

SUPERIOR COURT OF THE STATE OF CALIFORNIA
FOR THE COUNTY OF LOS ANGELES

ORIGINAL FILED

JUL 25 2010

SUNOCO, INC., ET AL)
Plaintiffs)
vs)
AMERICAN INTERNATIONAL)
SPECIALTY LINES, ETC.,)
ET AL)
Defendants)
_____)

**LOS ANGELES
SUPERIOR COURT**

CASE NO. BC330538

COURT'S RULING ON LEGAL ISSUES 1, 2 AND 3 HEARD ON JULY 22,
2010

Legal Issue #1

The parties stipulated to have this Court address the following legal issue in order to facilitate orderly discovery and mediation:

Did Sunoco provide timely notice of a batch occurrence under Section V(d) of the Helios Policy.

See Notebook 1, Exhibit 12, page 2, lines 20-21.

1. Applicable Facts

The parties stipulate to the following facts:

Helios issued policy NO. HEL-1028(98) to Sunoco, for the policy period December 31, 1998 to December 31, 2000, with a retroactive date of November 1, 1991 for all operations except product liability claims (for which there is an April 1, 1986 retroactive date).

The Helios policy is based on the XL-003 Bermuda Form and has a number of features.¹ For the purposes of this legal issue, the relevant provisions revolve around (1) the definition of "occurrence", (2) the definition of "integrated occurrence" and (3) Section V(d), "Notice of Occurrence and Claim."

The Helios policy defines occurrence as follows:

The term "occurrence" means:

- (i) an event or a continuous, intermittent or repeated exposure to conditions which causes, allegedly causes or is deemed to cause personal injury or property damage or gives rise to advertising liability, which event or conditions, commence at or subsequent to the Inception Date (or, if applicable, the Retroactive Coverage Date) and prior to the expiration of Coverage A, or
- (ii) use of the Insured's product which causes, allegedly causes or is deemed to cause personal injury or property damage taking place both prior to the expiration of Coverage A and at or

¹ The Sunoco excess liability policy wordings were written on two Bermuda market forms commonly identified as the XS-003 and XS-004 forms. Thus, the Helios policy (fully reinsured by MRAM) and the quota share AISLIC policy, among others, were written on the SL-003 form; higher level excess policies written by Zurich and XL, among others, employed the XL-004 form.

subsequent to the Inception Date (or, if applicable, the Retroactive Coverage Date) . . .

The Helios policy also defines "Occurrence Integration" as follows:

(f) Occurrence Integration

Where a series of and/or several actual or alleged losses, injuries, damages or liabilities occur which are attributable directly, indirectly or allegedly to the same actual or alleged event, condition, cause, defect or hazard or failure to warn of such, all such actual or alleged losses, injuries, damages or liabilities shall be added together and treated as one Occurrence irrespective of the period or area over which the actual or alleged losses, injuries, damages or liabilities occur or the number of such actual or alleged losses, injuries, damages or liabilities, [s]o far as losses, injuries, damages or liabilities resulting or alleged to result from the design, formulation, manufacture, distribution, use, operation, maintenance or repair or an Insured's product or the failure to warn as to the use, operation or maintenance of an Insured's product, the term "the same actual or alleged event, condition, cause, defect or hazard or failure to warn of such" means any such design, formulation, manufacture, distribution, use, operation, maintenance, repair or failure to warn, as the case may be, as to which such losses, injuries or damages are directly, indirectly or allegedly attributable.

Section (d) of Article V (Conditions) of the Helios policy states:

If any claims is made against any Insured likely to involve this Policy, the Named Insured shall, as a condition precedent to the rights of any Insured under the Policy, give written notice thereof to Underwriters as soon as practicable and shall promptly forward to Underwriters copies of any written claim, demand, notice, summons, complaint or other process received by the Insured or its representatives or agents. Failure to provide such written notice as

required herein shall result in a forfeiture of any rights to coverage hereunder.

Where applicable, notice of occurrence or claim shall identify an occurrence in respect of actual or alleged personal injury and/or property damage arising from two or more units of a product as a "batch occurrence." A batch occurrence exists where actual or alleged personal injury and/or property damage arising out of two or more units of a product is attributable directly, indirectly or allegedly to the same event, condition, cause, defect or hazard or failure to warn of such but only if such is identified hereunder as a "batch occurrence." With respect to any batch occurrence, (1) all actual or alleged personal injury and/or property damage attributable to the same actual or alleged event, condition, cause, defect or hazard or failure to warn of such shall be added together and treated as one occurrence irrespective of the period or area over which the actual or alleged injuries or damages occur or the number of such actual or alleged injuries or damages, and (2) the aggregate limit, the per occurrence limit and the terms, conditions and exclusions of coverage shall be determined under the annual period of the Policy as in effect at the time such notice of such batch occurrence is first given ("batch policy period") notwithstanding that prior notice may have been given with respect to such occurrence other than as a batch occurrence; provided, however, that if such prior notice was given, then the ultimate net loss with respect thereto shall be included with the ultimate net loss in respect of such batch occurrence for all purposes, and appropriate adjustments shall be made in the prior annual period of such notice and in the batch policy period to transfer any loss payments and erosion of limits from the former to the latter. Notwithstanding Sections (e) and (f) of Article III, if an occurrence arising out of a unit of a product is not identified in the notice thereof as a "batch occurrence," then, subject to the preceding sentence, actual or alleged personal injury and/or property damage in connection therewith shall be deemed to arise

from a separate occurrence from which actual or alleged personal injury and/or property damage arises from any other unit of such product.

Defendant MRAM reinsures 100% of the Helios Policy limits. The MRAM reinsurance certificate provides, in part, as follows:

The Reinsurer agrees to indemnify the Company against losses or damages which the Company is legally obligated to pay with respect to which Insurance is afforded during the term of this Certificate under the policy reinsured, subject to the reinsurance limits and coverage shown in the Declarations. The Reinsurer shall not indemnify the Company for liability beyond circumscribed policy provisions, including but not limited to punitive, exemplary, consequential or compensatory damages resulting from an action of an insured or assignee against the Company. . .

In addition, in paragraph 4 of the General Conditions, MRAM is entitled to be advised "promptly of any claim and any subsequent developments pertaining thereto which, in the opinion of the Company, may involve the reinsurance hereunder."

After Sunoco was sued in its first MtBE product liability claim in early 2000, Sunoco's broker (Aon) reported the claim to Sunoco's current excess liability underwriters, including MRAM. In this February 25, 2000 letter, Sunoco provided "notice of claim and occurrence" with respect to the Berisha lawsuit.

On December 27, 2000, during the currency of the Helios policy in which Sunoco first reported the claim, Sunoco's Director of Risk Management and Insurance, Robert Vryhof,

informed MRAM that "pursuant to Conditions V, Notice of Occurrence and Claims," Sunoco provided "Notice of Integrated Occurrence encompassing claims of an environmental nature relating to the gasoline additive MTBE." That notice identified the Berisha lawsuit and other situations where Sunoco was providing remedial efforts but where litigation had not yet been commenced. On that same day, Vryhof also sent a second letter to MRAM in which it gave notice of the following occurrences as defined in the policy which may arise from:

- the manufacture, distribution, sale or use of MTBE, Benzene, Tolene, Xylene or other chemicals or products, exposure or use of which have resulted in claims being filed against others in the Energy, Petrochemical and Chemical Industries, and
- the distribution, sale or use of tobacco or tobacco products.

On January 9, 2001, MRAM's Stanley Kosloski acknowledged Mr. Vryof's correspondence and verified that he had received general claims data as well as a "Notice of Integrated Occurrence involving MTBE."

Over the next three years, as new claims were presented to Sunoco, they were forwarded to MRAM, as part of the previously identified integrated occurrence. On September 21, 2004, MRAM acknowledged that it had received a number of notices and CDs relating to "an Integrated Occurrence declared under policy HEL-1028 on December 27, 2000." MRAM also noted that it was "operating under the belief that [Sunoco] intended to report all of these MTBE claims to us under the one Integrated Occurrence of December 27, 2000."

In addition, MRAM asked for a "breakdown of the various claims filed against the insured," and a list of the "itemized amounts expended for each claim."

2. Analysis

Defendant asserts that timely "batch occurrence" notice was not given. First, MRAM argues that under the Helios policy, Sunoco was required to give notice to Helios of an occurrence prior to the expiration of the Helios policy. As such notice is a condition precedent to Sunoco being covered under the Helios policy, a failure by Sunoco to comply with this requirement excuses MRAM's reinsurance obligations. Second, to the extent that Sunoco's written notice to MRAM can be deemed constructive notice to Helios, the notices provided to MRAM do not comply with the insured's obligation under Section V(d) to identify an occurrence as a "batch occurrence" during the policy period. Specifically, the notices provided by Vryhof used the term "integrated occurrence," which is undefined in the policy and cannot be fairly read as "batch notice." As a result of this defect, MRAM argues that under the express terms of the policy, each MtBE claim constitutes a separate potential occurrence under the policy.

Plaintiff counters that MRAM's hyper-technical insistence on the use of the word "batch" rather than "integrated" in certain notices is wholly contrary to the parties' intentions, as reflected in their course of dealings, and contrary to New York law, which rejects defendant's strict construction of notice requirements in insurance policies. See Greenburgh Eleven Union Free School District v.

National Union Fire Ins. Co. of Pittsburgh, 758 N.Y.S. 2d 291, 293 (2003) ("Notice requirements are to be liberally construed in favor of the insured, with substantial, rather than strict, compliance being adequate.") Rather, Sunoco asserts that MRAM received timely notice that Sunoco intended to treat all of its MtBE claims as a single, integrated or batched occurrence.

1. Helios Had Actual Notice from Sunoco of an Integrated Occurrence.

Defendant's first argument regarding the sufficiency of Helios' notice during the currency of the policy is unsupported by the undisputed facts in this case. At the time of these letters, Vryhof was both the President of Helios and a Director of Risk Management and Insurance at Sunoco. In order to prepare the December 27, 2000 letters to MRAM, Sunoco, through its Director (Vryhof), notified Helios, through its President (Vryhof), that it had decided to elect to treat its MtBE related-events as an integrated occurrence under the Helios policy.²

That the December 27, 2000 letters to MRAM were not addressed to Helios does not vitiate the fact that Sunoco had informed Helios of its decision. MRAM would not have received these letters in the first instance had Helios not concluded that its policy was implicated. MRAM was not a

²Vryhof, Helios' President, was first aware of Sunoco's decision to treat this claim as an integrated occurrence by no later than December 22, 2000, when he received the drafts of the letters from Sunoco that he sent to MRAM five days later. Thus, Helios, through its President, was on actual notice of Sunoco's decision to treat all of its MtBE-related claims as a single occurrence during the currency of the Helios policy.

direct insurer of Sunoco; it was a reinsurer of Helios. Thus, the fact that MRAM received these letters is undisputable evidence that Helios had already received timely notice of Sunoco's notice of an "integrated occurrence" with regard to the MtBE situation.

2. The Vryhof Letters to MRAM Provided Defendant with Notice of a Batched Occurrence as Required by Section (d) of Article V of the Helios Policy.

MRAM argues that, because the Vryhof letters failed to use the terms "batch occurrence," Sunoco failed to meet its obligation to provide notice that it had elected to treat all of its MtBE-related claims as a single occurrence under the provisions of the Helios policy.

That argument fails on two grounds. First, as a matter of law, it impermissibly exalts form over substance. New York law, which controls the Helios policy, rejects such an approach. New York courts look to whether the recipient understood the import of the notice, *i.e.*, was the information provided to the insurer sufficient to enable it to consider its rights and liabilities. Turkow v. Erie Ins. Co., 798 N.Y.S.2d 768, 769-70 (2005).

As testified to by Vryhof, there is no question that Helios understood that Sunoco intended to treat all of its existing MtBE claims and those that might be made against it in the future, as a single integrated, or batch, occurrence under Section V(d). And, based on that understanding, Vryhof provided MRAM and its other insurers with the same batch or integrated occurrence notice. The

information contained in the December 27 letters is not susceptible to any other interpretation.

Nor did MRAM misunderstand the nature of the notice that it had received. On more than one occasion, MRAM acknowledged the substance of Sunoco's election.³ Specifically, beginning in early 2001, MRAM acknowledged notice of an integrated occurrence in which the subject was "MTBE related claims which have been made against Sunoco."⁴ Further, MRAM understood this fact and, thereafter, batched the claims in a single claims file and used a single reference number to keep all of the Sunoco MtBE related claims under one integrated occurrence.

3. Conclusion

As all the parties clearly understood Vryhof's use of the word "integrated occurrence" to be synonymous with "batch occurrence," Sunoco timely complied with the integrated or batch notice provisions contained in the Helios policy.

³A number of treatises support plaintiff's argument that "batch" and "integrated" are used interchangeably in the insurance business. See M. Smith et al., "Coming to Grips with the Bermuda Form," Strategic Risk (February 2006) ("notice should be designated as notice of integrated occurrence"); R. Amengual, "The Integrated Occurrence Coverage," Biblioteca Juridica Online, (Oct. 11, 2008), at 3, n.4 ("To 'batch' or 'integrate' claims will be used interchangeably). In fact, in one publication titled *The Bermuda Form*, the index entry for "batch occurrence," refers the reader to "integrated occurrence.")

⁴In fact, the successor Bermuda form, which comprised some of Sunoco's coverage during this policy period, replaced the term "batch" with the term "integrated." This fact reflects the fact that MRAM as an insurer knew that the term "integrated" could be used interchangeably with the term "batch."

Legal Issue # 2

The parties stipulated to have this Court address the following legal issue in order to facilitate orderly discovery and mediation

When does Helios's obligation with respect to defense costs arise?

See Notebook 1, Exhibit 12, page 2, lines 22-23.

1. Introduction

Plaintiff argues that defense costs associated with the MtBE claims should be paid as they are incurred. Defendant asserts that payment of defense costs is not required under the Helios policy unless and until Sunoco's liability has been fixed and rendered certain by final judgment or settlement.

Helios issued an Excess Liability Insurance policy to Sunoco, Inc. for the policy period December 31, 1998 to December 31, 2000, with a retroactive date of November 1, 1991 for all operations except product liability claims (for which there is an April 1, 1986 retroactive date).¹

¹ The Court denies defendant's request to take judicial notice of (1) the Complaint in Sunoco, Inc. v. Illinois National Ins. Co; (2) Sunoco's Memorandum of Law in Opposition; (3) a transcript of proceedings in Sunoco, Inc. v. Illinois National Ins. Co., and (4) an Order in that case. While arguably susceptible to judicial notice, these materials are irrelevant. Sunoco's arguments and or/admissions regarding its intentions in a policy containing different language (including an express provision regarding the duty to defend) are neither binding in this action nor useful to the interpretation of the Helios policy.

The Helios policy has a "limit of liability of \$50 million each occurrence and aggregate, part of \$100 million each occurrence and aggregate, in excess of \$5 million each occurrence not subject to an aggregate."

Defendant MRAM reinsures 100% of the Helios Policy limits.

2. Analysis

The court has already found that the obligation of defendant MunichRe, as a facultative reinsurer, of Helios, follows the fortunes and/or follows the settlements of the ceding company. The question for this court, therefore, is whether Helios' decision to advance the costs of defense (in excess of its self-insured retention ("SIR")) incurred by its insured, Sunoco, in defending the MtBE litigation, was made in good faith.

Defendant MunichRe contends that this threshold cannot be reached where there is absolutely no contractual obligation to pay Sunoco's defense costs before there is a final judgment or settlement involving a covered occurrence.

Both parties agree that there the express language of the Helios policy obviates a separate duty to defend by the insurer. The only question, therefore, is whether there are other provisions in the Helios policy that can be construed to require pre-judgment/settlement payment of defense costs (in excess of the SIR) by the insurer.

Under the Helios policy, the "provisions, stipulations, exclusions and conditions of this Policy are to be construed in an evenhanded fashion as between the Insured [Sunoco] and Underwriters [Helios]. This provision, therefore, expressly precludes application of any doctrine that construes ambiguities in the policy in favor of the insured. And, pursuant to its express terms, the policy is to be construed under New York law.

A review of the Insuring Agreement, Loss Payable provision and Damages definition contained in Section A of the Helios Policy (i.e., the excess liability coverage), supports defendant's argument that Helios agreed only to indemnify Sunoco for defense costs as a component of damages payable upon the conclusion of the litigation (by judgment or settlement).

The court reaches this conclusion based on the express terms and structure of the Damages definition. Under that provision, enumerated types of damages include, *inter alia*, all forms of damages, costs of compliance and legal expenses that the policyholder may be required to pay by reason of judgment and settlement, and for litigation, including but not limited to attorneys fees, which are paid "*as a consequence of an occurrence covered hereunder.*"² See

² Under the express terms of the Helios policy, the term "occurrence" is defined to include, *inter alia*, an event or repeated exposure, which causes or is alleged to cause or which is deemed to cause personal injury or property damage during the relevant coverage period. See Notebook 2, Exhibit 21, §III(e), page 6 of 27.

Notebook 2, Exhibit 21, §III(g), page 7 of 27 (emphasis added).

Under the express terms of the Helios policy, then, the litigation costs, including attorneys' fees must be found to have been incurred as a consequence of a covered occurrence before they are compensable under the indemnity policy.

In Stonewall Ins. Co. v. Asbestos Claims Management Co., 73 F.3d 1178, 1219 (2d Cir. 1995), the Second Circuit addressed the question of the timing of payment of defense costs under a policy with virtually identical language. In Stonewall, the insuring agreement required the insurer to indemnify the insured for "damages and defense costs 'paid as a consequence of any occurrence covered hereunder.'" The Second Circuit held that there was no duty to advance the payment of defense costs. Rather, the court held that "under policies containing a duty to reimburse defense costs, but not a duty to defend, the Insurers have a duty to reimburse defense costs for claims that are established to be covered through judgment and settlement, and not for claims only potentially falling within the policy's coverage. See also Save Mart Supermarkets v. Underwriters at Lloyd's London, 843 F. Supp. 597, 603-04 (N.D. Cal. 1994).

Plaintiff's efforts to distinguish Stonewall are unpersuasive. Although the Helios policy defined "occurrence" more broadly than the policy in Stonewall, that fact does not change the outcome. In both Stonewall and the Helios policy, before damages were payable, they

had to be found to have been incurred "as a consequence of an occurrence covered hereunder." Even if that "occurrence" arises as a result of an alleged injury as pled in a complaint, before litigation fees and costs can be recovered as an element of damages, there needs to be a determination that these amounts were incurred as a consequence of a covered event. That cannot be determined until there is a final judgment or settlement in the underlying lawsuit.

Further, the cases relied upon by the plaintiff in support of their reading of the Helios insurance contract are factually distinguishable. In Federal Ins. Co. v. Kozlowski, the fiduciary liability policy contained an express "duty to defend" provision - a provision that is noticeably absent in the Helios policy. See also Federal Insurance Co. v. Tyco International, 2 Misc. 3d 1006 (A) at *2 (2004 WL 583829 (N.Y. Sup.)); In re Worldcom, Inc. Securities Litigation, 354 F. Spp. 2d 455, 466 (S.D.N.Y. 2005).

Nor can the language of the Loss Payable provision in the Helios policy create an immediate obligation by Helios to pay defense costs in excess of the SIR. The Loss Payable provision of the Helios policy provides:

Liability under this Policy with respect to any occurrence shall not attach unless and until the Insured and/or the Insured's underlying insurer shall have paid the amount of the underlying limits or the retention amount set forth in Item 2 of the Declarations as provided in this policy, and with respect to the Insured's liability on account of personal injury, property damage or advertising

liability, unless and until the Insured's liability shall have been fixed and rendered certain either by final judgment against the Insured after trial or by settlement approved in writing by the Underwriters.

See Notebook 2, Exhibit 21, SV(g), page 15 of 27.

This provision, a condition precedent to coverage, expressly provides that liability under the policy will not attach until the SIR has been satisfied, and until the insured's liability on account of personal injury, property damage or advertising liability has been "fixed and rendered certain" by a final judgment or approved settlement.

As in FMC Corp. v. Plaisted, 61 Cal. App. 4th 1132, 1201 (1998), the loss payable provision incorporates the obligation "to indemnify" language in the insuring agreements and the enumerated damages provision, which (as discussed above) is defined as those amounts "paid as a consequence of an occurrence covered hereunder." Taking these three provisions together, until (1) the claim underlying the need for defense costs has been resolved and, (2) thereafter found to be covered by the policy, does the obligation to indemnify Sunoco for any damages, including attorneys fees and costs paid in defense of the action, arise. To construe the policy otherwise would be to impose a duty to defend upon a contract where no such intention can be explicitly found.

The failure of the loss payable provision to mirror the enumeration of damages provision does not create an

ambiguity nor can it be fairly read to obligate Helios to advance attorneys' fees before the claim is resolved.

As Helios had absolutely no contractual obligation to pay defense costs incurred by Sunoco before a final judgment or settlement and a finding of a covered occurrence, it did not act with good faith in so doing. Accordingly, MunichRe is not bound by the ceding company's decision and there is no current obligation on their part to pay defense costs in excess of the SIR.

Legal Issue # 3

The parties stipulated to have this Court address the following legal issue in order to facilitate orderly discovery and mediation:

Is the MRAM certificate subject to the "follow the settlements" or "follow the fortunes doctrine" as a matter of law?

See Notebook 1, Exhibit 12, page 2, lines 24-25.

Plaintiff argues that, under New York law, MRAM, as the reinsurer of Helios, "follow the fortunes and/or follow the settlements" of Helios, as the insurer of Sunoco. Accordingly, defendant cannot disregard good faith determinations made by Helios, the insurer of Sunoco.

Defendant asserts that absent express language in the reinsurance certificate, the "follow the fortunes or follow the settlements" doctrine should not be read into the contract.

1. Evidentiary Rulings

At the outset, plaintiff objects to the declaration of attorney Robert J. Bates, Jr. (see Notebook 1, Exhibit 20) as set forth in Notebook 1, Exhibit 19 on the following grounds: (1) Lack of personal knowledge, (2) documents are hearsay, and (3) the documents are irrelevant.

The objection is sustained based on lack of personal knowledge and hearsay. Bates did not participate in the creation of any of the documents attached to his declaration, nor can he establish the factual prerequisites for their admission as business records. Nor was sufficient information provided regarding these documents so as to justify taking judicial notice.

2. Background Facts

The parties stipulate to the following facts:

Helios issued an Excess Liability Insurance policy to Sunoco, Inc. for the policy period December 31, 1998 to December 31, 2000, with a retroactive date of November 1, 1991 for all operations except product liability claims (for which there is an April 1, 1986 retroactive date.). The Helios policy has a limit of liability of \$50 million each occurrence and aggregate, part of \$100 million each occurrence and aggregate, in excess of \$5 million each occurrence not subject to an aggregate."

Defendant MRAM reinsures 100% of the Helios Policy limits. The reinsurance certificate provides, in part, as follows:

The Reinsurer agrees to indemnify the Company against losses or damages which the Company is legally obligated to pay with respect to which Insurance is afforded during the term of this Certificate under the policy reinsured, subject to the reinsurance limits and coverage shown in the Declarations. The Reinsurer shall not indemnify the Company for liability beyond circumscribed policy provisions, including but not limited to punitive, exemplary, consequential or

compensatory damages resulting from an action of an insured or assignee against the Company. . .

The Company shall settle all claims under its policy in accordance with the terms and conditions thereof. If the reinsurance hereunder is pro rata, the Reinsurer shall be liable for its pro rata proportion of the settlements made by the Company. If the reinsurance hereunder is excess, the Reinsurer shall be liable for its excess proportion of settlements made by the Company after deduction of any recoveries from pro rata reinsurance insuring to the benefit of the Reinsurer.

The reinsurer shall be liable for its proportion of allocated loss expenses incurred by the Company in the same ratio that the Reinsurer's share of the settlement or judgment bears to the total amount of such settlement or judgment under the policy reinsured.

The Company shall advise the Reinsurer promptly of any claim and any subsequent developments pertaining thereto which, in the opinion of the Company, may involve the reinsurance hereunder. The Company, when so requested, will afford the Reinsurer an opportunity to be associated with the Company, at the expense of the Reinsurer, in the defense or control of any claim, suit or proceeding involving this reinsurance, and the [C]ompany and the Reinsurer shall cooperate in every respect in the defense and control of such claim, suit or proceeding.

The Company shall place at the disposal of the Reinsurer and the Reinsurer shall have the right to inspect . . . the books, records and papers of the Company pertaining to the reinsurance provided hereunder and all claims made in connection herewith.

The MRAM reinsurance certificate contains no "follow the fortunes and/or follow the settlements" language.

On February 25, 2000, Sunoco's broker gave notice of the Berisha lawsuit to "Interested Underwriters," consisting of Sunoco's "Current Excess Liability Underwriters," which

included AISLIC and MRAM, and "Settled Defendants in the Jalisco Litigation and Products Liability Coverage Remaining in Place." On December 27, 2000, Robert Vryhof, Sunoco's Director of Risk Management and Insurance and Helios' President, provided MRAM with two letters. On January 9, 2001, MRAM's Stanley Kosloski acknowledged Mr. Vyrof's correspondence.

3. Choice of Law

Sunoco submits that the law of New York controls in this case. Specifically, plaintiff argues that because the underlying Helios Policy expressly provided that it would be governed and interpreted by New York Law, that the reinsurance certificate issued by MRAM similarly followed form regarding the choice of law.

Defendant contests that contention. Rather, defendant asserts that the MRAM reinsurance certificate had its own terms and conditions that governed the respective duties and obligations of the parties to that agreement and, therefore, that New York law does not automatically govern. However, defendant argues that there is no need to apply a "governmental interest" test here to determine which state's laws govern the reinsurance certificate because the law of California and New York are the same.

First, as a preliminary matter, the court does not agree with defendant that New York and California treat the issue presented in this instance

identically. For instance, New York implies the application of "follow the fortunes" where, as in this case, there is concurrency of coverage between the ceding company's policy and the policy of reinsurance.¹ See Granite State Ins. Co. v. ACE American Reinsurance Co., 849 N.Y.S.2d 201, 203 (2007). By contrast, there are no reported decisions in California on this issue, and two unpublished federal court decisions opining on California state law provide no precedential authority.

If the application of the "follow the fortunes" as an implied term of the reinsurance certificate is a question of contract interpretation, then the choice of law determination is performed pursuant to Section 1646 of the California Civil Code. See Frontier Oil Corp. v. RLI Ins. Co., 153 Cal. App. 4th 1436, 1449 (2007). Here, the nature of the contract and its surrounding circumstances implicate New York law.

First, the reinsurance contract was made in New York. See Costco Wholesale Corp. v. Liberty Mutual Ins. Co., 472 F. Supp. 2d 1183, 1197 (S.D. Cal. 2007) ("a contract is "made" in the place of acceptance"). MRAM issued the certificate from its New York office and Sunoco's broker in New York accepted it.

¹Defendant's argument that the holding of Granite should be limited to reinsurance policies where there is an express "follow the fortunes" and/or "follow the settlements" provision. This court declines to do so. There is nothing in the express holding of Granite, nor in its policy rationale, nor in the authority cited by that court in reaching its conclusion that would so require.

Second, the place of its performance of the reinsurance certificate was New York. The certificate at issue fully reinsured the obligations in the Helios policy, which expressly provided that it be governed by New York law. The circumstances surrounding the reinsurance agreement, therefore, lead to the conclusion that the intended place of performance was New York.

Moreover, even if the choice of laws issue requires the court to perform a governmental interest analysis, the decision to apply New York law to construe this contract would be the same. Under prong two of the three prong test mandated by the governmental interest standard, the court must examine the interest of each jurisdiction in having its own law applied to the particular dispute. See Frontier Oil, 153 Cal. App. 4th at 1454-55.

In this case, New York is the only state with a plausible interest in the application of its law to this dispute. The contract at issue, which was created and accepted in New York, provides for 100 percent indemnity for an insurance policy that expressly provides for the application of New York law. In addition, several of the underlying cases for which Sunoco seeks coverage, and for which the insurer seeks reinsurance, were filed in New York. Finally, the MtBE Multidistrict Litigation that is at issue in this action is pending in New York City. Defendant fails to explain why California would have any interest in the application of its law to two foreign

corporations whose dispute and contract have no discernable ties to California. As discussed *supra*, California law in this area is, at best, unsettled, or (as defendant's contend) consistent with New York. California would, therefore, have no interest in having its law applied to this action. See, e.g., Hurtado v. Superior Court, 11 Cal. 3d 574, 580 (1974).

Accordingly, the law of New York shall control the interpretation of the MRAM reinsurance certificate.

4. Application of New York Law

Under New York law, the "follow the fortunes" or "follow the settlements" doctrine binds the reinsurer to the good faith coverage determinations made by its reinsured, regardless of whether those decisions are made in or outside of coverage litigation. Granite State, 849 N.Y.S.2d at 203.

Historically, the "follow the fortunes" doctrine referred merely to underwriting risk and the concept that the reinsurer followed form as to the risks insured under the reinsurance contract. And, the "follow the settlements" doctrine referred to the reinsurer's obligation to follow the claims decisions made by the reinsured.

Over time, however, these doctrines have been applied in the context of claims decisions and the courts have, by implication, applied both notions to require the reinsurer to provide coverage coextensive to that afforded by the reinsured policy, regardless of whether the term "follow

the form," or "follow the fortune," or "follow the settlements" appears in the contract.

Thus, where there is concurrency of coverage between the ceding company's policy and the policy of reinsurance, the doctrine imposes a contractual obligation upon the reinsurer to indemnify the ceding company for payments it makes pursuant to a loss settlement under its own policy, provided that such settlement is not fraudulent, collusive, or otherwise made in bad faith, and provided further that the settlement is not an *ex gratia* payment, *i.e.*, one made by a party that recognizes no legal obligation to pay, but makes payment to avoid grater expense, as in the case of a settlement by an insurance company to avoid the cost of a suit.

Granite State, 849 N.Y.S. 2d at 203.

The "follow the fortunes" doctrine requires the reinsurer to indemnify for payments reasonably within the terms of the original policy, even if technically not covered by it. See Travelers Cas. And Surety Co. v. Certain Underwriters at Lloyd's of London, 96 N.Y. 2d 583, 596 (2001). Thus, the reinsurer is required to "accept the cedent's good faith decisions on all things concerning the underlying insurance terms and claims against the underlying insured: coverage, tactics, lawsuits, compromise, resistance or capitulation." See British Intl. Ins. Co. v. Seguros La Re-publica, 342 F.3d 78, 85 (2d Cir. 2003). Under New York law, therefore, unless a reinsurer can demonstrate that the settlement by the underlying insurer is in bad faith, fraudulent or clearly outside the scope of coverage, the reinsurer is bound by that decision. Granite State, 849 N.Y.S. 2d at 203.

There is no question in this case that there is a "concurrency of coverage" between the Helios policy and the policy of reinsurance issued by defendant. Under its express terms, the MRAM certificate assumed 100% of the financial liability originally assumed by Helios. Thus, even in the absence of an express provision to this effect, the reinsurance policy would, as a matter of law, follow the fortunes of the underlying Helios policy.

Defendant's argument that the parties intended a contrary outcome is predicated on a tortured and implausible construction of the certificate's express terms. Rather, a reading of the plain language of the loss settlement provisions of the reinsurance certificate shows that Helios, not defendant, was responsible for making claims determinations. In another reinsurance policy containing loss settlement provisions nearly identical to those in this case, a court concluded that the reinsurer followed the form and fortunes of the underlying insured. See Insurance Company of the State of New York v. Associated Manufacturers' Mutual Fire Ins. Co. of New York, 74 N.Y.S. 1038, 1039 (App. Div. 1902). Thus, none of the express terms of the reinsurance certificate can be fairly read to express an intention by the parties to eschew the implied "follow the fortunes" or "follow the settlements" doctrine.

There is nothing at this juncture that would support a conclusion that there was collusion, bad faith or fraud in Helios' decision to pay Sunoco's MtBE claim. That Helios was a captive insurer does not meet the "extraordinary showing of a disingenuous or dishonest failure," sufficient to excuse a reinsurer from the application of the follow

the fortunes doctrine.² See Travelers Casualty & Surety Co. v. Gerling Global Reinsurance Corp. of Am., 419 F.3d 181, 191 (2d Cir. 2005).

² In this case, MRAM was directly and intimately involved in these MtBE cases. Defendant had the ability to address any concern over Helios' status as a captive insurer, including the express right to associate into any proceeding. In fact, Sunoco invited defendant to participate in the handling and disposition of the underlying MtBE-related claims, but MRAM declined.