

## CORPORATE INSURANCE LAW

Eastern District Holds That Exclusion Bars  
Defense Obligation

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**N**ew York courts recognize the well-settled principle that the duty to defend in an insurance policy is broader than the duty to indemnify. They also construe policy exclusions narrowly and place the burden on the insurer to prove that an exclusion applies.

Nevertheless, that does not mean the courts will not enforce a clearly-drafted exclusion when the facts plainly fall within the scope of the exclusion. Just recently, the U.S. District Court for the Eastern District of New York granted summary judgment to an insurer, holding that the insurer had no duty to defend, based on the terms of an exclusion in the policy.

**'Clear Blue Specialty Insurance'**

In *Clear Blue Specialty Insurance v. TFS NY, d/b/a Sugar Daddy's et al.*, 22-CV-1915, 2023 WL 5806110 (E.D.N.Y. Sept. 6, 2023), the dis-



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trict court was presented with an insurance dispute arising out of an alleged assault at the defendant policyholder's nightclub. The underlying claimant filed suit in state court against the nightclub, several employees and the nightclub's outside security contractor seeking to recover damages. In addition to alleging assault and battery, the complaint asserted a cause of action for negligent hiring.

The nightclub sought coverage under its commercial general liability policy. Following notice of the state court action, the insurer filed a federal declaratory judgment action against the policyholder seeking a declaration that it had no duty to defend or indemnify the nightclub or its employees. The insurer then filed a motion for summary judgment.

## The Insurance Dispute

The parties to the federal action agreed that the insurance policy was triggered because the underlying claim included negligence allegations. The dispute before the district court centered around the third party or contracted security exclusion, which the insurer contended excluded coverage for both defense and indemnity due to the involvement of the security contractor.

The policyholder disagreed, arguing that the insurer was required to defend the entire action because, in addition to the claims against the security contractor, the lawsuit also included claims against the nightclub and its employees.

The contracted security exclusion barred coverage, in relevant part, for "any loss, claim, 'suit', cost, expense or liability for damages, directly or indirectly based on, attributable to, arising out

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of, involving, resulting from or in any way related to the acts, omissions or operations of any third party or contracted security services provider . . . including, but not limited to: (a) Defense, safety, protective, barricade or security fencing operations or activities; (b) Crowd, patron or audience control, supervision or management operations or activities; or (c) T-shirt security, patron search, patron pat down, wandling, patron property search, patron ejection, door supervision, line control, bouncer activities or security guarding.

In addition, the exclusion barred coverage for "any loss, claim, 'suit' cost, expense or liability for damages . . . in any way related to the hiring, contracting of, investigation, supervision, management, training or retention of any entity or non-employee individuals" engaged in security operations.

Further, the exclusion expressly provided that the insurer has "no duty to defend any insured against any claims or 'suits' seeking damages for 'bodily injury', 'property damage', 'personal and advertising injury' or 'injury' in regard to the matters covered by this exclusion and we have no duty to pay damages in regard to the matters covered by this exclusion."

Finally, the exclusion provided that "[i]f a 'suit' or claim is brought against any insured which contains allegations relating in any way to the matters covered by this exclusion, we will have no obligation or liability to pay sums or perform acts or services." *Clear Blue Specialty Insurance v. TFS NY, d/b/a Sugar Daddy's et al.*, 2023 WL 5806110 at \*1-2.

## The District Court Weighs In

According to the district court, the policyholder contended that the exclusion was silent as to how the policy would respond to claims against the nightclub and its employees that were separate from the claims against the security contractor. The policyholder also maintained that the exclusion was ambiguous.

The district court rejected these arguments, explaining that the terms of the exclusion were clear and not "hidden away in a footnote or fine

print." It emphasized that the exclusion explicitly provided that the policy does not cover any "suit . . . directly or indirectly based on, attributable to, arising out of, involving, resulting from or in any way related to the acts, omissions or operations of any third party or contracted security services provider."

Further, the exclusion expressly cautioned that if a suit or claim is filed against an insured that contains allegations related in any way to the matters covered by the contracted security exclusion, the insurer "will have no obligation or liability to pay sums or perform acts or services" under the policy.

The policyholder also argued that the contracted security exclusion, read as the insurer suggested, would swallow coverage and render the policy illusory.

The district court rejected this position as well, pointing out that the policy would require the insurer to defend a suit involving an incident in which a security contractor was not involved—for example, where the policyholder's employee acted alone or where no security contractor was hired by the nightclub.

As further explanation, the district court noted that it is standard practice for the security contractor to obtain its own insurance and for that insurance to cover the nightclub as an indemnitee of the contractor. Thus, according to the court, it made sense that the nightclub's own insurance would be narrowly tailored to exclude risks involving a security contractor.

Further, it explained that the fact that the security contractor's insurer in this case had also denied coverage does not impact the scope of the nightclub's own policy.

### **Duty To Indemnify**

The district court granted the plaintiff insurer's motion for summary judgment on the duty to defend and the duty to indemnify. However, the court noted that further development of the facts in the underlying lawsuit could alter the situation.

For example, if the claims against the security contractor were dismissed, leaving only claims against the policyholder and its employees, or if the jury decided that only the employees were involved in the assault, the exclusion would no longer be applicable.

Consequently, while the court granted the motion for summary judgment, the order permitted the policyholder to move to reopen on the issue of indemnification if it is determined in the underlying case that the security contractor was not involved in the assault.

### **Looking Forward**

When a court is reviewing the applicability of an exclusion, the burden of proof is on the insurer and the standard of review requires a narrow construction that favors the insured.

Even so, as the Eastern District ruling demonstrates, where the facts plainly fall within a clearly-drafted exclusion, courts will not hesitate to enforce the exclusion as written.