CHANCES ARE . . . A FORTUITY CASE STUDY

A POLICYHOLDER’S PERSPECTIVE

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A. Introduction


2. When presented with substantial claims arising from a catastrophic event, insurers may contend that the event was caused by the insured’s failure to adhere to industry standards or its own procedures, and that these failures render non-fortuitous all loss resulting from the event, including property damage and business interruption.

3. Under New York law, the test for fortuity, in circumstances in which the conduct of the insured is alleged to be the cause of the loss, is whether the insured intended the loss, or whether the insured acted, or failed to act, with knowledge that the loss was substantially certain to result (sometimes expressed as knowing that the loss “would flow directly and immediately from the insured’s intentional act”). We will discuss whether certain hypothetical scenarios present these circumstances.

B. The Meaning of Fortuity Under New York Law

4. Under New York law, a loss is fortuitous unless the insured intended the loss, or unless the insured acted, or failed to act, with knowledge that the loss was substantially certain to result.

5. In National Union Fire Ins. Co. of Pittsburgh, PA v. Stroh Cos., 265 F.3d 97 (2d Cir. 2001), the Second Circuit, applying New York law, explained the scope of the “fortuity” and “known loss” doctrines that exist independently of the language in insurance policies. Id. at 106.

5.1. The Second Circuit held that a loss is “fortuitous” unless the insured either intended the loss or knew that the loss would flow directly and immediately from the insured’s intentional acts. National Union, 265 F.3d at 111. The insurer
argued that the loss at issue was not “fortuitous” because it was not “beyond the control of either party” within the meaning of N.Y. Ins. Law § 1101(a)(2). In rejecting the insurer’s argument and interpreting Section 1101(a)(2), the Second Circuit held that the loss was fortuitous unless the insured had knowledge that “damages . . . [would] ‘flow directly and immediately from [the insured’s] intentional act’ and thus could not ‘be considered ‘accidental’ or fortuitous.” *Id.* (citing *City of Johnstown v. Bankers Standard Ins. Co.*, 877 F.2d 1146, 1150 (2d Cir. 1989)).

5.2. In the cited passage from *City of Johnstown*, the Second Circuit held that in defining what constitutes “accidental” loss:

the distinction is drawn between damages which flow directly and immediately from an intended act, thereby precluding coverage, and damages which accidentally arise out of a chain of unintended though expected or foreseeable events that occurred after an intentional act . . . . *It is not enough that an insured was warned that damages might ensue from its actions, or that, once warned, an insured decided to take a calculated risk and proceed as before . . .* Recovery will only be barred if the insured intended the damages . . . or if it can be said that the damages were, in a broader sense, ‘intended’ by the insured because the insured knew that the damages would flow directly and immediately from its intentional act . . . .

877 F.2d at 1150 (emphasis added; citations omitted).

5.3. The Second Circuit also held that under one “variation on the fortuity theme” – the so-called “known loss” defense – a loss is fortuitous unless “the inevitability of [the] loss was . . . known to the insured before coverage took effect . . . .” *National Union*, 265 F.3d at 109 (emphasis added).

5.4. The Second Circuit rejected the insurer’s argument “that the fortuity doctrine bars coverage not only for known losses, but for *likely* losses, i.e., known enhanced risks. We have expressly rejected the existence of such a ‘known risk’ doctrine under New York law.” *Id.* at 108 (citing *City of Johnstown*, 877 F.2d at 1152-1153 (emphasis in original).
6. This definition of fortuitous loss is consistent with decisions of the New York Court of Appeals.

6.1. In *Consolidated Edison Co. v. Allstate Ins. Co.*, 774 N.E.2d 687 (N.Y. 2002), the New York Court of Appeals held that “[i]nsurance policies generally require ‘fortuity’ and thus implicitly exclude coverage for intended or expected harms.” *Id.* at 692.

6.2. In an earlier decision, the Court of Appeals defined “intended or expected” as simply meaning “intended.” *See ¶ 6.4, infra.* And by “intended,” that earlier decision meant that the insured either intended the loss or knew that the loss would occur as a direct and immediate result of the insured’s intentional acts.

6.3. *Consolidated Edison* involved policies of general liability insurance that did not, as such policies normally do, expressly provide that there was no coverage for harms intended or expected by the insured. Instead, the policies simply provided either that there was coverage for an “accident” or coverage for an “occurrence.” *See Consolidated Edison*, 774 N.E.2d at 690-91 (“[E]ach of the policies speaks of damages caused by or arising from either an ‘accident’ or an ‘occurrence.’ None of the policies contains an exclusion for intended or expected harm.”). Nonetheless, the Court of Appeals held that the policies must therefore be read as though they expressly barred coverage for “intended or expected” harms. *Consolidated Edison*, 774 N.E.2d at 692.

6.4. Nine years earlier, the Court of Appeals had held that where general liability policies expressly provide that “[f]or an occurrence to be covered . . . the injury must be unexpected and unintentional, [w]e have read such policy terms narrowly, barring recovery only when the insured intended the damages.” *Continental Cas. Co. v. Rapid-American Corp.*, 609 N.E.2d 506, 510 (N.Y. 1993). *Continental Casualty* specifically cited *City of Johnstown, supra*, to illustrate what kinds of losses are covered. *Id.* at 510 (citing *City of Johnstown*, 877 F.2d at 1150).
7. In fact, under New York law, because the question is whether the insured had knowledge that its actions would cause damage, even damage from an intentional or willful act is “fortuitous” if the insured did not intend the harm or know it was substantially certain to occur.

7.1. In Continental Casualty, supra, 609 N.E.2d at 510, the New York Court of Appeals held that “[r]esulting damage can be unintended even though the act leading to the damage was intentional . . . .” (citations omitted).

7.2. In Allegany Co-op Ins. Co. v. Kohorst, 678 N.Y.S.2d 424 (N.Y. App. Div. 1998), an insured intentionally set fire to a property that he owned and was convicted of attempted arson. Id. at 425. Nonetheless, the court held that in an action brought by a person injured as a result of the fire, the insured could still be covered under his policy of liability insurance, which required that the injury be “accidental,” because the insured “did not intend to hurt [the third party] when he intentionally set the fire” and “accidental results may flow from intentional acts.” Id.

8. Damages resulting from negligence are, of course, fortuitous. See, e.g., David Danzeisen Realty, supra, 565 N.Y.S.2d at 224 (“Mere negligence of an insured is not a defense to coverage under an ‘all risk’ policy.”) (citations omitted). In David Danzeisen Realty, where the insured lacked the expertise to repair its own roof and hired a roofing company to do the repairs, the court held that the subsequent sliding of the roof, which the insurer alleged was caused by the inadequacy of the repairs, constituted negligence and was “to a substantial extent beyond [the insured’s] control” and therefore fortuitous. 565 N.Y.S.2d at 224.

C. Certainty, “Control” and New York Insurance Code Section 1101

9. Some courts applying New York law have relied on the New York Insurance Law in determining whether losses are fortuitous. See, e.g., National Union, supra; David Danzeisen Realty, supra; Petroterminal De Panama, S.A. v. QBE Marine & Specialty Syndicate 1036, No. 14-8614; 2017 U.S. Dist. LEXIS 7638 (S.D.N.Y. Jan. 19, 2017). Section 1101(a) of that statute defines a “fortuitous event” as “any occurrence or failure
to occur which is, or is assumed by the parties to be, to a substantial extent beyond the control of either party.” See N.Y. INS. LAW § 1101(a).

10. Professor Edwin Patterson, one of the drafters of that statute, wrote a treatise on insurance law. Patterson discussed fortuity and the concept of the insured’s “control” in these terms:

_The Designing Act of the Insured_. An insurance enterprise would soon fail if the insurer were liable for losses designedly caused by the persons insured and if those persons should take advantage of the opportunity this offered to impose liability on the insurer. . . Hence it is implied in every insurance contract that the insured event is a fortuitous one, _i.e._, one not designedly brought about by the insured. . . But to say that the insurer is not liable if the happening of the insured event was within the control of the insured would be erroneous or at least likely to mislead. Unless control means only designedly causing the insured event, a meaning narrower than the ordinary sense of the word, it includes a great many situations in which the insurer is undoubtedly liable. Thus, a defective chimney is “within the control” of the insured, since it can be repaired; yet fires due to defective flues are covered by the ordinary fire policy. Even if control is narrowed to include only situations of which the insured has knowledge, it is still too broad, since an insured who carelessly put off repairing a known defect in his chimney would not thereby be barred from recovering on his fire-insurance policy.

Edwin W. Patterson, ESSENTIALS OF INSURANCE LAW 257-58 (2d ed. 1957).

11. Thus, (and even accepting for purposes of argument that Section 1101 applies to questions of coverage as opposed to licensure), the analysis of fortuity is not properly centered around the degree of control that an insured exercises over the risk, and reliance on Section 1101 to support such an argument is misplaced. Non-fortuity requires certainty, and neither the insured’s control of risk, nor even courting of risk, is sufficient to show non-fortuity.

12. The fortuity doctrine does not bar coverage for risks – even very sizable risks – about which the insured knew.
12.1. See National Union, supra, 265 F.3d at 108 (under New York law, “the fortuity
doctrine [does not] bar[] coverage . . . for likely losses, i.e., known enhanced
risks.”) (emphasis in original); id. (“Even if the risk [of the loss that occurred] was
known [by the insured], and known to be high,” when the coverage at issue was
added to the policy, that would not bar coverage).

12.2. See Wal-Mart Stores, Inc. v. United States Fid. & Guar. Co., No. 06-4417/2002,
(a rockslide, “while a known risk at the time the [all-risks] policies took effect,
was not ‘substantially certain to occur,’” and was therefore fortuitous, even
though (a) it involved a sixty-ton boulder falling from a hillside above the
insured’s store, (b) there had been numerous rockslides before the inception of
coverage, including another sixty-ton boulder falling on the store, and (c) the
insured was aware of the geologic instability of the hillside) (citing National
Union, supra).

13. A loss resulting from the taking of a “calculated risk” is “accidental” and thus fortuitous.
See Continental Casualty, supra, 609 N.E.2d at 510 (“A person may engage in behavior
that involves a calculated risk without expecting that an accident will occur – in fact,
people often seek insurance for just such circumstances . . . .”) (citing, inter alia, City of
Johnstown, supra).

D. The Burden of Proof On The Issue Of Fortuity

14. Under New York law, the insured under an all-risks policy has a “relatively light” burden
of showing that its loss was fortuitous. Petroterminal De Panama, supra, 2017 U.S. Dist.
LEXIS 7638 (quoting Int’l Multifoods Corp. v. Commercial Union Ins. Co., 309 F.3d 76,
83 (2d Cir. 2002)). Once the insured meets that burden, the burden then shifts to the
insurer to prove otherwise.

15. In National Union, supra, the Second Circuit held that “[t]he initial burden of showing
that the loss in question was fortuitous – here meaning that the inevitability of such loss
was not known to the insured before coverage took effect – is on the insured party . . .
Once that burden is met, the insurer must come forward with evidence showing that ‘an exception to coverage applies,’ including exceptions based on the non-fortuity or known loss doctrines.” *National Union*, 265 F.3d at 109 (citations omitted).

16. In *Union Carbide Corp. v. Affiliated FM Ins. Co.*, 955 N.Y.S.2d 572, 757 (N.Y. App. Div. 2012), a New York appellate court held that where the policy covered damages resulting from an “occurrence,” and also contained an express exclusion for damages intended by the insured, the insured met its burden of establishing coverage by providing evidence that it did not intend to harm third parties. Once the insured did that, “the burden shifted to defendant [insurer]s to show that, pursuant to the policy’s exclusion, [the insured] intended the damages.” *Id.*

17. The insured’s initial burden of proof is also “fairly light” in that the insured “does not have to prove the precise cause of the loss.” *Fleet Business Credit, L.L.C. v. Global Aerospace Underwriting*, 812 F. Supp. 2d 342, 354 (S.D.N.Y. 2011).

E. **Conclusion**

18. The relevant standard under New law is whether the evidence presented shows that, at the time of the catastrophic event, the insured intended the event, or knew that the event was substantially certain to occur. If the evidence does not meet this standard, under New York law, the loss was fortuitous.

18.1. If the insured believed that it was operating in a manner consistent with relevant industry standards relevant to the prevention of the root cause of the event, the loss is fortuitous.

18.2. Even accepting for the sake of argument that, with the benefit of hindsight, an insured could have discovered the root cause of, and thus prevented, the event, that does not lead to the conclusion that the insured intended the event to occur, or knew that it was substantially certain to occur, which is the standard under New York law.