

Appellate Court Upholds Allocation of Loss Based on "Relative Exposure" Standard

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The New York Supreme Court Appellate Division has affirmed a trial court's ruling that the terms of a management liability policy allowed the insurer to allocate loss between insured and non-insured parties through the application of the "relative exposure" standard. *Clifford Chance Ltd. Liab. P'ship v. Indian Harbor Ins. Co.*, 2007 WL 1704202 (N.Y. App. Div. June 14, 2007).

The insurer issued a management liability policy to a law firm. The policy contained an allocation provision requiring the parties to "use their best efforts" to allocate loss where a claim is made against both parties insured under the policy and parties who are not insured. The allocation provision stated 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."

After 17 partners of another firm, including the second firm's former managing partner, left the second firm to join the policyholder firm, both the policyholder firm and the defecting partners became embroiled in litigation concerning the defection of the partners and the collapse of the second firm. The underlying litigation settled, and the insured law firm sought coverage for the entire amount of the settlement. The insurer maintained that an allocation of loss was necessary since the 17 defecting partners were not being sued for wrongful acts taken while they were at the policyholder firm. The insurer therefore forwarded a check for 40 percent of the settlement amount to the policyholder firm based on the insurer's assessment of the proper allocation.

The trial court denied the policyholder firm's motion for summary judgment on the issue of allocation, holding that "[i]nsurers 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." *Clifford Chance Ltd. Liab. P'ship v. Indian Harbor Ins. Co.*, 2006 WL 3821841 (N.Y. Sup. Ct. Dec. 27, 2006). (Summarized in the February 2007 issue of Executive Summary.) The trial court reasoned that the policy language specifically supported application of the "relative exposure rule" articulated in *PepsiCo, Inc. v. Continental Casualty Co.*, 640 F. Supp. 656 (S.D.N.Y. 1986).

In its summary opinion affirming the trial court's decision, the Appellate Division held that "[i]n light of the

clear allocation provision in the policy, which had the effect of a partial exclusion, and despite the joint and several liability of the insured and uninsured defendants in the underlying litigation, the insurer is only required to pay a portion of its insured's claim for reimbursement of the settlement amount based on a determination of the insured's and the uninsured's relative exposures in the litigation and the benefits received from the settlement."