Plaintiff if so advised may replead and particularize its allegations within thirty (30) days.

New York State Insurance Law Claims

PepsiCo alleges in Count VI that Continental [**24] wrongfully cancelled the 1984-1987 policy and seeks declaratory relief and damages. Continental claims that, under the contract, it was entitled to terminate the policy at will. It also points out that N.Y. Ins. Law § 3425 has placed restrictions only on the cancellation of specific sorts of insurance policies, and does not include directors and officers policies among them. The parties have not cited nor has the Court found any New York cases that have extended non-cancellation protection to this sort of insurance policy. In light of the detail of the section, we may conclude *expressio unius est exclusio alterius* and find accordingly that PepsiCo does not have a wrongful termination remedy available to it under New York law.

Count VI, however, does not cite to the New York Insurance Law as the sole basis for its claim. This count may properly be read as alleging a violation by Continental of the implied covenant of good faith and fair dealing, which is implied in all contracts under New York law. *See Kirke La Shelle Co. v. Paul Armstrong Co.*, 263 N.Y. 79, 188 N.E. 163 (1933). Whether or not Continental has violated this implied covenant remains a disputed issue of fact on [**25] the present state of the record and so Count VI survives the motion to dismiss.

PepsiCo's complaint refers to other sections of the New York Insurance Law. Counts VIII, IX, and X make reference to N.Y. Ins. Law § 2403 and Counts VI, IX, and X include N.Y. Ins. Law § 2601. Section 2403 provides as follows:

> "No person shall engage in this state in
> any trade practice constituting a defined

violation or a determined violation defined herein [in specified sections of the Insurance Law]."

Section 2601(a) provides as follows:

"No insurer doing business in this state shall engage in unfair claim settlement practices. Any of the following acts by an insurer, if committed without just cause and performed with such frequency as to indicate a general business practice, shall constitute unfair claim settlement practices:

[*665] (1) knowingly misrepresenting to claimants pertinent facts or policy provisions relating to the coverage at issue;

(2) failing to acknowledge with reasonable promptness pertinent communications as to claims arising under its policies;

(3) failing to adopt and implement reasonable standards for the prompt investigation of [**26] claims arising under its policies;

(4) not attempting in good faith to effectuate prompt, fair and equitable settlements of claims submitted in which liability has become reasonably clear . . .; or

(5) compelling policyholders to institute suits to recover amounts due under its policies by offering substantially less than the amounts ultimately recovered in suits by them."

New York courts have not established a private right of action pursuant to these regulations. *See Cohen v. New York Property Insurance Underwriting Ass'n.*, 65 A.D.2d 71, 79, 410 N.Y.S.2d 597 (1978); *see also Royal Globe Insurance Co. v. Chock Full O'Nuts Corp.*, 86 A.D.2d 315, 316-317, 449 N.Y.S.2d 740 (1982). A private right of action would only be implied where a court can discern the legislative intent to create such a private remedy. *See Burns Jackson et al. v. Lindner*, 59 N.Y.2d 314, 464 N.Y.S.2d 712, 451 N.E.2d 459 (1983). These sections were promulgated to protect New York state insurance customers from generally deceptive business practices and are part of a single, cohesive administrative scheme that empowers the State Insurance Department to regulate the insurance industry. *See* [**27] *Frizzy Hairstylists, Inc. v. Eagle Star Insurance Co.*, 93 Misc.2d 59, 403 N.Y.S.2d 389, 390 (App. Term 2d Dep't. 1977). This Court is unable to discern any legislative intent to create a private right of action for policy holders pursuant to either of these provisions.

The fact that these provisions do not provide for private causes of action, however, is not fatal to any of PepsiCo's claims. Count VII (fraud) and Count IX (antitrust) are based on either common law or statutory causes of action. The inclusion of the Insurance Law provisions in these counts is proper as an expression of public policy and as evidence of Continental's duties to its insureds. Count X alleges general and systematic deceptive business practices and may be maintained as a claim for violation of the implied covenant of good faith and fair dealing for the same reasons as explained in connection with the discussion of Count VI above.

Continental has challenged Count XI as a kitchen sink count intended to support a claim for punitive damages. Whether or not this count is viewed in that light, it survives this motion to dismiss. New York courts permit an award of punitive damages when one of two conditions [**28] is present. First, when defendant's actions are directed at the public generally and second when the availability of such an award is essential to induce a potential plaintiff to go to court to right a wrong that might otherwise go unremedied if the injured party were limited to compensatory damages. *See Walker v. Sheldon*, 10 N.Y.2d 401, 405, 223 N.Y.S.2d 488, 179 N.E.2d 497 (1961); *see also Newburger, Loeb & Co., Inc. v. Gross*, 563 F.2d 1057, 1080 (2d Cir. 1977); *Texaco, Inc. v. Pennzoil Company*, 626 F. Supp. 250, 254 (S.D.N.Y. 1986). Viewed at this stage of the litigation, punitive damages should be regarded as unlikely but not impossible. Since plaintiff can only recover once, however many theories are pleaded, the complaint seems unduly complex and theoretical. When pre-trial proceedings are completed, the Court may make an order limiting the issues to be tried, as contemplated by Rule 16(c)(1) Fed. R. Civ. P.

PepsiCo's motions for partial summary judgment are

granted in part and denied in part. Continental's motions to dismiss are denied except that PepsiCo's fraud claims are dismissed without prejudice to amend its complaint if so advised within thirty (30) days.

[**29] The parties shall confer and establish a schedule to complete pre-trial proceedings [*666] and shall go forward with any necessary discovery. They shall attend a status conference at the United States Courthouse, 101 East Post Road, White Plains, New York on September 29, 1986 at 9:00 a.m.

So Ordered.

MEMORANDUM & ORDER

Brieant, J.

Continental Casualty Company ("Continental") has asked this Court to clarify and reconsider portions of its Partial Summary Judgment decision, dated June 23, 1986 (the "Decision"). Familiarity with the Decision and the circumstances surrounding this litigation must be assumed. In that Decision this Court determined, *inter alia*, that the insurance policy issued to PepsiCo established a duty on Continental's part to pay the directors' and officers' defense costs as they were incurred. This Court also determined that, with respect to the allocation of the settlement cost, Continental bore the ultimate burden of proof on that issue. Continental seeks to clarify whether defense costs, like the settlement costs must be allocated and asks reconsideration of the burden of proof assignment.

Defense Costs

PepsiCo moved in this Court for an [**30] interpretation of its insurance policy as it applied to the Class Action Securities Litigation defense costs. Accordingly, this court's decision interpreting that aspect of the policy resolved the issue concerning that litigation and did not necessarily resolve the issue concerning those defense costs incurred in behalf of the officers and directors in the SEC and the Grand Jury investigations. At least on the record presently before this Court, because the litigation and the investigations were each directed at the same allegedly fraudulent activity, and were directed against both PepsiCo and its directors and officers, it would seem that these defense costs, like the costs of defending the class action, are properly the subject of indemnification, and therefore a covered loss within the policy.

Implicit, and we think obvious, in the portion of the Court's opinion addressing the defense costs issue is our conclusion that Continental has no contemporaneous duty to pay *all* defense costs incurred by Pepsico, where a portion of those costs is attributable not to the officers and directors, but to the defense of PepsiCo itself. Only defense costs incurred on behalf of the directors [**31] and officers are within the "Loss" definition of the policy.

Burden of Proof

On reconsideration the Court adheres to its conclusion that, "Continental must . . . bear the ultimate burden of proving what amount of the settlement cost should be excluded from the policy coverage." Decision at 662. PepsiCo paid the settlement fund and received releases in favor of itself and its directors and officers as well as its accounting firm. The policy language, Section III.(d), defines "Loss" as

> "any amount which the Directors and Officers are legally obligated to pay for which they are not indemnified by the Company, or for which the Company may be required or permitted by law to pay as indemnity to the Directors and Officers, for a claim or claims made against them for Wrongful Acts, and shall include . . . settlements."

In order to avoid total liability Continental must show the amount that the uninsured defendants are equitably required to share. The lesson of *H.S. Equities v. Hartford Accident and Indemnity Co.*, 661 F.2d 264 (2d Cir. 1981) is that once an insured has presented a claim under the policy based on a good faith settlement, the insurer bears the [**32] burden of proving that all or a portion of the total paid in settlement is excluded from the policy coverage.

The foregoing constitutes this Court's clarification of its Memorandum and Order dated June 23, 1986. In all other respects Continental's motion is denied.

So Ordered.

TAB 6

INTERNATIONAL INSURANCE COMPANY, an Illinois Corporation, Plaintiff, -v- NEWMONT MINING CORPORATION, et al., a Delaware Corporation, et al., Defendant.

88 Civ. 7500 (RO)

UNITED STATES DISTRICT COURT FOR THE SOUTHERN DISTRICT OF NEW YORK

800 F. Supp. 1195; 1992 U.S. Dist. LEXIS 14134

September 17, 1992, Decided
September 21, 1992, Filed

CORE TERMS: insured's, common interest, insurer, attorney-client, coverage, carrier, mining

COUNSEL: [**1] Attorneys for Plaintiff: Mound, Cotton & Wollan, One Battery Park Plaza, New York, NY 10004, John Mezzacappa, Esq., Of Counsel. Orrick, Herrington & Sutcliffe, 599 Lexington Avenue, New York, NY 10022, Nancy I. Ruskin, Esq., Of Counsel.

Attorneys for Defendant, Newmont Mining Corp.: Tofel Berelson & Saxl, P.C., 823 United Nations Plaza, New York, NY 10017, Mark A. Lopeman, Esq., Of Counsel.

JUDGES: Owen

OPINION BY: RICHARD OWEN

OPINION

[*1196] MEMORANDUM

OWEN, District Judge

In this action for a declaratory judgment brought by International Insurance Company against its insured, Newmont Mining Corporation to declare certain environmental-impairment liability policies void or not affording coverage, the carrier seeks certain discovery from the company which opposes it on the ground of attorney-client privilege.

It appears that the company itself defended two separate environmental actions brought against it by the State of Colorado and the EPA after International declined coverage and failed to provide a defense. International, in this action now seeks materials from the company in those two actions which would normally be within the attorney-client privilege asserting, however, the "common interest" exception to the [**2] rule.

Relying principally on *Waste Management, Inc., v. International Surplus Lines Ins. Co.*, 144 Ill. 2d 178, 579 N.E. 2d 322, 161 Ill. Dec. 774 (Ill. 1991), the Magistrate Judge below applied the exception and ordered the materials turned over. This appeal followed.

I conclude that while the insurer had the same "desire" as its insured to have a successful defense of the said actions, for if coverage was later determined to exist, it would be responsible for any obligation of its insured remaining, this in my view is an insufficient "common interest" to warrant invasion of the attorney-client relationship with the privilege attaching to confidential communications which the law rather zealously protects. 1

1 Indeed, where a carrier declines to defend, a climate of actual antagonism between the insured and the carrier is more likely.

The "common interest," logically viewed, and New York law supports, which makes the privilege inapplicable, is where an attorney actually represents both the insured and the insurer -- joint representation -- and accordingly both clients are working together with a single attorney toward a common goal. See, e.g. *Goldberg v. American Home Assurance Co.*, 80 A.D.2d 409, 439 N.Y.S.2d 2 [**3] (App. Div., 1st Dept. 1981). That is not the situation before me. [2] Consequently, [*1197] whatever validity *Waste Management,* supra, has in any other situation, I conclude it has no force here.

2 The fact that the insurer had a separate contract with several others of the mining company's insurers under which it paid some part of the company's lawyers' fees in one of the two underlying actions does not, in my view, give it either factually or legally, the "common interest" with the company which would justify a court in removing the law's protection accorded confidences between that company as client and its attorneys. *Emons Industries Inc. v. Liberty Mutual Ins. Co.,* 747 F. Supp. 1079, 1082-3.

Accordingly, paragraph 2 of the order of the Magistrate Judge dated December 17, 1991 is reversed on the law and International's motion is denied, the insured's assertion of the attorney-client privilege to the materials discussed therein being sustained.

Date: September 17, 1992

New York, N.Y.

Richard Owen

United States District Judge

TAB 7

[*1] Vigilant Insurance Company et al., Appellants, v The Bear Stearns Companies, Inc., Respondent.

No. 25

COURT OF APPEALS OF NEW YORK

2008 NY Slip Op 2080; 10 N.Y.3d 170; 884 N.E.2d 1044; 855 N.Y.S.2d 45; 2008 N.Y. LEXIS 542

February 6, 2008, Argued
March 13, 2008, Decided

PRIOR HISTORY: Appeal, by permission of the Appellate Division of the Supreme Court in the First Judicial Department, from an order of that Court, entered November 14, 2006. The Appellate Division modified, on the law, an order of the Supreme Court, New York County (Karla Moskowitz, J.; op 10 Misc 3d 1072[A], 814 NYS2d 566, 2006 NY Slip Op 50047[U]), which had granted plaintiffs' motion for summary judgment to the extent of declaring that defendant could not recover the $ 25 million disgorgement payment through its insurance policies with plaintiffs, and otherwise denied the motion. The modification consisted of granting summary judgment to defendant on the investment banking exclusion and the independent research/investor education issue, and denying summary judgment to plaintiffs regarding disgorgement. The following question was certified by the Appellate Division: "Was the order of the Supreme Court, as modified by this Court, properly made?"
Vigilant Ins. Co. v Bear Stearns Cos., Inc., 34 AD3d 300, 824 NYS2d 91, 2006 N.Y. App. Div. LEXIS 13428 (N.Y. App. Div. 1st Dep't, 2006), reversed.

DISPOSITION: Order reversed, with costs, plaintiffs' motion for summary judgment granted, judgment granted declaring in accordance with the opinion herein and certified question answered in the negative.

CORE TERMS: insurer, settlement, final judgment, investment banking, disgorgement, breached, coverage, policy provision, investor, regulator, settling, issues of fact, obligating, summary judgment, insured, settle, triable, agreed to pay, insurance policy, settlement-in-principle, signature, lawsuit, carriers, notice, settlement agreement, citation omitted, insurance contracts, ill-gotten, executing, modified

HEADNOTES

Insurance -- Disclaimer of Coverage -- Failure to Obtain Insurers' Consent before Settling

Defendant insured, having executed a consent agreement in settlement of the underlying federal lawsuit against it providing for the payment of $ 80 million and certain other relief three days before it notified plaintiff liability carriers and asked for their consent to the settlement, breached a provision in its liability policies with plaintiffs obligating it to obtain plaintiffs' consent before settling claims in excess of $ 5 million. The policy provision provided that defendant would not "settle any Claim, incur any Defense Costs or otherwise assume any contractual obligation or admit any liability with respect to any Claim in excess of" $ 5 million without plaintiffs' consent. Upon signing the consent agreement defendant acquiesced to the relief sought in the federal action and agreed that a final judgment could be presented to the federal court for signature and entry without further

notice to defendant. Although the federal court did not approve the settlement until it entered a final judgment almost six months after plaintiffs had been notified of the settlement, defendant was not free to walk away from the consent judgment before entry of a final judgment, and it had settled the claim within the meaning of the insurance policy at the time it signed the consent agreement.

COUNSEL: *DLA Piper US LLP*, New York City (*Joseph G. Finnerty III, Arthur F. Fergenson* and *Howard S. Schrader* of counsel), and *Bondas, Skarzynski, Walsh & Black, LLC* (*James A. Skarzynski, Evan Shapiro* and *Eleftherios Stefas* of counsel) for appellants. I. The First Department violated the Supremacy Clause of the United States Constitution by nullifying a federal court final judgment. (*Frew v Hawkins,* 540 US 431, 124 S Ct 899, 157 L Ed 2d 855; *Hunt v Mobil Oil Corp.,* 557 F Supp 368; *Washington v Washington State Commercial Passenger Fishing Vessel Assn.,* 443 US 658, 99 S Ct 3055, 61 L Ed 2d 823; *Delaware Val. Citizens' Council for Clean Air v Commonwealth of Pa.,* 755 F2d 38; *Central Nat. Bank v Stevens,* 169 US 432, 18 S Ct 403, 42 L Ed 807; *Riggs v Johnson County,* 73 U.S. 166, 6 Wall [73 US] 166, 18 L Ed 768; *Stoll v Gottlieb,* 305 US 165, 59 S Ct 134, 83 L Ed 104; *Deposit Bank v Frankfort,* 191 US 499, 24 S Ct 154, 48 L Ed 276; *Matter of New York State Commr. of Correction v Gulotta,* 194 AD2d 540, 598 NYS2d 547; *Jamaica Hosp. v Blum,* 68 AD2d 1, 416 NYS2d 294.) II. The First Department misapplied basic principles of contract interpretation to the insurance policies' "investment banking" exclusion. (*Mount Vernon Fire Ins. Co. v Creative Hous.,* 88 NY2d 347, 668 NE2d 404, 645 NYS2d 433; *Silva v Utica First Ins. Co.,* 303 AD2d 487, 755 NYS2d 433; *Matter of Manhattan Pizza Hut v New York State Human Rights Appeal Bd.,* 51 NY2d 506, 415 NE2d 950, 434 NYS2d 961; *People v Shapiro,* 50 NY2d 747, 409 NE2d 897, 431 NYS2d 422; *Bailey v AGR Realty Co.,* 260 AD2d 322, 689 NYS2d 65; *State of New York v Home Indem. Co.,* 66 NY2d 669, 486 NE2d 827, 495 NYS2d 969; *Newin Corp. v Hartford Acc. & Indem. Co.,* 62 NY2d 916, 467 NE2d 887, 479 NYS2d 3; *Hartford Acc. & Indem. Co. v Wesolowski,* 33 NY2d 169, 305 NE2d 907, 350 NYS2d 895; *Matter of Ideal Mut. Ins. Co. [Superintendent of Ins. of State of N.Y.--Harbour Assur. Co. of Bermuda],* 231 AD2d 59, 659 NYS2d 273; *Tierra Props. v Lloyd's Ins. Co.,* 206 AD2d 288, 614 NYS2d 518.) III. The court below erred in not holding that Bear Stearns' failure to obtain the insurers' consent prior to its settlement with the regulators voided coverage under the policies. (*Argo Corp. v Greater N.Y. Mut. Ins. Co.,* 4 NY3d 332, 827 NE2d 762, 794 NYS2d 704; *Royal Zenith Corp. v New York Mar. Mgrs.,* 192 AD2d 390, 596 NYS2d 65; *AIU Ins. Co. v Valley Forge Ins. Co.,* 303 AD2d 325, 758 NYS2d 16; *Travelers Indem. Co. v Eitapence,* 924 F2d 48; *Valentino v State of New York,* 48 AD2d 15, 367 NYS2d 593; *Silverman v Member Brokerage Servs.,* 298 AD2d 381, 751 NYS2d 245; *Winston v Mediafare Entertainment Corp.,* 777 F2d 78; *Flores v Lower E. Side Serv. Ctr., Inc.,* 4 NY3d 363, 828 NE2d 593, 795 NYS2d 491; *Brown Bros. Elec. Contrs. v Beam Constr. Corp.,* 41 NY2d 397, 361 NE2d 999, 393 NYS2d 350; *Matter of Express Indus. & Term. Corp. v New York State Dept. of Transp.,* 93 NY2d 584, 715 NE2d 1050, 693 NYS2d 857.) IV. The trial court and the First Department erred in not ruling that Bear Stearns' future payments for "independent research" and "investor education" programs are not "loss" covered by the policies. (*Loblaw, Inc. v Employers' Liab. Assur. Corp.,* 57 NY2d 872, 442 NE2d 438, 456 NYS2d 40; *Breed v Insurance Co. of N. Am.,* 46 NY2d 351, 385 NE2d 1280, 413 NYS2d 352; *Roundabout Theatre Co. v Continental Cas. Co.,* 302 AD2d 1, 751 NYS2d 4; *Continental Ins. Cos. v Northeastern Pharm. & Chem. Co., Inc.,* 842 F2d 977; *Mazzola v County of Suffolk,* 143 AD2d 734, 533 NYS2d 297; *2619 Realty v Fidelity & Guar. Ins. Co.,* 303 AD2d 299, 756 NYS2d 564; *Avondale Indus., Inc. v Travelers Indem. Co.,* 887 F2d 1200; *Ellett Bros., Inc. v United States Fid. & Guar. Co.,* 275 F3d 384; *Maryland Cas. Co. v Armco, Inc.,* 822 F2d 1348.)

Proskauer Rose LLP, New York City (*John H. Gross, Seth B. Schafler, Francis D. Landrey, Matthew J. Morris* and *Sarah Reisman* of counsel), for respondent. I. The insurers' Supremacy Clause argument was not preserved and is without merit. (*Bingham v New York City Tr. Auth.,* 99 NY2d 355, 786 NE2d 28, 756 NYS2d 129; *Motor Veh. Mfrs. Assn. of U.S. v State of New York,* 75 NY2d 175, 550 NE2d 919, 551 NYS2d 470; *Lichtman v Grossbard,* 73 NY2d 792, 533 NE2d 1048, 537 NYS2d 19; *Matter of Barbara C.,* 64 NY2d 866, 476 NE2d 994, 487 NYS2d 549; *Balbuena v IDR Realty LLC,* 6 NY3d 338, 845 NE2d 1246, 812 NYS2d 416; *Capitol Records, Inc. v Naxos of Am., Inc.,* 4 NY3d 540, 830 NE2d 250, 797 NYS2d 352; *Department of Treasury v Fabe,* 508 US 491, 113 S Ct 2202, 124 L Ed 2d 449; *SEC v National Securities, Inc.,* 393 US 453, 89 S Ct 564, 21 L Ed 2d 668; *Munich Am. Reins. Co. v Crawford,* 141 F3d 585; *Washington v Washington State Commercial Passenger Fishing Vessel Assn.,* 443 US 658, 99 S Ct

3055, 61 L Ed 2d 823.) II. There are triable issues of fact as to whether the payment labeled as disgorgement is a loss as that term is defined in the policy. (*Zuckerman v City of New York,* 49 NY2d 557, 404 NE2d 718, 427 NYS2d 595; *Winegrad v New York Univ. Med. Ctr.*, 64 NY2d 851, 476 NE2d 642, 487 NYS2d 316; *Lipsky v Commonwealth United Corp.*, 551 F2d 887; *Cambridge Fund, Inc. v Abella,* 501 F Supp 598; *Singleton Mgt. v Compere,* 243 AD2d 213, 673 NYS2d 381; *Matter of Halyalkar v Board of Regents of State of N.Y.*, 72 NY2d 261, 527 NE2d 1222, 532 NYS2d 85; *Matter of Becker v DeBuono,* 239 AD2d 664, 657 NYS2d 471; *Allstate Ins. Co. v Zuk,* 78 NY2d 41, 574 NE2d 1035, 571 NYS2d 429; *Public Serv. Mut. Ins. Co. v Goldfarb,* 53 NY2d 392, 425 NE2d 810, 442 NYS2d 422; *Messersmith v American Fid. Co.*, 232 NY 161, 133 N.E. 432.) III. The Appellate Division correctly granted summary judgment to Bear Stearns on the investment banking issue. (*Belt Painting Corp. v TIG Ins. Co.*, 100 NY2d 377, 795 NE2d 15, 763 NYS2d 790; *RJC Realty Holding Corp. v Republic Franklin Ins. Co.*, 2 NY3d 158, 808 NE2d 1263, 777 NYS2d 4; *242-44 E. 77th St., LLC v Greater N.Y. Mut. Ins. Co.*, 31 AD3d 100, 815 NYS2d 507; *Uribe v Merchants Bank of N.Y.*, 91 NY2d 336, 693 NE2d 740, 670 NYS2d 393; *Metropolitan Life Ins. Co. v Noble Lowndes Intl.*, 84 NY2d 430, 643 NE2d 504, 618 NYS2d 882; *State of New York v Home Indem. Co.*, 66 NY2d 669, 486 NE2d 827, 495 NYS2d 969; *Newin Corp. v Hartford Acc. & Indem. Co.*, 62 NY2d 916, 467 NE2d 887, 479 NYS2d 3; *Hartford Acc. & Indem. Co. v Wesolowski,* 33 NY2d 169, 305 NE2d 907, 350 NYS2d 895; *Ender v National Fire Ins. Co. of Hartford,* 169 AD2d 420, 563 NYS2d 85; *Mount Vernon Fire Ins. Co. v Creative Hous.*, 88 NY2d 347, 668 NE2d 404, 645 NYS2d 433.) IV. The Appellate Division correctly granted summary judgment to Bear Stearns on whether the policy covers payments for investor education and independent research. (*Vermont Teddy Bear Co. v 538 Madison Realty Co.*, 1 NY3d 470, 807 NE2d 876, 775 NYS2d 765; *Westview Assoc. v Guaranty Natl. Ins. Co.*, 95 NY2d 334, 740 NE2d 220, 717 NYS2d 75; *Mazzuoccolo v Cinelli,* 245 AD2d 245, 666 NYS2d 621; *S.E.C. v Lorin,* 869 F Supp 1117; *ZKZ Assoc. v CNA Ins. Co.*, 89 NY2d 990, 679 NE2d 629, 657 NYS2d 390; *Woodson v American Tr. Ins. Co.*, 281 AD2d 282, 722 NYS2d 138; *Yoi-Lee Realty Corp. v 177th St. Realty Assoc.*, 208 AD2d 185, 626 NYS2d 61; *Maryland Cas. Co. v Armco, Inc.*, 822 F2d 1348; *Ellett Bros., Inc. v United States Fid. & Guar. Co.*, 275 F3d 384; *Gerrish Corp. v Universal Underwriters Ins. Co.*, 947 F2d 1023.) V. There are triable issues of fact concerning the settlement issue. (*Isadore Rosen & Sons v Security Mut. Ins. Co. of N.Y.*, 31 NY2d 342, 291 NE2d 380, 339 NYS2d 97; *Prudential Lines v Firemen's Ins. Co. of Newark, N.J.*, 91 AD2d 1, 457 NYS2d 272; *Texaco A/S [Denmark] v Commercial Ins. Co. of Newark, N.J.*, 160 F3d 124; *Luria Bros. & Co., Inc. v Alliance Assur. Co., Ltd.*, 780 F2d 1082; *Silverman v Member Brokerage Servs.*, 298 AD2d 381, 751 NYS2d 245; *Hover v National Grange Ins. Co.*, 20 AD2d 178, 245 NYS2d 515; *Winston v Mediafare Entertainment Corp.*, 777 F2d 78; *Joseph Martin, Jr., Delicatessen v Schumacher,* 52 NY2d 105, 417 NE2d 541, 436 NYS2d 247; *Schlegel Mfg. Co. v Cooper's Glue Factory,* 231 NY 459, 132 N.E. 148; *Souveran Fabrics Corp. v Virginia Fibre Corp.*, 37 AD2d 925, 325 NYS2d 973.)

Jacob H. Stillman, Washington, D.C., and *Mark Pennington* for Securities and Exchange Commission, amicus curiae. I. The U.S. Securities and Exchange Commission's complaint alleged that Bear Stearns failed to guard against conflicts of interest that threatened the independence of its securities analysts and sought disgorgement of the ill-gotten gains arising from this misconduct. II. Bear Stearns agreed to pay disgorgement, and the District Court entered a judgment ordering it to do so. III. Despite the plain language of the complaint of the consent to judgment and of the final judgment, Bear Stearns urged in the Appellate Division that it did not pay disgorgement, and that the US Securities and Exchange Commission used a "legal fiction" to obtain compensatory damages.

JUDGES: Opinion by Judge Graffeo. Judges Ciparick, Read, Smith, Pigott and Jones concur. Chief Judge Kaye took no part.

OPINION BY: Graffeo

OPINION

[***1045] [**174] Graffeo, J.

In this insurance dispute, we conclude that the insured breached a policy provision obligating it to obtain the consent of its liability carriers before settling claims in excess of $ 5 million. We therefore reverse the order of the Appellate Division denying the insurers' motion for summary judgment.

Defendant Bear Stearns Companies, Inc., a financial

services firm, was issued a [*2] primary professional liability insurance policy by plaintiff Vigilant Insurance Company that provided coverage for losses resulting from claims made against the insured for its wrongful acts. The Vigilant policy afforded $ 10 million in coverage after Bear Stearns exhausted its $ 10 million self-insured retention. Plaintiffs Federal Insurance Company and Gulf Insurance Company further provided Bear Stearns an additional $ 40 million in coverage under follow-form excess liability policies. * Pursuant to the terms of these insurance contracts, Bear Stearns agreed not to settle any claim in excess of $ 5 million without first obtaining the consent of its insurers. In addition, the policies excluded coverage for claims arising from investment banking work undertaken by Bear Stearns.

> * The Travelers Indemnity Company is the successor-in-interest by merger to Gulf Insurance Company. Bear Stearns was also covered by additional excess policies not relevant to this appeal.

In early 2002, the U.S. Securities and Exchange Commission (SEC), National Association of Securities Dealers (NASD) and New York Stock Exchange (NYSE), along with state attorneys general, initiated a joint investigation into the practices of research analysts working at financial services firms and the potential conflicts that could arise from the relationship between research functions and investment banking objectives. The investigation focused on allegations that research analysts employed at 10 major financial institutions, including Bear Stearns, were improperly influenced by investment banking concerns. Toward the end of 2002, the regulators met separately [**175] with each of the investigated firms to discuss a global settlement.

[***1046] On December 20, 2002, Bear Stearns signed a settlement-in-principle document, acknowledging that each regulator would commence an action or administrative proceeding against it and that Bear Stearns would subsequently "consent to the action and the relief sought without admitting or denying the allegations." Bear Stearns further agreed to pay $ 50 million in retrospective relief, plus $ 25 million to fund independent research and $ 5 million for investor education. The document indicated that the terms of the settlement were subject to approval by the SEC and other regulators. Also taking place on December 20, 2002, the regulators issued a press release announcing they had achieved an industry-wide settlement with the 10 financial institutions that would result in payments of more than $ 1.4 billion in penalties, restitution and education funds.

A few months later, Bear Stearns executed a consent agreement in which it acceded to the entry of a final judgment in the SEC's federal lawsuit against Bear Stearns in the United States District Court for the Southern District of New York. Under the terms of the [*3] "Consent of Defendant Bear, Stearns & Co. Inc.," dated April 21, 2003, Bear Stearns consented to be permanently enjoined from violating a number of NASD and NYSE rules and agreed to pay a total amount of $ 80 million allocated as follows: $ 25 million as a penalty, $ 25 million in disgorgement, $ 25 million for independent research and $ 5 million for investor education. Of the $ 50 million in retrospective relief, $ 25 million was designated to resolve the SEC action and related proceedings instituted by the NASD and NYSE, while the remaining $ 25 million covered the settlement of proceedings with various state regulators. Bear Stearns explicitly agreed not to seek insurance coverage for the $ 25 million penalty. The agreement also allowed the SEC to present a final judgment to the federal court "for signature and entry without further notice" to Bear Stearns.

Three days after executing the settlement agreement, Bear Stearns sent letters to its insurers requesting their consent to the settlement. The insurers disclaimed coverage and commenced this declaratory judgment action seeking a declaration that the $ 45 million sought by Bear Stearns (after depletion of the $ 10 million self-insured retention) was not covered by the policies.

[**176] In October 2003 the federal District Court found the Bear Stearns settlement to be "fair, adequate, and in the public interest," and entered a final judgment ordering Bear Stearns to pay the agreed-upon sum of $ 80 million. Shortly thereafter, the insurers moved for summary judgment in this declaratory judgment action. In support of their motion, the insurers argued that they were not liable for all or part of the $ 45 million sought by Bear Stearns for four reasons. First, they asserted that Bear Stearns could not recover any of the settlement because it had breached the policy provision obligating it to obtain the insurers' consent before settling the case. Second, they claimed that the investment banking exclusion precluded recovery of the settlement proceeds.

Third, the insurers contended that the $ 25 million disgorgement payment was uncollectible either as a matter of public policy or under contract interpretive principles. Finally, they posited that neither the $ 25 million payment for independent research nor the $ 5 million payment for investor education was covered because those liabilities were not "losses" within the meaning of the policies.

Supreme Court found that triable issues of fact existed as to whether Bear Stearns breached the policy clause prohibiting it from settling without the insurers' consent [***1047] and whether the investment banking exclusion applied. Siding with the insurers on the disgorgement issue, the court held that the $ 25 million disgorgement payment did not constitute damages under the terms of the policies and that Bear Stearns was not entitled to look behind the settlement to ascertain whether the entire $ 25 million truly represented ill-gotten gains. The court also rejected the insurers' position that the $ 25 million payment for independent research and $ 5 million payment for investor education were not losses under the policies. Bear Stearns and the insurers [*4] appealed.

The Appellate Division modified, by granting Bear Stearns summary judgment on the investment banking exclusion and independent research/investor education issues and denying the insurers summary judgment on the disgorgement issue, and otherwise affirmed. The court concurred with Supreme Court in finding an issue of fact as to whether Bear Stearns breached the provision obligating it to obtain the consent of the insurers, but determined that the investment banking exclusion was not applicable. Despite the agreement by Bear Stearns to pay $ 25 million as disgorgement, the court found "an issue of fact as to [**177] whether the portion of the settlement attributed to disgorgement actually represented ill-gotten gains or improperly acquired funds" (34 AD3d 300, 302, 824 NYS2d 91 [2006]). Finally, the court rejected the insurers' contention that the combined $ 30 million payment for independent research and investor education were not covered losses.

The Appellate Division granted the insurers leave to appeal and certified the following question to this Court: "Was the order of the Supreme Court, as modified by this Court, properly made?" We conclude that it was not.

The insurers raise a number of objections to the Appellate Division order, but we find it necessary to address only one of them. The insurers contend that the Bear Stearns settlement is not recoverable because Bear Stearns breached the policy provision obligating it to obtain their consent prior to settling the regulator lawsuits. Specifically, the insurers claim that Bear Stearns resolved and finalized the settlement of the case when it executed the settlement-in-principle in December 2002 or, at the latest, when it signed the consent agreement in April 2003 without advising the insurers. Bear Stearns counters that the courts below properly found a triable issue of fact as to whether its execution of these two documents constituted a breach of the policy provision.

The primary insurance policy, whose terms and conditions are incorporated into the follow-form excess policies, provides in relevant part:

> "The Insured agrees not to settle any Claim, incur any Defense Costs or otherwise assume any contractual obligation or admit any liability with respect to any Claim in excess of a settlement authority threshold of $ 5,000,000 without the Insurer's consent, which shall not be unreasonably withheld ... The insurer shall not be liable for any settlement, Defense Costs, assumed obligation or admission to which it has not consented."

As with the construction of contracts generally, "unambiguous provisions of an insurance contract must be given their plain and ordinary meaning, and the interpretation of such provisions [*5] is a question of law for the court" (*White v Continental Cas. Co.*, 9 NY3d 264, 267, 878 NE2d 1019, 848 NYS2d 603 [2007] [citation omitted]).

We conclude that Bear Stearns breached this provision when it executed the April 2003 consent agreement before [***1048] notifying [**178] the insurers or obtaining their approval. As contemplated by the earlier settlement-in-principle, Bear Stearns signed the April 2003 agreement acquiescing to the relief sought in the SEC federal action. Under this agreement, Bear Stearns agreed to pay $ 80 million, covering four payment categories, in order to resolve the various federal and state regulatory actions and proceedings pending against it. Bear Stearns further accepted

injunctive relief that prevented it from violating certain NASD and NYSE rules. And it acknowledged that the SEC could present a final judgment to the federal court for signature and entry without further notice. In short, Bear Stearns did everything within its ability to settle the matter and no further action was required on its part.

We are unpersuaded by the contention that a triable issue of fact exists because the federal court did not approve the settlement until it entered a final judgment in October 2003. Parties are free to enter into a valid settlement agreement that is made subject to court approval. Notably absent from the agreement, however, was any provision similarly subjecting it to the insurers' approval. Having signed the consent agreement, Bear Stearns was not free to walk away from it before entry of a final judgment (*see TLC Beatrice Intl. Holdings, Inc. v Cigna Ins. Co.*, 2000 WL 282967, *7, 2000 US Dist LEXIS 2917, *20-21 [SD NY 2000] ["Although the Court, whose approval was sought by the parties, could accept or reject the Settlement, subject to that approval the parties themselves were bound by the Settlement's terms" (citation omitted)], *affd sub nom. Lewis v Cigna Ins. Co.*, 234 F3d 1262 [2d Cir 2000] [table; text at 2000 WL 1654530, 2000 US App LEXIS 27848 (2000)]). In executing the April 2003 agreement, Bear Stearns settled a claim within the meaning of the insurance policy provision.

As a sophisticated business entity, Bear Stearns expressly agreed that the insurers would "not be liable" for any settlement in excess of $ 5 million entered into without their consent. Aware of this contingency in the policies, Bear Stearns nevertheless elected to finalize all outstanding settlement issues and executed a consent agreement before informing its carriers of the terms of the settlement. Bear Stearns therefore may not recover the settlement proceeds from the insurers.

Accordingly, the order of the Appellate Division should be reversed, with costs, plaintiffs' motion for summary judgment [**179] granted, judgment granted declaring in accordance with this opinion and the certified question answered in the negative.

[*6] Judges Ciparick, Read, Smith, Pigott and Jones concur; Chief Judge Kaye taking no part.

Order reversed, etc.