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Insurance Alert

Second Circuit finds that New York notice requirements inapplicable to disclaimers based on coverage grant of the policy

Overview

Where an insurer's disclaimer of coverage is not based on a policy exclusion, but rather on the basis that no coverage exists in the first instance, must the carrier still comply with the stringent notice requirements of New York Insurance Law § 3420(d)(2)? No, said the Second Circuit in its recent ruling in *NGM Insurance Company v. Blakely Pumping, Inc.*

Background

The issue in *NGM Insurance Company v. Blakely Pumping, Inc.* was whether coverage was available under a business owners' liability policy issued to Blakely Pumping. Brian Blakely, an officer and employee of Blakely Pumping, was involved in an automobile accident while operating his own vehicle in the course of his work for Blakely Pumping. Blakely Pumping's insurer, NGM Insurance Company, denied coverage for the personal injury claim brought against Mr. Blakely on the basis of the policy's automobile exclusion.

The claimant subsequently advised NGM that the policy issued to Blakely Pumping contained a Hired or Non-Owned Auto endorsement. NGM responded by disclaiming coverage again, reasoning that since Brian Blakely was an executive officer of Blakely Pumping, his vehicle was neither a Hired nor Non-Owned Auto as defined in the endorsement.

District Court applies § 3420(d)(2) notice requirement

NGM commenced an action seeking a declaratory judgment that it was under no obligation to defend or indemnify Blakely Pumping. The District Court held that, since Blakely Pumping had borrowed an automobile owned by one of its officers, the accident was not covered under the terms of the policy as modified by the Hired or Non-Owned Auto endorsement. The District Court also concluded that, since the Hired or Non-Owned Auto endorsement "generally covered auto accidents," the definitions of the endorsement constituted exclusions to that general coverage. Thus, pursuant to New York Insurance Law § 3420(d)(2), NGM was required to provide written notice of this basis for disclaiming coverage and, because it originally disclaimed coverage pursuant to the policy's exclusion for automobiles, it waived its right to disclaim coverage on other grounds. Accordingly, the District Court found that NGM's subsequent notice of disclaimer was ineffective, that it could now not rely on those exclusions, and that it had a duty to defend and indemnify Blakely Pumping in the underlying matter.

Second Circuit puts the case in "reverse"

On appeal, the Second Circuit reversed. It held that the insurance policy in question did not cover the officer's automobile under any circumstances and, therefore, the District Court erred in finding that New York Insurance Law § 3420(d)(2) required NGM to timely disclaim coverage on the language of the endorsement. In so ruling, the court relied heavily on the New York Court of Appeals decision in *Zappone v. Home Insurance Co.*, 55 N.Y.2d 131 (1982). Paraphrasing *Zappone*, the Second Circuit noted the New York high court interpreted § 3420(d)(2) as requiring notice only for a "denial of liability predicated upon an exclusion set forth in a policy which, without the exclusion, would provide coverage for the liability in question." *Blakely Pumping* at 6 (quoting *Zappone* at 134). In other words, compliance with New York Insurance Law § 3420(d)(2) is not required where coverage never existed in the first place.

Applying that principle here, the Second Circuit held that, since Blakely's vehicle could never have been covered, there was no coverage "by reason of lack of inclusion." Thus, compliance with New York Insurance Law § 3420(d)(2) was not required because this was not an initially covered claim that was now the subject of an exclusion. *Blakely Pumping* at 7 (quoting *Zappone* at 137). Accordingly, the Second Circuit held that NGM's subsequent disclaimer did not violate New York Insurance Law § 3420(d)(2) and, thus, was effective.

Comment

The Second Circuit's *Blakely Pumping* decision reads *Zappone* to limit the applicability of § 3420(d)(2) to disclaimers based on policy exclusions. Where, as here, a disclaimer is based on the absence of any coverage in the first instance—what the court calls a "lack of inclusion"—it reads *Zappone* to say that the § 3420(d)(2) notice requirements have no applicability. However, while the Federal Court decision is instructive, it is not a definitive statement of New York law. We anticipate that it is not the last word on the subject in New York State. Whether other New York courts—including the Court of Appeals—agree with the Second Circuit's interpretation of *Zappone* must await subsequent decisions. Accordingly, until this issue is *definitively* resolved in New York, insurers issuing disclaimers should consider complying with the notice requirements of §3420(d)(2)—even where the denial is based on the absence of coverage in the first instance.

Wilson Elser's Insurance Practice Group will continue to monitor subsequent decisions interpreting § 3420(d)(2) and will make any noteworthy rulings on this important topic the subject of future Insurance Practice Alerts. To view a copy of the Second Circuit's *Blakely Pumping* decision, click here.

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