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OCTOBER 20, 2009

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DELAWARE CHANCERY COURT INTERPRETS NEW YORK LAW TO APPLY "ALL SUMS" METHOD OF ALLOCATION IN ASBESTOS BODILY INJURY COVERAGE ACTION

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On October 14th, a Delaware Court of Chancery judge issued an 88-page opinion granting summary judgment to two insureds, Warren Pumps LLC ("New Warren") and Viking Pump, Inc. ("New Viking"), on critical issues of allocation and a corporate successorship. *Viking Pump, Inc. v. Century Indem. Co.,* C.A. No. 1465 (VCS) (Del. Ch. October 14, 2009). Vice Chancellor Leo E. Strine, Jr. held that New Viking and New Warren could avail themselves of their predecessor's excess insurance program for asbestos exposure claims emanating from the predecessor's period of ownership. And in a surprising departure from well-established New York law, the Court further held that coverage should be allocated on an "all sums" basis, contradicting the numerous New York cases adopting pro-rata allocation.

In 1985, New Warren and New Viking acquired pump manufacturing businesses from Houdaille Industries, Inc. ("Houdaille") and, as a result, both entities face numerous asbestos bodily injury claims arising from asbestos exposures during Houdaille's ownership. New Warren and New Viking seek to use Houdaille's insurance coverage, that includes forty-five excess insurance policies provided by twenty different insurers. In the first phase of the consolidated declaratory judgment actions, the court ruled that New Warren was entitled to Houdaille's primary and umbrella insurance from Liberty Mutual. *Viking Pump, Inc. v. Liberty Mutual Insurance Company and Warren Pumps LLC,* 2007 WL 2752912 (Del. Ch. Apr. 2, 2007) (unpublished opinion). Liberty Mutual reached a global resolution of its dispute with New Warren and New Viking, and the case proceeded to the next phase, involving rights to Houdaille's excess insurance.

On cross-motions for summary judgment, the excess insurers argued that Houdaille never agreed to transfer its insurance rights to New Viking and New Warren for the "Houdaille-Era Claims," and if they did, the assignments were precluded by the policies' anti-assignment provisions. The Court examined the New Warren acquisition of Warren Pumps through a 1985 Asset Sale Agreement and subsequent amendment, and ruled that the parties indeed assigned New Warren the rights to Houdaille's excess policies. The Court also found that New Viking acquired Houdaille's insurance rights through a more complex Assignment and Assumption Agreement. Finally, the Court rejected the insurers' attempt to void the assignments under the policies' anti-assignment provisions, holding that New York law does not enforce such provisions in the context of "post-loss assignments." Vice Chancellor Strine rejected the insurers' argument that the anti-assignment clauses should be enforced because the asbestos liabilities were too speculative as of the 1985 acquisition date, or were not reduced to a fixed amount at the time of assignment. Instead, the judge ruled that the loss occurs when liability arises, i.e. exposure to asbestos, because the insured risk is no greater than it was pre-assignment.

After determining that New Warren and New Viking were entitled to insured status under Houdaille's excess insurance policies, the Court turned to the allocation issue. The excess insurers argued that controlling New York precedent requires a *pro-rata* allocation as set forth in *Con Edison v. Allstate Ins. Co.,* 774 N.E.2d 208 (NY 2002), while the insureds argued for an "all sums" approach. The Court captured the competing policy considerations in a particularly cogent passage:

> Courts more concerned with guaranteeing full compensation to tort plaintiffs and holding insurers accountable up to the full policy limits when a policy is triggered, tend to favor the all sums method. By contrast, other courts have thought it unfair to hold a particular insurer fully responsible for an asbestos judgment against its insured when that insurer only had the coverage for, say, a year of the exposure period. These courts have tended to favor the pro-rata approach.

From there, the Court launched an attack on the *Con Ed* decision (from New York's highest court), then distinguished its ruling based on policy language. In casting aside the conclusion reached in *Con Ed,* the court noted that "the New York Court of Appeals did not engage in an extended public policy analysis (or even any at all). It simply decided that the insurance policy in question was best read as embracing the pro-rata method of allocation." The Court interpreted *Con Ed's* "terse reasoning" to mean that the Court of Appeals did not intend to establish a bright-line rule. Thus, the Court declared that New York's Court of Appeals has not committed to a blanket position on allocation, but rather looks to the policy language at issue to effectuate the agreement of the parties. In *Con Ed*, the Court based its pro-rata allocation ruling on policy language limiting coverage to occurrences happening "during the policy period." While purporting not to "quibble with the ultimate holding" in *Con Ed,* Vice Chancellor Strine unabashedly noted that its analysis is "extremely abbreviated and, at least to this mind, hardly compelled" by the policy language, and "it is not at all clear why the 'during the policy' period language would be seen as limiting an insurer's responsibility[.]"

Turning to the Houdaille policies, the Court concluded that the policies' Non-Cumulation or Prior Insurance provisions "cannot sensibly be applied within a pro-rata allocation scheme." The Court reasoned that the Non-Cumulation provision expressly takes into account situations where different policies must respond to the same injury, and deems the plaintiff's injury as indivisible and resulting from a single occurrence. According to the Court, the pro-rata allocation approach effectively treats an injury as *divisible* – a separate occurrence during each policy period – in contravention of the plain language of the policies. The Court also took note of other jurisdictions, including the Delaware Supreme Court, that recognize the inherent contradiction of Non-Cumulation provisions with the pro-rata allocation method, which can result in a "double credit" for insurers.

Viking Pump is a potentially troubling development for insurers operating under New York law. Pursuant to Vice Chancellor Strine's "all sums" ruling, New Warren and New Viking can now designate a single policy year to bear the responsibility for a covered loss, and leave it up to those insurers to then seek reimbursement from other insurers. Also, under the "all sums" allocation method, the insurers bear the brunt of any insurer insolvencies or uninsured periods of time. The decision may reopen what was deemed settled law on allocation in New York and make Delaware a magnet for coverage litigation, particularly for insureds with policies written out of New York.

For a further analysis of the coverage issues arising from this decision, please contact William Shelley (wshelley@cozen.com or 215.665.4142), Global Insurance Group Department Chair, or Joseph Arnold (jarnold@cozen.com or 215.665.2795). Cozen O'Connor is a nationally recognized leader in representing the insurance industry in all coverage areas.