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# New York’s Treatment of “Arising Out Of” Insurance Exclusions

*A discussion of New York’s extremely insured friendly reading of “arising out of” language in insurance agreements.*

By **Evan Bolla**

In this period of economic uncertainty, with seemingly new sources of significant widespread losses appearing weekly, individuals and businesses find themselves increasingly looking to available insurance for relief. Insurance carriers have received more than 60 million claims since March, and previous weekly claim filing records have been surpassed time and time again. With an unprecedented number of claims has come an unprecedented number of coverage denials—many of which are based on exclusions in policies.

For far too many, the receipt of a denial letter that reasonably describes why insurance is not available is the end of the road. However, the burden that insurance carriers have to meet in denying coverage, particularly when they are relying on an exclusion, is incredibly high. Applying this high burden, New York courts have established that certain common insurance phrases, such as “arising out of,” have precise legal meanings which, when applied, can negate a carrier’s seemingly reasonable basis to disclaim coverage.

Under New York law, courts initially address the right to coverage under an insurance contract as they would any other contract, and unambiguous terms are given their plain and ordinary meaning to assure that each portion of the policy is given force and effect. *Lend Lease (US) Const. LMB Inc. v Zurich Am. Ins. Co.*, 28 N.Y.3d 675, 681–82 (2017); I*n re Viking Pump, Inc.*, 27 N.Y.3d 244, 257 (2016). However, where the policy “may be reasonably interpreted in two conflicting manners, its terms are ambiguous, and “any ambiguity must be construed in favor of the insured and against the insurer.” *Lend Lease (US) Constr. LMB Inc.*, 28 N.Y.3d at 682.
If a carrier is looking to rely on an exclusion as a basis to deny coverage, however, the dynamic shifts. An exclusion to coverage must be clear through unmistakable language. *Pioneer Tower Owners Ass’n v. State Farm Fire & Cas. Co.*, 12 N.Y.3d 302, 307 (2009). Any such exclusions must be specific and are “to be accorded a strict and narrow construction.” Id. In sum, there can be no other reasonable interpretation of the exclusion that would allow for coverage.

While exclusions vary by policy, they often use similar phraseology. One commonly used phrase is “arising out of,” which typically precedes terms such as contracts, business relationships, pollutants, or employment, among others. It is common for both carriers and insureds to equate “arising out of” with “generally connected to,” and in fact, many states apply this approach which assigns “arising out of” a broad meaning. *Meadowbrook, Inc. v. Tower Ins. Co., Inc.*, 559 N.W.2d

411, 419 (Minn. 1997) (the words "arising out of" in an insurance policy means "causally connected with" and not "proximately caused by.") The U.S. Court of Appeals for the Tenth Circuit has commented that the "general consensus" is that the phrase is equivalent to "originating from" or "growing out of" or "flowing from" or "done in connection with." *Fed. Ins. Co. v. Tri-State Ins. Co.*, 157 F.3d 800, 804 (10th Cir. 1998).

However, in *Mount Vernon Fire Insurance Co. v. Creative Housing Ltd.*, the New York Court of Appeals explained that "the phrases 'based on' and 'arising out of,' when used in insurance policy exclusion clauses, are…legally indistinguishable." 88 N.Y.2d 347, 351-353 (1996). And, while New York Courts have continued to cite broader language similar to that used by the Tenth Circuit in describing "arising out of" language, New York courts have in practice applied a stringent "but-for" test that applies the "based on" definition and examines the elements of each alleged cause of action. *Country-Wide Ins. Co. v. Excelsior Ins. Co.*, 46 N.Y.S.3d 96, 98 (1st Dept. 2017).

In other words, where the plaintiff in an underlying action or proceeding alleges the existence of facts falling within such an exclusion, an insurer must show that those allegations that are within the exclusion are necessary for each of the causes of action or it cannot exclude coverage. *Scottsdale Indemn. Co. v. Beckerman*, 992 N.Y.S.2d 117, 121 (2d Dept. 2014).

In *Great American Insurance Company v. Houlihan Lawrence, Inc.*, the Southern District of New York recently applied New York law in examining two "arising out of" exclusions to address whether an insured was entitled to a defense of underlying claims that he engaged in real estate fraud by inducing individuals to enter into duel agent transactions. 449 F.Supp.3d 354, 359 (S.D.N.Y. 2020). The first exclusion the court examined provided that the policy did "not apply to any Claim…based on or arising out of any dishonest, intentionally wrongful, fraudulent, criminal[,] or malicious act or omission by an Insured." Id.

The court held that while the underlying complaint alleged primarily intentional acts that fell within the exclusion, it was required to liberally construe the underlying allegations when determining whether the insured had a duty to defend. Such construction required the court to assume the pleadings contained allegations of negligence whenever possible, even when negligence was not explicitly pled. Id.

As the court found that certain of the alleged breaches of fiduciary duty could be established through negligent acts alone, it determined the exclusion did not apply as there could be an underlying adverse finding against the insured based on negligence rather than the excluded conduct.

The second provision that was examined by the Great American Insurance court provided that the policy did not apply to "any claim…based on or arising out of…any disputes involving an Insured's fees, commissions[,] or charges." Id. at 370. The court likewise rejected the application of this exclusion—despite the complaint's primary focus on the payment of commissions. It found the exclusion did not apply, as some of the underlying plaintiffs' claims under New York General Business Law only required wrongful conduct and did not require economic damages. In other words, coverage was required, as the proper analysis was not that plaintiffs' claims would not exist

but for the commissions, but that "[p]laintiffs' claims would not exist but for the alleged misrepresentations and omissions made by [d]efendant." Id.

In *National Union Fire Insurance Company of Pittsburgh, PA v. The Burlington Insurance Company*, a case with clear applicability to the current COVID-19 crisis, the issue before the New York Supreme Court was whether claims concerning injuries suffered during post-September 11 cleanup work were covered under the primary policy or whether a provision which excluded coverage for "[a]ny loss, cost or expense arising out of any [pollutant]" barred coverage. 2018 N.Y. Slip Op. 30741(U), 3, 2018 WL 1988852, at *2 (N.Y. Sup. April 27, 2018).

The primary insured argued that that "[a]lthough the injuries may be alleged to have been caused by a lack of proper safety equipment…, none of the workplace safety issues or injuries would exist but for the polluted environment." Id. at *7. The *Nat. Union Fire Ins. Co. of Pittsburgh, PA* court rejected this argument and found that the insurer must demonstrate that the allegations in the complaint cast the pleading solely within the policy exclusion and that here the failure to provide a safe workplace was an independent wrong which did not trigger the pollutant exclusion.

In a time of increased insurance claims and denials, it is important for insureds, and their attorneys, to ensure they are maximizing coverage by fully analyzing any insurance carrier's disclaimer, as they may be surprised where a basis to fight a denial of coverage can arise.

**Evan W. Bolla is a partner and general counsel for Harris St. Laurent in New York. His practice focuses on insurance recovery, executive employment, and other commercial matters.**

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