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NEWSLETTER

New York Court Holds Insured v. Insured Exclusion Bars Coverage Only for Portion of Suit Brought by Individual Insureds

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A New York State trial court has held that an insured v. insured exclusion in a not-for-profit policy barred coverage only for the portion of a suit that was brought by "Individual Insureds," ruling that there was coverage for the remainder of the suit brought on behalf of private individuals who were not insureds. *Trustees of Princeton Univ. v. Nat'l Union Fire Ins. Co.*, 2007 WL 1063870 (N.Y. Sup. Ct. Apr. 10, 2007).

The insurer issued a not-for-profit policy to a university. The policy provided coverage for "Loss arising from a Claim first made against the Organization during the Policy Period." The policy contained an insured v. insured exclusion barring coverage for a "Claim made against an Insured . . . which is brought by or on behalf of the Organization against any Individual Insured. . . ." The policy contained a $15 million aggregate limit of liability. An endorsement provided that a $5 million sub-limit of liability would be available for the cost of defending an action "seeking injunctive or equitable relief."

The underlying action involved one of the university's privately funded foundations. The foundation was a "subsidiary" of the "Organization" under the terms of the policy, and the foundation's trustees were "Individual Insureds." A minority of the foundation's trustees, along with the private, non-insured individuals funding the foundation, alleged that the majority of the foundation's trustees had misappropriated the foundation's funds for improper purposes. The minority trustees and private individuals brought suit, seeking equitable relief and over $100 million in damages.

The court first addressed whether the insured v. insured exclusion barred coverage. The university argued that the exclusion should have no application because the purpose of the exclusion is to bar coverage for collusive suits. The court disagreed, stating that the exclusion applied according to its terms. In so ruling, however, the court stated that "the exclusion must be construed narrowly and strictly, and thus it only applies to the claims explicitly brought on behalf of the [foundation] against individual insureds." The court ruled that the exclusion applied here to bar coverage only for the two counts brought derivatively on behalf of the foundation and did not apply to the counts brought directly by the private individuals who were not insureds.

The court addressed allocation. It explained that because the university had already exceeded $15 million in defense costs, apportionment among covered and uncovered "claims" was not necessary because it was "unlikely to affect the insurer's ultimate financial obligation."

The insurer also sought to limit defense costs to $5 million based on the equitable sub-limit in the policy. The provision that created the sub-limit, however, stated that "for Claims that involve multiple allegations, the $5,000,000 sublimit will only apply to the portion of the Claim which is related to the equitable or injunctive relief allegations." The court ruled that not all of the allegations were subject to the sub-limit, but the insurer could seek apportionment for those that were so limited.

Finally, the court addressed the university's bad faith allegations. The university first argued that the insurer owed a fiduciary duty to it and that duty had been breached. The court rejected this argument, explaining that the insurance relationship is a contractual relationship unless the insurer has induced reliance, and such proof of reliance had not been submitted. The court also held that because the insurer had adopted a "reasonable" coverage position, damages for bad faith were not recoverable. Finally, the court addressed the university's allegations that the insurer's marketing materials concerning the scope of the insured v. insured exclusion violated New Jersey's Consumer Fraud Act. The court rejected this argument, stating that the statute was inapplicable because the university could not establish that it had suffered an "ascertainable loss" and, furthermore, the alleged advertisements were issued after the inception of the policy.