Ohio Supreme Court Rules That Payments Into a Lead Paint Abatement Fund Are Not "Damages"

Several California counties and cities sued Sherwin-Williams and other paint companies for the public nuisance created by their sale and promotion of lead paint. Sherwin-Williams and two other paint companies were ordered to pay money into an abatement fund administered by the State of California.

Sherwin-Williams sought reimbursement from its commercial general liability insurers for the payments Sherwin-Williams made into the fund. The insurers declined, and the dispute made its way up to the Ohio Supreme Court.

The policies covered Sherwin-Williams' liability for damages because of bodily injury or property damage (or some similar variation). The issue was whether the payments into an abatement fund are "damages." The Ohio Supreme Court held that they are not.

"Damages" are money paid to compensate for loss or injury. The abatement fund established in the California litigation, however, did not compensate the counties and cities for past loss or injury. The fund instead was meant to prevent future harm related to lead poisoning.

Recognizing that children were most at risk from lead paint exposure, the trial court in the California litigation developed an abatement plan to mitigate the risk of future harm to children. The plan called for screenings to see which properties qualified for inspection, priority groups, and educational outreach programs.

The Ohio Supreme Court disagreed with the intermediate appellate court's finding that the abatement fund was also to compensate the counties and cities for money depleted by their efforts to remediate lead contamination in houses and buildings throughout California. The court found no evidence that any part of the fund was to pay back the counties and cities for work already done.

The court also rejected Sherwin-Williams' argument that because it was found liable for the nuisance created by lead paint in residences built before 1951, that its payment into the abatement fund was to compensate for past property damage. The court found no evidence that lead paint causes physical damage to property. Nor did the California trial court create the fund to fix any damage to buildings because the counties and cities never alleged that the buildings suffered physical injury.

The insurers had no duty to indemnify Sherwin-Williams. The abatement fund was designed to eliminate future harm, not to compensate for past harm. Sherwin-Williams' payment into the abatement fund therefore did not qualify as "damages."

The case is *Sherwin-Williams Co. v. Certain Underwriters at Lloyd's London*, No. 2023-0255 (Ohio Dec. 10, 2024).

North Carolina Supreme Court Breaks with Majority of States: Finds Business Interruption Losses from Covid-19 Orders Are Covered "Direct Physical Loss"

The North Carolina Supreme Court, deciding companion cases of business interruption coverage related to Covid-19 government orders, departed from most jurisdictions in finding that such losses constitute covered "direct physical loss."

In *N. State Deli*, the lead case, the insureds were bars and restaurants in North Carolina forced to suspend operations because of Covid-19-related government orders. In *Cato*, the insured was a clothing retailer with more than 1,300 stores across North Carolina and other states. The policies contained broadly similar "all risks" commercial property insurance language that protected property and business income from "direct physical loss."

The main issue in both cases was whether there was a "direct physical loss" when the government orders forced temporary restrictions on the use and access of the plaintiffs' properties. The insurers argued that Covid-19 orders regulated the activities of people, not property, and the restaurants experienced no physical change to the business property itself. By analogy, the insurers argued that "loss of a car" is not the same as "loss of use of a car," "as any grounded teenager could confirm."

The North Carolina Supreme Court disagreed. It held that a reasonable insured would expect that property "loss" occurs when the property is no longer usable for its insured purpose. The court added that the policies used "direct physical loss" in conjunction with "direct physical damage." The court surmised that this means "loss" is something distinct from "Damage." The court noted that the policy excludes certain kinds of government zoning regulations, government ordinances, government seizures, and war and military actions and found that an insured could reasonably expect virus-related government orders that are *not* an excluded cause of loss to be covered. Similarly, in *Cato*, the court noted that the policy exclusions for unexplained disappearances, seizure or other governmental destruction, the cumulative effects of dust, and "delay, loss of market, or loss of use" suggested that "direct physical loss" was broader than physical tangible alteration to property, or else they need not be mentioned as exclusions at all.

The North Carolina Supreme Court recognized that its conclusion conflicted with the many jurisdictions that have addressed the same issue. The court stated that it believed that the term "direct physical loss" was ambiguous, and other courts were imposing judicial definitions of the phrase. The court emphasized that the lodestar in North Carolina is the reasonable expectation of the insured and that ambiguities should be resolved in favor of the insured.

In *N. State Deli,* the court's ruling on "direct physical loss" meant a reversal of a lower court opinion for the insurers. But that ruling was not dispositive in *Cato*. The *Cato* policy had an additional provision that barred coverage for "Contamination, and any cost due to Contamination including the inability to use or occupy property or any cost of making property safe or suitable for use or occupancy." Contamination meant "any condition of property due to the actual presence of any . . . virus." Since Cato's stores were compelled by government order to close due to Covid-19, the court held that a reasonable insured would understand such allegations to qualify as a condition of the property based on the presence of a virus. For this reason, the North Carolina Supreme Court modified the lower court decision but affirmed its judgment.

The cases are *N. State Deli, LLC v. Cincinnati Ins. Co.*, 225PA21-2 (N.C. Dec. 13, 2024) and *Cato Corp. v. Zurich Am. Ins. Co.,* No. 353PA23 (N.C. Dec. 13, 2024).

Connecticut Supreme Courts Finds That Insurer Ineffectively Cancelled Workers' Comp Policy

This case reaffirms the principle that when cancelling an insurance policy, the insurer's notices must be clear and consistent. And compliance with statutory notice requirements will not supplant contractual obligations.

Napolitano operated a roofing business. He had two workers' compensation policies with Ace: one effective from October 21, 2017, to February 9, 2018 ("2017 policy"), the other effective from February 9, 2018 to February 9, 2019 ("2018 policy").

On March 28, 2018, Ace informed Napolitano that it would impose an audit noncompliance charge if he did not provide access to payroll and tax records required for the premium on the 2017 policy. Ace resent the letter on April 3.

On April 5, Ace sent two more letters to Napolitano. One was a Notice of Noncooperation with Audit on the 2018 policy, stating that failure to comply will result in the policy being cancelled, and that the cancellation will remain in effect if the audit is not conducted before the effective date of cancellation. The letter did not provide a cancellation date.

The other April 5 letter was a notice of cancellation for the 2018 policy effective April 25. The letter told Napolitano to contact his "producer" for information about the cancellation.

On April 6, Ace sent the cancellation notice to the Workers' Compensation Commission (but not the noncooperation notice).

On April 7, Napolitano mailed Ace the tax records. Three days later, he contacted the producer to check his compliance status and was told that he was in compliance. The producer then issued certificates of insurance certifying that he had workers' compensation insurance under the 2018 policy.

Ace's agent emailed Napolitano on April 16 stating that it had the tax records but not the audit report. The email requested compliance by April 21 and did not mention the April 25 cancellation date. Napolitano dismissed this email as "noise" and did not provide the audit report.

On May 29, an employee of Napolitano's roofing company was injured and filed a claim for compensation benefits with the Workers' Compensation Commission. The Commission determined that Napolitano did not have workers' compensation insurance because it was cancelled on April 25. The commissioner determined that the cancellation complied with the statutory requirements (General Statutes § 31-348) because it was reported to the chairperson 15 days before the cancellation took effect.

Napolitano then sued Ace for a declaration that he was owed defense and indemnity for the employee's claim. Napolitano prevailed before the trial court, but the intermediate appellate court reversed.

Napolitano argued to the Connecticut Supreme Court that the Appellate Court was wrong. Ace sent the cancellation notice to the Commission chairperson in compliance with the statutory requirement, but the cancellation notice itself did not comply with the contractual requirements because it was not definite, certain, and unambiguous. The Appellate Court considered only the fact that the cancellation notice was timely delivered to the chairperson, but did not consider all the other communications.

The Connecticut Supreme Court agreed with Napolitano. Ace's communications to Napolitano did not provide him with definite, certain, and unambiguous notice of cancellation, despite Ace having complied with the statutory requirements. So, the court held that when considering whether notice of cancellation under a workers' compensation policy is definite and certain, all relevant communications must be considered, not just the cancellation notice sent to the chairperson under the statute. In other words, compliance with the statutory requirement does not supplant the insurer's obligations under contract law.

The court rejected Ace's argument that the communications unambiguously notified Napolitano that his policy was cancelled on April 25. Napolitano received two conflicting notices on April 5, one stating that the policy was cancelled, the other stating that noncompliance would result in cancellation. Napolitano was told by his producer, whom he was told to contact about cancellation, that he was in compliance after submitting the tax records. And the April 16 email set an April 21 date for compliance without mentioning cancellation on April 25.

The Connecticut Supreme Court thus held that the Appellate Court incorrectly concluded that Ace effectively cancelled the workers' compensation policy.

The case is *Napolitano v. Ace Amer. Ins. Co.*, No. SC 20922 (Conn. Dec. 24, 2024).

North Carolina Court of Appeals Finds No Duty to Defend Under Commercial Automobile Policy Because Underlying Suit Relied on Case Law That Brought It Within Fellow Employee Exclusion

In August 2017, Plaintiff Luis Ortez became distracted while driving his employer's vehicle. He was involved in an accident, which resulted in the death of fellow employee, Darren Drake Estes, a passenger in the vehicle.

The employer had a commercial auto policy with Penn National Security Insurance Company. The policy covered an "insured" for "[a]nyone else while using with [employer's] permission a covered 'auto' you own, hire or borrow . . . ." But the policy excluded as an "insured" a "fellow employee."

A wrongful death suit was filed against Ortez. A few days before trial, the Estes Estate transmitted a settlement offer to Penn National, offering to execute a covenant not to enforce judgment for Ortez in exchange for delivery of a check of $30K before 3 p.m. on April 8, 2019, the day before the trial. Penn National agreed to the settlement but asserted that it could not deliver the check by the deadline. Counsel for the Estes Estate withdrew the settlement.

The trial went forward, and an order was entered against Ortez for $9.5M. Ortez and the Estes Estate filed a complaint in North Carolina court alleging that Penn National had breached its duty to defend by failing defend Ortez. Ortez and the Estes Estate also alleged that Penn National had breached its duty to settle, and that they had committed unfair and deceptive trade practices under North Carolina's Unfair and

Deceptive Trade Practices Act ("NCUDTPA"). The trial court granted Ortez's motion for judgment on the pleadings and entered judgment for $28M, including treble damages under the NCUDTPA.

The North Carolina Court of Appeals reversed. The court held that there was no duty to defend because the underlying complaint alleging Ortez's "reckless, willful, and wanton conduct" fell under the "fellow employee" exclusion in the insurance policy. While the complaint omitted facts about the co-employee relationship of the parties, it referenced a well-known North Carolina workers' compensation decision, *Pleasant v. Johnson*, that allowed an injured worker to receive workers' compensation benefits and still maintain a common law claim against the employee. That was enough to bring the allegations within the exclusion.

The court also found that the lower court had erred in concluding that Penn National had breached its duty to settle. Asking for a one-day extension to deliver payment to a demand – a turnaround of less than one business day – did not support a finding and conclusion that Penn National had failed to act in good faith to settle under NCUDTPA.

Because the trial court erred in granting Ortez's partial motion for a Rule 12(c) judgment on the pleadings, the Court of Appeals reversed the trial court's decision.

The case is *Ortez v. Penn Nat'l Sec. Ins. Co.*, No. COA24-169 (N.C. Ct. App. Dec. 17, 2024).

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