

Perspectives on Insurance Recovery



Welcome to the latest edition of Pillsbury's *Perspectives on Insurance Recovery*. In the past year, our firm has welcomed a nationally renowned team of insurance litigators to its Washington, DC, office. We also won what the *National Law Journal* hailed as the two biggest U.S. insurance recovery jury verdicts of 2015—a \$55 million win for Victaulic and a \$72 million jury verdict for Lion Oil. And most recently, we launched *Policyholder Pulse*, our Insurance Recovery & Advisory practice blog that provides news and insights on all aspects of insurance coverage law. (Visit policyholderpulse.com to learn more.)

Whether you need an advocate in a dispute with carriers or advice on the placement of coverage, you can count on Pillsbury's team of more than 30 attorneys to provide you with knowledgeable, efficient and practical assistance.

This 2016 edition of *Perspectives* touches on some of the most challenging issues insureds face today—from new risks for directors and officers to emerging trends in case law, and beyond. We hope you enjoy this edition, and we welcome any feedback.

Peter Gillon and Robert Wallan
Co-leaders, Insurance Recovery & Advisory

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The Yates Memo's Focus on Individuals in Corporate Misconduct Investigations Puts D&O Insurance in the Crosshairs



By Robert L. Wallan and Vernon Thompson, Jr.

On September 9, 2015, United States Deputy Attorney General Sally Yates released a memorandum refocusing the Department of Justice's prosecution of corporate misconduct. That memorandum, now known as the "Yates" memo, directed federal prosecutors to, among other things, not settle with corporations under investigation unless those corporations forsake the individuals that engaged in the wrongdoing and to focus investigations on individuals from the start. Not surprisingly, the DOJ's renewed focus on the prosecution of individuals has left many directors and officers concerned about their potential exposure should the DOJ come knocking at their company's door. As should be the case, D&O insurance is often a key part of the defense when it comes to addressing potential threats of legal action from the government or otherwise. This note discusses the potential risks to D&O insureds due to the approach outlined in the Yates Memo.

The Yates Memo reflects a change in the DOJ's approach for investigating and prosecuting corporate misconduct distinctively focused on holding individuals responsible for wrongdoing that puts a corporation on the DOJ's hot seat. It does not, however, necessarily represent an increase in the powers that were already available to the DOJ. Instead, the memo outlines six "key steps" to strengthen the DOJ's pursuit of individual corporate wrongdoing. Yates Memo at 2. These steps include (1) requiring corporations to provide the DOJ "all relevant facts relating to the individuals responsible for the misconduct" in order to qualify for any cooperation credit; (2) focusing criminal and civil corporate investigations on individuals from the start; (3) maintaining routine communication between criminal and civil attorneys handling corporate investigations; (4) not releasing culpable individuals from civil or criminal liability when resolving a matter with a corporation absent extraordinary circumstances; (5) not resolving matters with a corporation without a clear plan to resolve related individual cases; and (6) requiring civil attorneys to consistently focus on individuals as well as the company and to evaluate whether to bring suit against individuals as well as the company based on considerations beyond that individual's ability to pay. Yates Memo at 2-3.

The good news for D&O policyholders is that the new focus outlined in the Yates Memo does not appear to foreshadow an emergence of new categories of claims or enforcement powers for the DOJ. But while the categories of claims or enforcement have not increased, directors and officers, and their companies, will likely face increased risk in that the Yates Memo suggests that resolution of DOJ claims will be more difficult. The Yates Memo could result in more investigations and potential claims against individual executives (and more extensive internal investigations of executive misconduct).

At the very least, the Yates Memo should inspire policyholders to take a second look at their D&O coverage, and to ensure that they have sufficient limits to address an increased likelihood of more expensive claims.

One method for addressing potential limits gaps for individual directors and officers is through the purchase of what is known as Side-A/Difference in Conditions (DIC) coverage which generally provides coverage in instances where a corporation fails or refuses to indemnify its directors and officers, and in some instances can provide coverage where a loss is not indemnifiable by the company. It is also worth checking to see if the available D&O coverage includes civil or criminal investigation coverage for the company in addition to coverage for investigations of individual insureds. Such expanded coverage can offset some of the increased investigations cost that might be incurred as a result of the Yates Memo.

Despite the shift in focus of DOJ enforcement towards individuals, however, the Yates Memo does not take corporations off the hook for corporate wrongdoing. To the contrary, more actions against insureds (both against companies who refuse to fully cooperate with the DOJ and against individual executives whose companies have cooperated) are likely to result in an increase in the costs incurred in investigating and defending those actions. Moreover, in addition to costs for reimbursing embattled executives as a result of more actions against them, corporations might also see an increase in costs incurred due to conflicts of interest created by the Yates Memo's requirement that they hand over their executives to the DOJ in order to receive cooperation credit. In such cases, a corporation may be required to retain independent counsel to defend individual executives, rather than relying on a single firm to handle the investigation and defense of the corporation and its executives. This requirement that a corporation

must provide DOJ investigators with all relevant facts related to the individuals responsible for the misconduct in order to qualify for cooperation credit could also increase costs as it places a higher burden of investigation squarely upon the corporation.

Finally, although the largest impact of the Yates Memo on D&O insurance may be on limits, policyholders must still take care to ensure that the terms of their policies are appropriate for responding to potential claims. The provisions of a D&O policy most likely to come into play for claims related to alleged executive misconduct include what are known as the "conduct exclusions." These include exclusions related to "the gaining of any profit, remuneration or financial advantage to which any Insured was not legally entitled" and "any deliberately fraudulent or deliberately criminal act, error or omission." These exclusions, however, should include standard industry enhancements that limit their applicability to instances where there is "a final, non-appealable adjudication" as to such conduct in an underlying action not brought by the Insurer. For purposes of DOJ investigations, and potential settlements, this language is crucial as it can protect directors and officers from having to foot their own bill for what can be a very costly process. Thus, in addition to addressing their policy's limits, it is vital that D&O policyholders review their policies with an eye toward ensuring that these and other enhancements are in place. ■ ■ ■



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Viking Pump: Landmark Victory for Policyholders

By Joseph D. Jean, David F. Klein and Benjamin D. Tievsky

New York has developed a reputation as an unfavorable jurisdiction for policyholders facing “long-tail” claims involving gradually occurring property damage or bodily injury liabilities, such as environmental contamination, asbestos-related illness, and certain toxic tort and construction defect claims. It owes this reputation, in part, to unfavorable case law on the allocation of insurers’ coverage obligations for claims triggering coverage across multiple policy periods, epitomized by the New York Court of Appeals’ decision in Consolidated Edison Co. of New York v. Allstate Insurance Co., 98 N.Y.2d 208 (2002). On May 3, however, the Court of Appeals issued a landscape-changing unanimous decision in In re Viking Pump, 2016 WL 1735790 (N.Y. May 3, 2016).

Ruling on allocation and a related issue, exhaustion, the Court of Appeals granted the policyholders’ request to employ “all sums” and “vertical exhaustion” approaches to policies containing “non-cumulation” and “prior insurance” provisions. These two methods allow a policyholder to maximize coverage by (1) picking policy year(s) in which triggered policies will be tapped, and (2) accessing excess or umbrella coverage

immediately upon exhausting the underlying primary policy.

This article introduces the concepts of allocation and exhaustion; discusses the dominant approaches to these issues; examines the context and import of the *Viking Pump* decision; and discusses practical lessons for continuous damage claims under New York law. While specific policy wording remains

controlling in every coverage case, *Viking Pump* represents a significant victory for policyholders in New York and has important national ramifications.

Allocation and Exhaustion

Commercial General Liability (CGL) policies typically cover bodily injury or property damage caused by an “occurrence” during the policy period. Certain types of claims, such as latent environmental or bodily injury exposures, present a continuing process that may span multiple successive policy periods. Because CGL policies usually define a “continuous or repeated exposure to conditions” as a single occurrence, courts frequently hold that multiple policies may be triggered by one occurrence. For example, in *Continental Casualty Co. v. Rapid-American Corp.*, the Appellate Division held that numerous CGL policies issued over a nine-year period were all triggered by claims of asbestos-related illness where the claimants allegedly inhaled asbestos fibers during a corresponding period of time. 177 A.D.2d 61, 65-66 (1st Dept. 1992), aff’d, 80 N.Y.2d 640 (1993). Similarly, the U.S. Court of Appeals for the Second Circuit, applying New York law, held that progressive damage to soil and groundwater resulting from environmental contamination implicated multiple successive policies. *Olin Corp. v. Insurance Co. of North America*, 221 F.3d 307 (2d Cir. 2000).

When multiple policies are triggered in such a way, courts must determine how coverage is allocated among the triggered policies. This issue has given rise to epic litigation in many jurisdictions. Policyholders typically invoke CGL insurers’ agreement to reimburse “all sums” or “those sums” the insured becomes legally obligated to pay due to an “occurrence” during the policy period, stressing that once an occurrence “triggers” coverage under a policy, each insurer becomes “jointly and severally” liable to pay “all sums” up to

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its policy limits. When multiple policies are triggered, insurers may use equitable contribution to sort out the allocation of liability among themselves.

Insurers, on the other hand, often seek pro rata allocation, which apportions damages to coverage based on each insurer's "time on the risk," corresponding to the damage presumed to occur during each policy period. Insurers argue this approach is more efficient and equitable. But practically speaking, pro rata allocation reduces each insurer's liability, while the policyholder faces increased exposure. Because the loss is prorated among multiple "triggered" years, significant parts of the loss may be allocated to years in which no coverage is available for the loss, whether because it could not be purchased in the market or individual insurers have become insolvent. Moreover, by triggering multiple years, pro rata allocation makes the policyholder absorb multiple self-insured retentions or deductibles, such that a much larger portion of the loss—and often the entire loss—fails to reach in the insurers' coverage at all.

While courts in other jurisdictions have been sharply divided, "all sums" appears to be the better rule. It is based upon contract construction, as opposed to debatable extra-contractual notions of "fairness." It is more easily applied, insofar as it avoids complex disputes about the precise method of proration. It leads to more predictable results, and is also in concert with many insureds' reasonable expectations as consumers, in the absence of contrary policy language. At the macro level, it may also provide an incentive to purchase insurance, ultimately furthering the public policy goal of compensating injured parties. Still, no clear "majority view" has emerged. *Viking Pump*, however, teaches that some policies may contain particular provisions arguably favoring an all sums approach, such as non-cumulation or prior insurance clauses.

A related issue, on which courts also have taken different approaches, is determining

when and how excess or umbrella policies are triggered by the exhaustion of underlying primary coverage. When policies in multiple periods are triggered, insurers often argue for "horizontal exhaustion," requiring the policyholder to exhaust primary policy limits in all policy periods before excess coverage can be invoked in any period. That approach effectively imposes a form of pro rata allocation before any excess insurance can be tapped, and thereby reduces the policyholder's recovery significantly.

Policyholders frequently favor "vertical exhaustion," under which excess coverage is tapped upon the exhaustion of immediately underlying primary coverage, regardless of exhaustion in other policy periods, allowing easier access to the highest limits of excess coverage. Courts have been more likely to apply vertical exhaustion when the excess policy specifically identifies the primary policy over which it sits, and horizontal exhaustion where the excess policy does not specifically identify the primary policy and "other insurance" clauses purport to include all triggered primary policies as part of a retained limit.

Like all sums allocation, vertical exhaustion seems generally to be the better rule—it is more easily applied, leads to predictable results, and conforms to policyholders' expectations. Even so, there is no "majority rule," and specific policy language may be dispositive.

"All Sums" or "Pro Rata"

Prior to *Viking Pump*, New York state and federal courts had, for the most part, applied pro rata allocation in a variety of circumstances. The New York Court of Appeals did not squarely address the allocation of indemnifiable losses until 2002 in *Consolidated Edison*. 98 N.Y.2d 208 (2002).

Consolidated Edison involved claims arising from environmental contamination from the operation of a manufactured gas plant from 1873 to 1933.

THE TOP 100 VERDICTS OF 2015

National Law Journal

Pillsbury's Insurance Recovery & Advisory team helped policyholder clients—Lion Oil and Victaulic Company—achieve two landmark verdicts in 2015. Lion Oil won a \$72 million breach of contract verdict and Victaulic Company was awarded \$55 million in a landmark bad faith verdict and judgment. Both verdicts were ranked in the top third of the year's largest verdicts by *National Law Journal* and VerdictSearch.

Download *National Law Journal's* coverage of Pillsbury's top-ranked 2015 verdicts here:
<http://goo.gl/s9atFd>

The allegedly continuous release and migration of coal tar and other hazardous wastes through groundwater triggered policies over 50 years. One of the excess insurers moved for dismissal, arguing that under a pro rata allocation, the policyholder's highest damages projection would be insufficient to reach its excess coverage in the relevant year. The trial court applied pro rata allocation and dismissed over a dozen insurers from the case. *Id.* at 215-16. The Appellate Division and the Court of Appeals affirmed.

The Court of Appeals held that pro rata allocation, "while not explicitly mandated by the policies," was consistent with the policies' definition of "occurrence." *Id.* at 224. The court, however, declined to construe non-cumulation clauses in some

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Don't Allow Terrorism Exclusions to Attack Your Coverage

By Vincent E. Morgan and Tamara D. Bruno



The recent bombings at the Brussels Airport and Maalbeek metro station are another sobering reminder of how much vigilance is needed to protect against these kinds of public health and safety from attacks. They show once again that violence—whether resulting from terrorism or otherwise—can occur any time at any place, and can have far-reaching impacts.

Risk management programs should generally include measures to reduce the risk of violent attacks, such as security policies and procedures. At the same time, companies should also prepare for the possibility that precautions are not enough to prevent all attacks. As a result, preparations should also include steps such as creating a comprehensive crisis response plan as well as reviewing the “terrorism” provisions in the company’s insurance policies.

Terrorism provisions may cover terrorism or exclude it. In addition, the scope of these provisions can vary widely from policy to policy.

Terrorism coverage usually defines “terrorism” narrowly. For example, under the Terrorism Risk Insurance Act, a terrorist attack must meet a minimum damage threshold and be officially certified as an “act of terrorism” to trigger coverage under the program.

Conversely, terrorism exclusions often define “terrorism” broadly. Sometimes these provisions are so broad they could be read to exclude coverage for claims

that would not normally be thought of as “terrorism.”

One recent piracy case we handled illustrates this point. Several gunmen boarded an oil rig off the coast of Nigeria, wounding workers and holding them hostage, even taking one of them ashore to a camp in Nigeria for ten days before he was rescued “amidst gunfire, bombings, and a helicopter raid.” After being sued by victims of this incident, our clients sought coverage under several policies, including package policies as well as stand-alone kidnap and ransom policies. Some of those policies defined “terrorism” as:

the use or threatened use of force or violence against persons or property, or commission of an act dangerous to human life or property, or commission of an act that interferes with or disrupts an electronic communication system, undertaken by any person or group, whether or not acting on behalf of or in connection with any organization, government, power, authority or military force when the effect is to intimidate or coerce a government,

the civilian population or any segment thereof, or to disrupt any segment of the economy.

The carriers denied coverage, principally relying on this definition, and suit was filed in response. The court found these events could reasonably be “terrorism” because such actions could (1) have a chilling effect on maritime activity in African coastal waters, a “segment of the economy,” and (2) could intimidate all vessel workers in that area, a “segment” of the “civilian population.”

On the other hand, the court also found that these events could reasonably be just a violent robbery and kidnapping only affecting the workers on that rig, and so not “terrorism” under the policies’ definition. Because both interpretations were reasonable and all doubts must be construed in favor of coverage, the court properly held in favor of the insureds.

Even though the insureds prevailed, it is significant that the court found a broad reading of the terrorism exclusion was “reasonable.” Under that reading, claims such as premises liability for a parking lot holdup might constitute “terrorism.” Insureds should check their policies for similar language. If broad terrorism exclusions are present as well as vulnerability to terrorist attacks, it may be worthwhile to ask for a narrower definition or look elsewhere in the market. As the history of this claim illustrates, insurers are not shy about raising terrorism exclusions to bar coverage. ■ ■ ■



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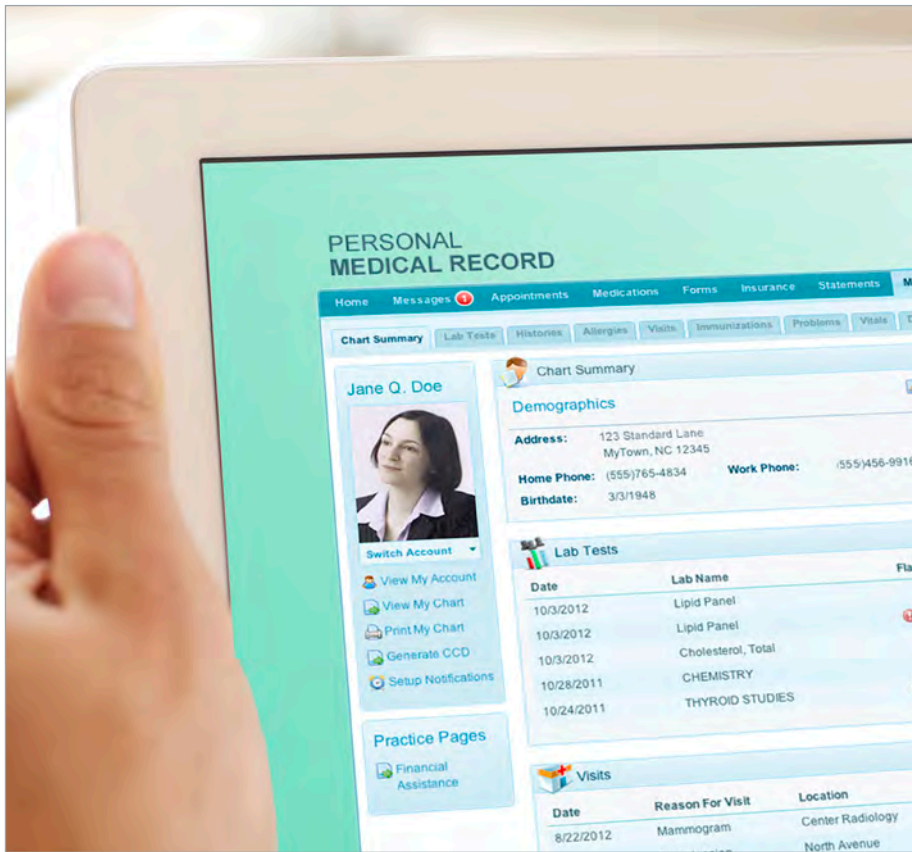


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Fourth Circuit Finds Coverage for Cyber Incident Under Commercial General Liability Policy

By James P. Bobotek, Peri N. Mahaley and Benjamin D. Tievsky

On April 11, the U.S. Court of Appeals for the Fourth Circuit rendered one of the first appellate-level decisions dealing with insurance coverage for a cyber event. The Fourth Circuit confirmed that a commercial general liability insurer was obligated, under the policy's "personal and advertising injury" coverage, to defend its insured against a class-action lawsuit arising out of the inadvertent posting of patient medical records on the internet. The decision is an important victory for policyholders because it validates a position against which insurers have aggressively fought for the past several years—coverage for cyber events is not only available under specialized "cyber" policies, but may also be obtained under traditional commercial policies.



The case, *The Travelers Indemnity Company of America v. Portal Healthcare Solutions, LLC*, involved a company specializing in maintaining and safeguarding medical records for hospitals, clinics, and other health care providers (Portal). In 2013, two patients of an upstate New York hospital discovered that their confidential hospital records were publicly accessible on the internet. When each of the

patients entered her name into Google's search engine, the first result that came up was a link to a file containing her treatment history, lab data, medications, examination results, and other private information. The patients filed a putative class-action against Portal, which had been engaged by the hospital to provide electronic storage and maintenance of patients' medical records. The suit alleged that, due to Portal's negligence,

2,300 hospital patients' personal health information and other private data had been posted online without authorization, and was available to the public to view, copy, and download without restriction. According to the complaint, this information could be accessed simply by searching for a patient's name in an internet search engine. While the complaint did not specify precisely how, or by whom, the data was posted to the internet, it alleged that Portal had acknowledged that "through human error," its server had been left "open" or "unprotected" for a period of four months, thus leaving the medical information accessible through simple internet searches.

Portal turned to its commercial general liability (CGL) insurer, Travelers, to defend it in the class-action suit and to cover any resulting settlement or judgment. Portal had purchased CGL policies from Travelers for two successive policy years. The first policy contained an endorsement covering "those sums the insured becomes legally obligated to pay as damages because of ... 'web site injury'["] "Web site injury" was defined as injury "arising out of ... [o]ral, written or electronic publication of material that ... gives unreasonable publicity to a person's private life." The second policy contained the traditional CGL coverage for "personal and advertising injury"

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Hurricane Season Is Here— Is Your Insurance Program Ready for the Next Storm?



By Joseph D. Jean, James P. Bobotek and Vincent E. Morgan

The past several years have witnessed massive storms ripping across the United States, causing unprecedented damage to coastal and inland areas lying in their path. Wreaking havoc across the land, they have caused tidal surges that have inundated areas that have otherwise never experienced such damage and knocked out critical infrastructure including power, rail and subway systems. Not to mention the tens of thousands of homes and businesses destroyed. 2012's Superstorm Sandy caused at least \$50 billion in physical damage and catastrophic business interruption losses.

As is the case after any natural catastrophe, affected businesses turn to their insurance carriers for help. But many policyholders are taken aback by the significant obstacles insurers place before them in responding to their property and business interruption insurance claims. Superstorm Sandy was the latest wake-up call for policyholders in the Northeast, many of whom had previously perceived the risks associated with hurricane, flood and storm surge damage as highly unlikely.

Given, however, that the National Oceanic and Atmospheric Association and other organizations have predicted “extreme activity in the Atlantic” this hurricane season, with “more

and stronger hurricanes” expected, there is no better time to review your property and business interruption insurance coverage. Here, we provide an overview of some insurance coverage-related issues typically experienced by commercial policyholders after a catastrophic storm.

Prepare in Advance and Review Sublimits and Deductibles for “Named Storm” and “Flood” Coverage

Property insurers have sought to limit their exposure to flood risks in coastal areas by reducing policy sub-limits and increasing deductibles. While many insurers have restricted coverage for

“Flood” perils in this fashion, they have not always included similar limitations for “Named Storm” perils. For example, while many policies categorize certain counties in New York, Connecticut and New Jersey as high-risk flood zones, they are still low-risk areas for “Named Storm” perils. Yet, as Sandy hit businesses with a double-whammy of hurricane force winds and resulting flooding, many insurers asserted applicability of the lower sub-limits and higher deductibles tied to Flood perils, instead of the more policyholder-friendly “Named Storm” sub-limits and deductibles. This led to a significant number of post-Sandy disputes. In cases in which policyholders were not aware of this distinction, they lost significant coverage.

In this regard, it is also important to understand whether your policy includes lower sub-limits for some locations and not others and whether your business has substantial operations at those locations. Similarly, courts have held that some policies do not include business interruption or “Time Element” losses within certain sub-limits such as Flood. Knowing this before the loss is important to ensuring that your loss is adjusted properly.

Beware of Concurrent Causation Language for Losses Involving Both Covered and Non-Covered Perils

Large impact storms compel policyholders and insurers alike to scrutinize policy language and case law for guidance on the extent to which losses are covered when caused concurrently or sequentially by perils that are covered by multiple perils (such as Named Storm, Fire, or Wind-Driven Rain) and also perils that are expressly excluded or sub-limited (such as Flood). For instance, as with the Named Storm vs. Flood discussion above, the issue may also arise because the loss originated from Named Storm or Wind, and the resulting storm surge. But insurance companies say the most immediate cause was Flood, subject to a lower sublimit

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Even in NY, Unclear Policy Terms Favor the Insured

By Stephen S. Asay

New York has a reputation for being a jurisdiction that is unfriendly to policyholders—and in many ways that reputation is justified. But in the recent case of Fabozzi v. Lexington Insurance Co., the U.S. Court of Appeals for the Second Circuit affirmed that New York still adheres to what is a bedrock principle in most jurisdictions around the country: ambiguities in an insurance policy must be construed against the insurer.

The case involves damage to a Staten Island home owned by the Fabozzi family. In 2002, the Fabozzis began to notice cracks and fissures in the walls and floors of their home, and gaps between the walls and window frames. After noticing these problems, the Fabozzis hired an architect to inspect the home. Those inspections revealed that the interior walls of the Fabozzis’ home were so rotted that the entire structure was on the verge of collapse. The imminent collapse made the home uninhabitable and the Fabozzis had to move out.

Faced with the complete loss of their home, the Fabozzis understandably turned to their homeowners’ insurance policy with Lexington Insurance—the same insurer that had been providing the

Fabozzis’ homeowners’ insurance since 1992. Among other things, the policy provided the Fabozzis with coverage for collapse (Additional Coverage 8):

Collapse. We insure for direct physical loss to covered property involving collapse of a building or any part of a building caused only by one or more of the following:

...

b. Hidden decay;

c. Hidden insect or vermin damage

...

At first glance, this provision appears straightforward and unambiguous: the policy provides coverage for collapse if the collapse is “caused only by one or more of” the named perils. But

that simple, seven-word phrase led to Lexington’s denial of coverage and a decade of litigation.

The Fabozzis read the phrase as providing coverage “only if the collapse is caused by one of the following” named perils. In other words, the Fabozzis would simply need to prove that one of the listed perils caused the collapse, even if another nonlisted peril had contributed. Lexington argued that the phrase limited coverage to a collapse “caused exclusively by one or more of the following” named perils. In other words, if any nonlisted peril contributed to the collapse, the Fabozzis were out of luck.

The U.S. District Court for the Eastern District of New York agreed with Lexington and instructed the jury that they must find for Lexington if the Fabozzis had not shown “that the collapse was caused only by hidden decay or insect or vermin damage.” This instruction was repeated on the jury verdict sheet, which asked: “Have the plaintiffs proven by a preponderance of the evidence that any collapse of the property ... was caused only by hidden decay or hidden insect or vermin damage?” The jury answered “no” and found in favor of Lexington.

On appeal, the Second Circuit disagreed with the trial court, finding that Additional Coverage 8 was ambiguous. The provision clearly operated as a limit on the perils against which Lexington insured. But neither party’s position was clearly the correct interpretation. The susceptibility of the policy to two opposite—but both reasonable—interpretations was a textbook example of ambiguity, and nothing elsewhere in the language of the policy indicated whether one interpretation should have prevailed. However, the Second Circuit noted that several considerations weighed strongly in favor of the Fabozzis’ interpretation.

First, New York law imbues the word “caused” with legal meaning in the context of insurance contracts. If both

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Viking Pump: Landmark Victory for Policyholders

of the policies, which might have argued in favor of an all sums methodology. The door therefore remained open for the Court of Appeals to revisit allocation in a case involving CGL policies with non-cumulation and other applicable provisions.

In *Viking Pump*, the high court considered questions of allocation and exhaustion on certification by the Delaware Supreme Court, which was reviewing lower Delaware court decisions applying New York law. *Viking Pump* involved asbestos exposure claims that triggered policies over 13 years. The Court of Appeals was asked to decide “(1) whether ‘all sums’ or ‘pro rata’ allocation applies where the excess insurance policies at issue either follow form to a non-cumulation provision or contain a non-cumulation and prior insurance provision, and (2) whether ... horizontal or vertical exhaustion is required before certain upper level excess policies attach.”

The insurers wanted to extend *Consolidated Edison*'s pro rata ruling. But the Court of Appeals unanimously sided with the policyholders, construing the relevant policy provisions as requiring all sums allocation and vertical exhaustion. Without overruling *Consolidated Edison*, the court definitively stated that pro rata allocation is not the “blanket rule” in New York.

Generally, non-cumulation clauses purport to prevent an insured from “stacking” together the limits of triggered policies in multiple periods to cover the same loss. The excess policies in *Viking Pump* either contained, or followed form to policies that contained, such clauses, providing that if personal injury or property damage occurs partly before and partly within the policy period, the policy's limits would be reduced by the amount paid under policies triggered in previous years.

PILLSBURY TRIAL TEAM ROARS WITH A \$72 MILLION WIN FOR LION OIL

A crude oil refinery company in El Dorado, Ark., was impacted severely when a 60-year-old Exxon crude pipeline ruptured in April 2012, causing a yearlong outage that prevented crude oil from reaching the company's refinery. Suffering a major disruption to its plant operations, the refinery company filed a business interruption claim under its all-risks policy with its group of 14 insurance carriers—basically, all of the major players in business interruption insurance.

Not only did the insurers take a year to finally deny the claim, but on that same day, they also sought a declaratory judgment in court denying the refinery company's claim, and requiring that all claims disputes involving the company be decided in Tennessee. Pillsbury stepped in, got the Tennessee case dismissed and then filed suit. Despite the insurers' summary judgment bids, numerous coverage-related trial motions, and repeated attempts to disqualify our expert witnesses through evidentiary objections and a request for a mistrial, Pillsbury's Insurance Recovery & Advisory team ultimately cleared every hurdle. After eight days of trial, and just two hours of deliberation, the jury delivered a spectacular win for our client. They awarded \$71.7 million—the full amount requested in our opening statement.

Not only was the award among the largest jury verdicts ever obtained in the state of Arkansas, this victory was one of the rare instances when an insured succeeded in obtaining full recovery on a disputed contingent business interruption claim. The case made news throughout the industry, delivering a clear and strong message that Pillsbury's trial lawyers deliver winning results, even under the most intense pressure.

Pillsbury's trial team was led by Washington **Insurance Recovery partner Geoffrey Greeves**. Pillsbury **partner Peter Gillon**, head of the firm's Insurance Recovery practice who served as trial co-counsel, added: “Proving a company's rights to insurance for damages to a supplier can be challenging, and we are pleased that both the jury and the court understood the way these policies are supposed to work and awarded our client the compensation they were owed. We particularly want to credit Lion Oil for having the fortitude not to cave when its insurers sought to evade their obligations to cover the company's losses.” Other members of the Pillsbury trial team included **senior associate Vernon Thompson** and former associate Ashley Joyner. The firm was assisted by Arkansas counsel Brian Ratcliff and Julie Greathouse of the Little Rock firm of PPGMR Law PLLC. ■ ■ ■

The court held that such language expressly contemplates that the coverage applies to damage before the policy period, subject only to a “credit” to the insurer for amounts recovered for the same occurrence under another policy. Similarly, prior insurance clauses in some of the policies provided that coverage for an occurrence continuing

after the policy period would be reduced by amounts recovered under subsequent policies; this likewise contemplated the policy's coverage also extended to losses beyond the policy period. The court held that pro rata “time on the risk” allocation would be inconsistent with

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Viking Pump: Landmark Victory for Policyholders

these provisions, which clearly indicated the policyholder could recover all loss from a multi-year occurrence under any triggered policy (i.e., all sums), subject to offsets.

With respect to exhaustion, the Court of Appeals rejected the excess insurers' assertion that horizontal exhaustion was the default rule in New York. The excess policies at issue specified that they sat above underlying policies covering the same policy periods that were identified by name, policy number, or policy limit. The clear implication of such excess attachment language is that only the specified underlying policy—but not all primary policies in all years—must be exhausted before the excess coverage is triggered (i.e., vertical exhaustion).

Against this, the insurers argued that “[t]he policy nowhere says that the exhaustion of the directly underlying ... policy is the only condition precedent” for the attachment of the excess coverage. They also pointed to the policies’ “other insurance” clauses, which, they argued, included sums recoverable under successive policies as part of the insured’s retained limit. The court rejected these arguments, noting that “other insurance” clauses only apply when multiple policies provide coverage for the same policy period, and only serve to prevent multiple recovery under such policies. The court also noted that vertical exhaustion is “conceptually consistent with an all sums allocation[.]”

Practical Takeaways

An example illustrates the profound effect of the *Viking Pump* ruling. Suppose a policyholder has a multi-year environmental claim to which New York law applies. Contamination resulting from site operations continued for 50 years, but only 10 years of insurance

policies are available, and in five of those years, the policies contain pollution exclusions barring coverage. Under a pro rata allocation, the policyholder can recover no more than one-tenth of the total loss (five years of available coverage for a 50-year loss)—and even this would likely be subject to five years’ worth of retentions or deductibles. But, under an all sums approach, the policyholder can target any one of the five years of available coverage and place the entire loss—vertically—into that single year. Thus, depending on available limits, the policyholder may recover 100 percent of the loss, subject to one policy year’s retentions and deductibles.

Many policyholders may be able to take advantage of the *Viking Pump* ruling to effectuate an all sums recovery for a progressive bodily injury or property damage claim, especially given the fairly common presence of non-cumulation and prior insurance clauses in excess and umbrella policies issued since the 1960s, as well as in policies sold by mutually owned insurers in certain industries. Indeed, other states’ high courts have applied all sums even in the absence of such clauses. ■ ■ ■



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Fourth Circuit Finds Coverage for Cyber Incident...

liability, covering “injury caused by [o]ral or written publication of material, including publication by electronic means, of material that ... [d]iscloses information about a person’s private life.” After denying its duty to defend Portal, Travelers filed a complaint in the U.S. District Court for the Eastern District of Virginia, seeking a declaration that it was not required to defend Portal.

On cross-motions for summary judgment, Travelers argued that the underlying complaint did not allege a “publication” of private information because there were no allegations that third parties actually viewed the plaintiffs’ medical records. Travelers also contended that there had been no “unreasonable publicity” or “disclosure” because the complaint did not allege that Portal acted affirmatively to attract public interest in the records or that it disclosed plaintiffs’ information to anyone other than the plaintiffs themselves. In keeping with the broad scope of the duty to defend under Virginia law, the district court rejected Travelers’ arguments, entering summary judgment in Portal’s favor.

Relying heavily on the dictionary definition of “publication,” the district court found that information is “published” when it is merely “placed before the public.” The court also cited dictionary definitions of “publicity” as “the quality of state of being ... exposed to the general view,” and “disclosure” as “[the] process of making something known that was previously unknown.” Thus, it was clear that Portal’s posting of medical records on the internet had effectively “placed before” all internet users private information that was previously unknown to the public. On appeal, Fourth Circuit agreed, holding that Travelers must defend Portal because the complaint alleged

PILLSBURY LAWYERS HAMMER AIG ON BAD FAITH CLAIM DENIAL

Jury Awards \$55 million to Victaulic—including \$46 million in punitive damages

Victaulic Company paid insurance giant AIG premiums for commercial general liability policies for more than a decade. Year after year, AIG honored those policies. That is, until 2012, when, following a series of new product-liability claims, Victaulic turned to AIG for the protection it had promised to provide. But rather than honoring its promises, AIG turned around and sued Victaulic to avoid more than \$340 million in promised coverage.

Victaulic handed Pillsbury a mission: Beat back AIG, the eight different law firms the insurer hired and the multiple actions they filed against Victaulic around the country. And beat back AIG Pillsbury did. Pillsbury sued AIG in California and succeeded in getting each of AIG's three other actions dismissed and obtained multiple sanction awards against AIG for its discovery abuses. The Pillsbury team then tried Victaulic's remaining claims for breach of contract,

bad faith and punitive damages to an Alameda County jury. In one surprising courtroom moment, a senior AIG claims director even invoked her Fifth Amendment right to avoid self-incrimination during a Pillsbury cross-examination about sworn statements she'd made in AIG's discovery responses.

In August 2015, the jury awarded Victaulic a sweeping victory. The jurors found that AIG had breached the insurance policies and did so in bad faith, acting with malice, oppression or fraud; that Victaulic was entitled to more than \$9.3 million in compensatory damages and attorneys' fees; and that AIG must pay Victaulic an additional \$46 million in punitive damages. The jury's award was the largest in Alameda County in nearly a decade.

Mark Van De Voorde, Esq., Victaulic's Chief Legal and Administrative Officer, commented "This matter is critically important to Victaulic. AIG was, in our view, seeking to take back years of insurance it wrote to Victaulic. We were right to put our trust in Joe Jean and the Pillsbury team. Not only are we thrilled with the jury's verdicts, but we could not be more pleased with how these matters have been handled by Pillsbury."

Victaulic's trial attorneys were **Insurance Recovery & Advisory Partners Joseph D. Jean and Colin T. Kemp and Counsel Jeffrey A. Kiburtz**. Lead lawyer Joseph Jean said: "We are happy to have proven to the jury not only that AIG breached their contracts, but that they did so in bad faith, and that their conduct warranted punitive damages. This decisive outcome demonstrates that significant punitive damages are attainable even in complex commercial litigation." ■ ■ ■

that "any member of the public with an internet connection could have viewed the plaintiffs' private medical records during the time the records were available online[.]" and as such the information had been published and disclosed for the purposes of triggering Travelers' duty to defend Portal.

The Portal decision is significant in that it found coverage for cyber liability under a CGL policy. Nevertheless, we expect insurers will contend that Portal should be limited to its facts. They are likely to argue that, in finding an act of "publication," the court was heavily influenced by the fact that Portal's own acts or omissions led to the plaintiffs' damages, as opposed to the acts of a third party.

Among the lessons to be learned from Portal are:

- Victims of a cyber attack or data breach should examine all of their insurance policies. In addition to cyber policies, commercial general liability, errors and omissions, crime, first-party property and business interruption, and other types of policies may provide coverage;
- Some traditional policies may be purchased with endorsements extending coverage to "web site injury" or other cyber risk; and
- Policyholders should continue to expect strong resistance from insurers when it comes to providing coverage for a cyber event under traditional commercial policies. ■ ■ ■



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Hurricane Season is Here— Is Your Insurance Program...

and higher deductible for Flood than the policy has for Named Storm or Wind.

Various theories have developed to address the issue of multiple or sequential causation, with some courts applying the broad doctrine of “concurrent causation,” whereby coverage will be available if any one of the multiple causes of loss is a covered peril. Other courts apply the “efficient proximate cause” theory, whereby the fact finder looks at the circumstances of the loss to determine which cause was the dominant or efficient cause. Which may or may not be the initiating event in the chain of events. Critical is the highly fact-specific causation analysis requiring careful inquiry into the circumstances of the loss.

The answer also depends on whether your policy employs “anti-concurrent causation” wording. Insurance companies have attempted to eliminate the need for courts to search for the efficient proximate cause or even to consider multiple causes by incorporating ACC clauses into certain exclusions in property policies. These clauses attempt to preclude any claim that involves the particular excluded peril, even if that is only one of multiple causes of the loss. Such clauses were challenged following Hurricane Katrina and they are still the subject of hot debate following Superstorm Sandy. Because some courts have upheld their application, some states have recently introduced legislation to prohibit them or, at a minimum, to provide an express warning in the policy of their inclusion.

Identify Challenges of Proving Contingent Business Interruption Loss

Although many companies have experienced loss due to “Contingent Business Interruption”—that is, the economic effect on the insured of damage to the property of its customers and suppliers—proving CBI loss can present

significant challenges. Policies usually offer little guidance on the proof required to establish that a loss of business is attributable to the impact of a covered peril on a policyholder’s customers or suppliers. For example, as a condition to payment under CBI provisions, retailers in Lower Manhattan suffering major losses because their customers were impacted were asked to prove exactly which customers were affected by the storm—a burden that is challenging to meet, and, in the opinion of most experts, highly unreasonable. Requiring policyholders to overcome such evidentiary burdens as a condition to coverage is almost certainly contrary to the reasonable expectations of the commercial insured.

In the best of circumstances, proving losses due to damage to a supplier is difficult for policyholders. The insured typically does not have access to the supplier’s records, suppliers may fail to document their damages or repairs, and suppliers often have commercial reasons for not disclosing the cause or magnitude of their losses. The same is true of customers.

Review Civil Authority, Ingress/ Egress, and Service Interruption Coverage Language

Civil Authority provisions provide coverage for an insured’s business interruption losses resulting from orders of civil authority, such as evacuation orders, curfews, highway closures, and the like, which prevent or impair access to the insured’s property. The challenge in establishing Civil Authority coverage begins with the fact that most policies require that the governmental order be the result of physical damage “of the type insured,” and not just a preventive or general public safety measure. Some policies require that the physical damage be within a limited distance of the insured’s location. At least one court has held that post-hurricane civil evacuation orders triggered Civil Authority coverage even without physical damage. In the case of Superstorm Sandy, insurers resisted this coverage by arguing that while

there were numerous orders impacting business, the orders were not the direct result of physical damage, but rather to prevent harm to public health and safety. In some cases, insurers have claimed that the insured did not demonstrate the orders were the result of physical damage to property of the type insured, within a certain distance of the insured’s premises. Likewise, insurers have argued that the orders did not completely prevent or prohibit access to the insured location.

In addition to orders of Civil Authority that restrict access to an insured property, storm-related physical damage may limit an policyholder’s ability, or the ability of its customers or employees, to enter or exit its property. Ingress/Egress coverage typically insures business interruption losses incurred when access to or from an the policyholder’s premises is “physically prevented” by the loss or damage. Even if a governmental authority does not issue an evacuation order, storm or flood damage may limit access to a business or property and result in business loss. Ingress/Egress clauses can extend business interruption coverage, at least where property damage “in the vicinity” restricts access to insured premises. This coverage is generally understood to include loss resulting from situations where insured damage in the vicinity of the property, and other such conditions prevent access to the insured’s property.

When utility services to insured premises are interrupted, Service Interruption coverage may be available to cover damage to property (e.g., spoiling of refrigerated food or medicine) and loss of income or extra expense. The coverage for such interruption can be substantial, including payroll incurred when the company is closed, loss from event cancellation, extra expense, contractual penalties and lost profits. Post-storm disputes usually involve whether the Service Interruption was caused by a covered event away from an insured’s premises. Service Interruption coverage generally requires damage to the property of a utility supplier used

by the insured, and sometimes includes requirements that the damage occur within a specified distance to the insured property, or even on the insured property. Service interruption coverage would typically apply to power outages where overhead power lines downed by a storm or physical disruption to a transformer or generating station prevent a manufacturing plant or hotel from operating normally. Understanding your specific requirements before the loss is important.

Conclusions

Recent storms have left a legacy of losses and disputes that will have lasting repercussions for policyholders around the United States. Major disputes with insurers, have shaped the landscape and will continue to challenge the conventional wisdom regarding Flood and Named Storm coverage. One point on which all those knowledgeable about these nuances agree is that the challenges normally inherent in presenting property damage, business interruption and other economic claims were are becoming more and more difficult for policyholders who are not prepared in advance of the loss. A pre-storm review of your policy will provide you with the opportunity to ensure that you understand the coverage you purchased before a loss occurs. And to maximize your coverage after the storm hits. ■ ■ ■



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Even in NY, Unclear Policy Terms Favor the Insured

covered and noncovered perils “cause” a loss, a policyholder is generally entitled to coverage as long as the noncovered peril is not the predominant cause of the loss. If parties to an insurance contract (i.e., the insurer) want to override that principle, they must be clear about it, and Lexington was not.

Second, Lexington knew how to be clear about such issues. Another policy provision (an “anti-concurrent” clause) excluded certain perils and expressly stated that the exclusions applied regardless of any other concurrent cause. If Lexington wanted to similarly limit the coverage available under Additional Coverage 8, it could have done so.

Finally—“and most fundamentally”—insurance policies are to be construed against the insurer and in favor of the policyholder’s reasonable expectations. The Second Circuit observed that any reasonable person whose home had collapsed would expect the policy to provide coverage if the collapse was mostly due to a named peril. “Few would suppose that coverage would be denied merely because some other factor contributed to the event in a minimal, more attenuated way.” Because the trial court was wrong to give preference to the insurer’s interpretation, the jury verdict was vacated and the case was remanded for a new trial or other proceedings.

While the Fabozzis prevailed on this key issue of policy interpretation, their appeal was not a complete victory. The Second Circuit also addressed the burden of proof, an issue that turned on a determination of whether the policy provided “all-risk” or “named-perils” coverage. Everyone agreed that Coverage A of the Lexington policy covered all risks of physical loss, except for those perils specifically excluded. If the Fabozzis had made a claim under this all-risk portion of the policy, their only burden would

have been to prove the existence of the policy and their loss. Lexington would then have had the burden of proving that the loss was caused by a peril specifically excluded from coverage.

Even though Coverage A provided all-risk coverage, the language and structure of the policy showed that Additional Coverage 8 provided named-perils coverage for collapse. On its face, Additional Coverage 8 appeared to provide named-perils coverage, and the language was a direct parallel to named-perils provisions discussed in other cases. The Fabozzis argued that nothing in the policy suggested that Additional Coverage 8 changed the type of coverage. But the Second Circuit observed that such a change was “decisively suggested” by Lexington’s decision to exclude collapse from Coverage A, then draft Additional Coverage 8 as a named-perils provision. The Fabozzis thus had the burden of proving that the collapse was the result of a named peril.

The Second Circuit’s short summary order blazes no new trails in the world of insurance coverage. In fact, relying as it does on well-established legal principles, the order is likely to have little impact on an insurance coverage dispute unless that dispute involves the exact same policy language. However, the case acts as an important reminder of one of the basic tenets of policy interpretation in most jurisdictions around the country, including those generally unsympathetic to policyholders. Where a policy provision is susceptible to more than one reasonable interpretation—even where that provision appears simple and straightforward—the insurer that is responsible for drafting the policy is going to have to live with an unfavorable interpretation. ■ ■ ■



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PILLSBURY ADDS HIGH-PROFILE TEAM TO ITS LEADING NATIONAL INSURANCE RECOVERY PRACTICE

Arrival of Washington, DC, group led by Mark Plumer, David Klein and Alex Lathrop enhances the firm's recognized strength in representing corporate policyholders

Building on its momentum from an extremely successful 2015, Pillsbury's Insurance Recovery practice has announced the addition of a nationally renowned team of insurance litigators to the firm's Washington, DC, office. The group of seven—led by partners Mark Plumer, David Klein and Alex Lathrop—joins from Orrick, Herrington & Sutcliffe, where Plumer served as chair of Orrick's national insurance practice and Klein was deputy chair.

Plumer and his team act exclusively on behalf of corporate policyholders, regularly advising mining and energy companies, public utilities and other manufacturers, retailers and transportation companies on the full range of insurance issues and claims. They are consistently recognized by *Chambers USA* and other leading guides as one of the foremost practices in policyholder-side insurance law.

Pillsbury's Insurance Recovery group co-chairs Peter Gillon and Robert Wallan described the move as adding strength on strength.

"The arrival of this team represents an incredible infusion of talent for our Insurance Recovery practice," said Gillon. "Mark, David and their team are among the most sought-after policyholder-side insurance litigators in the United States. We are extremely pleased that they chose Pillsbury over many other options."

"Pillsbury represents a perfect fit for this team," added Plumer. "Beyond our alignment in representing policyholders,

the firm's ideal geographic footprint and impressive sector strengths, especially in energy, natural resources, environmental and crisis management, present tremendous opportunities to grow our practice and offer even more to clients."

Plumer, Klein and Lathrop are joined by four long-time colleagues, several of whom they have worked with for almost two decades. This includes two seasoned litigators in senior counsel Peri Mahaley and counsel Matthew Jeweler; attorney Bryan Coffey, who bears the Associate of Risk Management designation; and engineer and scientific advisor Kirt Suomela. Together, the team delivers a unique interdisciplinary approach that combines in-depth economic and scientific analysis with vast trial experience and extensive insurance business know-how.

"This is an important addition to one of Pillsbury's most successful practice areas," noted Firm Chair Jim Rishwain. "Our Insurance Recovery practice has experienced great success, including two outstanding jury trial results in 2015: a \$55 million win for Victaulic, and, most recently, a \$72 million jury verdict for Lion Oil. Now, with standout practitioners like Mark, David and Alex on board, the future is brighter than ever."

Pillsbury's Insurance Recovery & Advisory practice was one of the first insurance policyholder practices in the United States—dating back to the Great San Francisco Earthquake and Fire of 1906, when the firm helped business



Mark Plumer



David Klein



Alex Lathrop

owners recover from their insurers to rebuild the city. The group has recovered nearly \$15 billion of insurance proceeds for policyholder clients—including more than \$1 billion in each of 2013 and 2014 alone—and regularly helps them obtain broad insurance coverage to address the risks inherent in business today. The group has been lauded by *Chambers USA*, *Legal 500* and *Best Lawyers in America* and was recognized as one of *Law360's* Insurance Practice Groups of the Year for 2015. ■ ■ ■

POLICYHOLDER PULSE **INTRODUCING PILLSBURY'S** **INSURANCE RECOVERY &** **ADVISORY BLOG!**

The *Policyholder Pulse* blog provides news and insights on all aspects of insurance coverage law. Contributors are members of Pillsbury's award-winning Insurance Recovery & Advisory practice.

policyholderpulse.com

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**PILLSBURY'S
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WAS NAMED 2015'S
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