

Clifford Chance LLP v Indian Harbor Insurance Company SUPREME COURT OF NEW YORK 14 Misc. 3d 1209A; 836 N.Y.S.2d 484; 2006 N.Y. Misc. LEXIS 3880; 2006 NY Slip Op 52460U; 237 N.Y.L.J. 5 (2006)

Bernard J. Fried J.

In this action, plaintiffs Clifford Chance Limited Liability Partnership, and Clifford Chance US LLP (Clifford Chance), seek to challenge the determination of defendant Indian Harbor Insurance Company (Indian Harbor), to allocate 60% of the amount paid by Clifford Chance under a December 17, 2004 Comprehensive Settlement Agreement (the Settlement), and all attorney's fees paid by Clifford Chance in excess of the \$ 2 million dollars "retention" under a Management Liability & Company Reimbursement insurance policy (the Policy), to non-insured parties...Clifford Chance moves for summary judgment on the sole cause of action asserted in its complaint for breach of contract.

The parties do not dispute the underlying facts. Plaintiffs are New York limited liability companies engaged in the practice of law. Clifford Chance LLP has its principal place of business in London, England, and Clifford Chance US LLP is its United States affiliate. In or around July 2002, seventeen former partners of the California based law firm of Brobeck, Phleger & Harrison LLP (Brobeck), including Brobeck's one time former managing partner, Tower Snow, defected from Brobeck to join Clifford Chance in its new offices in San Francisco, Palo Alto, Los Angeles and San Diego, California.

Clifford Chance purchased the Policy from Indian Harbor on January 24, 2003, effective for a period of one year, from January 27, 2003 to January 27, 2004. On September 17, 2003, Brobeck's creditors filed a Chapter 7 involuntary bankruptcy petition in the United States Bankruptcy Court for the Northern District of California (the Bankruptcy Court). On or about October 7, 2003, a group of retired Brobeck partners commenced an action against Clifford Chance and Tower Snow, in the Superior Court of California, Alameda County... asserting one cause of action against Tower Snow for breach of fiduciary duty, and two causes of action against Clifford Chance for unfair competition and intentional interference with prospective business relationships ... According to the California state court complaint, Tower Snow, at the request of, and with substantial assistance from Clifford Chance, orchestrated the exodus of the sixteen other former Brobeck partners, knowing that the departure of so many partners from Brobeck would trigger automatic default provisions in loan agreements that Snow negotiated for Brobeck during the time that he was Brobeck's Managing Partner. Plaintiffs in the California state court action alleged that activation of the automatic default provisions caused Brobeck's creditors to file the involuntary bankruptcy petition, and that Brobeck's involuntary bankruptcy substantially interfered with Brobeck's agreement to pay them retirement benefits.

On the motion of Clifford Chance and Tower Snow, the California state court action was removed to the Bankruptcy Court, which rejected the first two attempts to settle the consolidated matters. Parties to the Settlement, which ultimately was approved by the Bankruptcy Court,

include the Bankruptcy Trustee, the plaintiffs in the California state court action, Clifford Chance, and the seventeen former Brobeck partners that defected to join Clifford Chance, including Tower Snow. In accordance with the Settlement, Clifford Chance paid \$ 5.5 million to the Bankruptcy Trustee in exchange for a general release of all claims that could be asserted against it, and against the defecting Brobeck partners by Brobeck. Clifford Chance paid an additional amount under the Settlement which, pursuant to stipulation, would not be disclosed, to the plaintiffs in the California state court action, in exchange for a release of all claims that were or could have been asserted in that action. Clifford Chance alleges that it also paid \$ 2,259,660 in legal fees and expenses in connection with the Settlement and California state court action.

Indian Harbor rejected Clifford Chance's claim for reimbursement of the full amount paid out under the Settlement, and for legal costs and fees paid in excess of the Retention. The parties attempted, unsuccessfully, to negotiate an allocation, and on May 2, 2005, Indian Harbor forwarded a check to Clifford Chance for 40% of the total paid under Settlement, asserting that its determination to limit its exposure to 40% of the Settlement amount was a favorable "allocation of the settlement... between covered and uncovered Loss." Indian Harbor also denied Clifford Chance's demand for payment of legal fees and expenses over the \$ 2 million retention, asserting that any fees charged in excess of the \$ 2 million retention were allocable to Tower Snow. In this action, Clifford Chance seeks to recoup the total amount paid out under the Settlement, which it alleges is within the \$ 15 million policy limits, and all costs and attorneys fees paid in excess of the \$ 2 million Policy retention.

It is well settled that the party claiming insurance coverage bears the burden of proving entitlement... In determining a dispute over insurance coverage, analysis must begin with the language of the Policy. Who is covered, and the extent of coverage is to be determined within the four corners of the insurance agreement... and the agreement must be construed in a way that gives fair meaning to all of the language employed by the parties, and leaves no provision without force and effect... In this case, Indian Harbor agreed to provide up to \$ 15 million in coverage, as defined under Section I of the Policy:

(A)...on behalf of the Insured Persons Loss resulting from a Claim first made against the Insured Persons during the Policy Period...for a Wrongful Act...except for Loss which the Company is permitted or required to pay on behalf of the Insured Person as indemnification....,

and, as is relevant to this case, and as amended under the Section XI Management Liability Corrections clause:

(C)...on behalf of the Company Loss resulting from any Claim first made against the Company during the Policy Period or, if applicable the Optional Extension Period for a Company Wrongful Act.

"Loss" is defined under section II (M) of the Policy to include:

...damages, judgments, settlements or other amounts...and Defense Expenses in excess of the Retention that the Insured is legally obligated to pay....

"Insured Persons" are defined under section II (J) of the Policy to include, in pertinent part:

(1)any past, present or future director, officer, or member of the Board of Managers of the Company and those persons serving in a functionally equivalent role for the Parent Company or any Subsidiary...

(2)any past, present or future employee of the Company to the extent any Claim is a Securities Claim.¹

Under New York Law, a party that is not named as an insured or as an additional insured, on the face of the policy, is not entitled to coverage ...and none of the parties argue that any of the seventeen former Brobeck partners released under the Settlement, who joined Clifford Chase prior to its purchase of the Policy were, "Insured Parties" or acting as Insured Parties when the alleged "Wrongful Acts" took place as required pursuant to Section II (S) of the Policy.

Insurers are entitled to allocate loss, or settlement costs, between covered and non-covered claims, or parties, where there is a factual basis for the allocation.. Costs and attorneys fees incurred in defense of an action, that fall within the definition of "Loss" under the Policy, are also subject to allocation.... There is little case law, in this jurisdiction, outlining the factors and methods to be employed in determining a proper allocation of loss between insured and non-insured parties to a settlement agreement. In the matter sub judice, however, Indian Harbor maintains that it is entitled to allocate most of the Loss, including additional legal expenses, to non-insured parties, pursuant to Section V (D) of the Policy which states, in pertinent part:

If both Loss covered by this Policy and Loss not covered by this Policy are incurred, either because a Claim made against the insured contains both covered and uncovered matters, or because a Claim is made against both the Insured and others not insured under this Policy, the insured and insurer will use their best efforts to determine a fair and appropriate allocation of Loss between that portion of Loss that is covered under the Policy and that portion of Loss that is not covered under this Policy. Additionally, the Insured and the Insurer agree that in determining a fair and appropriate allocation of Loss, the parties will take into account the relative legal and financial exposures of, and relative benefits obtained in connection with the defense and/or settlement of the Claim by the Insured and others.

Under New York law, provisions in an insurance policy, that are inserted by the insurer, and accepted by the insured, unless they are the product of adhesion or overreaching, will not be disregarded, and equitable considerations will not be used to extend coverage beyond its fair

¹Reference to "Securities Claims," although edited out of a number of other Policy provisions, does not appear to have been edited out from this provision.

intent and meaning...

Clifford Chance cites no New York precedent in support of the argument it raises in support of summary judgment, that Indian Harbor should be precluded from allocating a portion of the Settlement, and the additional legal expenses, to non-insured parties under the "larger settlement rule." The "larger settlement rule," is applied most frequently in the Seventh and Ninth Circuits to settlements entered into on behalf of a defendant corporation and its officers and directors, when the corporation is not named as an insured under the policy in dispute.... Since Corporations cannot act independently of persons, the "larger settlement rule" is used to prohibit insurers from allocating a portion of the settlement to the uninsured corporation, unless the settlement is made larger by the activities of uninsured parties, or increased by persons not named in the underlying lawsuit, whose actions may have contributed to the suit. By contrast, in this case, Clifford Chance is both an insured under the Policy, and a party to the underlying action or proceeding.

The insurance policies that were the subject of interpretation in the seminal case cited by plaintiffs, *Nordstrom, Inc. v Chubb & Son, Inc.* (54 F.3d 1424, *supra*), and in *Caterpillar, Inc. v Great American Ins. Co.* (62 F.3d at 960-62), did not contain allocation clauses, and the policy in *Owens Corning v National Union Fire Ins. Co. of Pittsburgh PA* (257 F.3d at 492), required the parties to negotiate an allocation, without reference to the method to be employed. By contrast, the Policy in this case contains bargained for language that "the parties will take into account the relative legal and financial exposures of, and relative benefits obtained in connection with the defense and/or settlement of the Claim by the Insured and others." This language specifically charts a course for application of what some courts and commentators have denominated the "relative exposure rule," as articulated by the Second Circuit in *Pepsico, Inc. v Continental Casualty Co.* (640 F. Supp. at 662 [applying New York law]... It is not necessary, therefore, to join in the debate engaged in by the Circuit Courts on the proper application of the larger settlement rule, as it is inapplicable to this case on either the facts or the law.

Determining relative exposure and weighing the relative benefits of the Settlement and costs incurred requires a fact based analysis... Whether Indian Harbor properly allocated 60% of the Settlement and all additional costs to non-insured parties, therefore, raises triable issues of fact that cannot be determined from the papers submitted in connection with the motion for summary judgment. No other arguments or evidence are offered by Clifford Chance to demonstrate a right to judgment as a matter of law...

Accordingly, for the reasons stated, it is: ORDERED, that plaintiffs' motion for summary judgment is denied.