New York Law Journal

SERVING THE BENCH AND BAR SINCE 1888

WWW.NYLJ.COM

An ALM Publication

VOLUME 255—NO. 7

TUESDAY, JANUARY 12, 2016

Corporate Insurance Law

Expert Analysis

Revisiting Non-Assignment Clauses: California Returns to the Majority Rule

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In the June 2012 edition of this column,[1] we discussed the enforceability of non-assignment clauses in insurance policies and, in particular, the Supreme Court of California's decision in *Henkel Corp. v. Hartford Accident & Indemnity Co.*[2] In *Henkel*, the court had departed from the majority rule and denied a successor entity the right to its predecessor's insurance despite the fact that the underlying loss predated the assignment of insurance rights. But recently, in *Fluor Corp. v. Superior Court*,[3] the Supreme Court of California overruled *Henkel*. Corporate policyholders in California welcomed the court's decision in *Fluor Corp.*, which also served to align California's view with the view of the New York courts.

As a refresher, most liability insurance policies contain a standard non-assignment clause or anti-assignment clause that prohibits assignment without the insurer's prior written consent. This clause is intended to protect the insurer from a material increase in risk that might result from the transfer of the insurance policy to a new entity. In the context of an asset purchase deal, however, many clients will seek to transfer existing rights under insurance policies to the purchasing company, notwithstanding the non-assignment clause, and usually without the consent of the insurer.[4] Whether such a transfer is valid often depends on the applicable law governing the assignment of rights.

Under the majority rule, which New York courts continue to follow, a non-assignment clause prevents an insured, absent insurer consent, from assigning the right to make claims for future losses. But an insured can assign the rights to insurance coverage with regard to an existing loss without insurer consent and notwithstanding a non-assignment clause. Courts that follow the majority rule analogize the assignment of an accrued insurance claim—which accrues at the occurrence of the covered injury—to the assignment of a chose in action, and thus continue to recognize a post-loss exception to the restriction on assignments set forth in the non-assignment clause. Courts in a minority of jurisdictions, however, do not recognize this exception. For these courts, a chose in action does not exist, and therefore cannot be assigned, until an existing claim against an insured has "been reduced to a sum of money due or to become due under the policy."[5]

> In light of the decision in 'Fluor Corp.,' it now appears that courts are trending back toward the post-loss exception rule followed by a majority of jurisdictions.

In August, the California high court's decision in *Fluor Corp.* brought California law back in line with the law in New York and a majority of other jurisdictions. In the same month, a New Jersey appellate court also upheld an assignment of rights to insurance coverage for pre-assignment loss.[6] The Supreme Court of New Jersey granted review of the case and will likely soon resolve whether New Jersey will also follow the majority rule.

'Henkel' and Minority Rule

As we discussed in the June 2012 column, courts in a small minority of jurisdictions have narrowed the circumstances in which the assignment of an insurance claim for pre-assignment loss will be permitted without insurer consent. These courts have held that only claims involving an existing loss that can be identified with precision are assignable in the face of a no-transfer clause. The Supreme Court of California's decision in *Henkel* was perhaps the most notable departure from the majority rule.

In *Henkel*, the court denied the plaintiff-successor entity the right to its predecessor's insurance for a pre-assignment loss arising from allegations of injury due to exposure to metallic chemicals manufactured by the predecessor entity. Claimants filed suit against the plaintiff-successor entity which then tendered defense of the claims under the terms of occurrence policies that the defendant insurers had issued to the predecessor. The insurers denied coverage for the claims and refused to contribute to the plaintiff's settlement of the case. The court upheld the insurers' position, explaining that the plaintiff could not overcome the policies' non-assignment clause because the underlying claims had not been "reduced to a sum of money due or to become due under the policy."[7]

The decision in *Henkel* was an abrupt departure from a national trend permitting routine transfers in asset purchase deals and also departed from earlier California case law. Courts that followed the Henkel decision recognized the California Supreme Court's departure from the majority, but nevertheless adopted its rationale that "for an insured loss to generate an assignable coverage benefit, the loss must be identifiable with some precision. It must be fixed, not speculative."[8]

Over the years, the fixed-loss requirement underlying the decisions in jurisdictions such as California and Indiana did not garner much support. Finally, in August 2015, after a 12-year hiatus, the California Supreme Court once again adopted the majority rule allowing post-loss assignment of insurance rights, even in the face of a non-assignment clause.

Return to the Majority Rule

In *Fluor Corp.*, the court considered whether California Insurance Code Section 520, first enacted in 1872 and not considered by the court in *Henkel*, required a different result regarding the post-loss exception. Section 520 appears to contradict the ruling in *Henkel*. The statute provides

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that: "[a]n agreement not to transfer the claim of the insured against the insurer after a loss has happened, is void if made before the loss."[9]

The original Fluor Corp. (Fluor-1), established in 1924, performed engineering, procurement, and construction services (EPC). In the 1980s, Fluor-1 acquired A.T. Massey Coal Company. In 2000, through a reverse spinoff, Fluor-1 transferred its EPC operations to a newly incorporated Fluor Corp. (Fluor-2) in order to separate Fluor-1's core EPC business from the A.T. Massey coal mining operations. As part of the transaction, Fluor-1 transferred all of its EPC-related assets and liabilities to Fluor-2. The transfer included several comprehensive general liability insurance policies that Hartford issued to Fluor-1 from mid-1971 to mid-1986. Each policy contained a non-assignment clause.

Beginning in the mid-1980s, Fluor-1 was named as a defendant in a series of asbestos-related personal injury lawsuits that arose out of the EPC-related business. Hartford defended and settled these lawsuits on behalf of Fluor-1, and later Fluor-2, for several years. In 2006, Fluor-2 sued Hartford seeking declaratory relief regarding Hartford's coverage obligations. Hartford then filed a cross-complaint in which it asserted that Fluor-1 was the named insured on the policies and contended that even if Fluor-1 had attempted to assign its insurance coverage claims to Fluor-2, the assignment was not effective because Hartford did not consent to the assignment.

The trial court denied Fluor-2's request to disregard *Henkel* based on Section 520. An appellate panel then denied relief to Fluor-2 on the grounds that not only was it bound to follow *Henkel*, but also that Section 520 did not contradict *Henkel* because third-party liability insurance did not exist at the time of the statute's enactment. Thus, the California Legislature could not have contemplated that Section 520 would apply to insurance for third-party claims like the asbestos injury claims involved in *Fluor Corp.*

The Supreme Court of California disagreed. In a 59-page opinion overruling *Henkel*, the court discussed the original enactment of Section 520, acknowledging that it was unlikely that the Legislature had contemplated third-party liability insurance in 1872. The court noted, however, that by 1935, when the Legislature recodified Section 520 as part of the newly created California Insurance Code, and certainly by 1947, when the Legislature amended Section 520, third-party liability insurance was prevalent and well known to the Legislature. The court explained that by the 1935 enactment and the 1947 amendment, "it had become clear that the provision's coverage was not restricted to first party policies, and did indeed also regulate third party liability policies."[10]

The court also concluded that the relevant "loss" under Section 520 arises at the time of the covered occurrence or injury and not, as Hartford argued, "when the insured has incurred a direct loss by virtue of the entry of a judgment, or finalization of a settlement, fixing a sum of money due on a claim against the insured."[11] The court explained that, "[t]his result obtains even without consent by the insurer—and even though the dollar amount of the loss remains unknown or undetermined until established later by a judgment or approved settlement."[12]

Thus, the court in *Fluor Corp*. overruled *Henkel*, held that Section 520 applies to third-party liability insurance and ruled that an anti-assignment clause does not bar the assignment of rights under a policy if the covered personal injury or property damage occurred before the assignment. The court was also careful to recognize and affirm the traditional policy arguments which support the post-loss exception. For example, the court acknowledged that a post-loss assignment does not increase the risk to the insurer because the insurer agreed to cover the underlying loss when it issued the policy.

The court further explained that enforcing an anti-assignment clause to bar a post-loss transfer could provide an insurer with an unfair windfall by permitting the insurer to retain premiums collected without having to indemnify a successor entity for covered loss. Finally, the court stated that the post-loss exception to the anti-assignment clause has been recognized as encouraging economic activity by facilitating "the productive transformation of corporate entities." The rule is a "venerable rule that arose from experience in the world of commerce."[13]

The court in 'Fluor Corp.' explained that enforcing an anti-assignment clause to bar a post-loss transfer could provide an insurer with an unfair windfall by permitting the insurer to retain premiums collected without having to indemnify a successor entity for covered loss.

New York and New Jersey

New York and the majority of other jurisdictions continue to hold that a non-assignment clause cannot prevent assignment of the right to recover insurance for pre-assignment loss.[14] Courts that follow this majority rule recognize that insurers have a valid interest in preventing assignments that expand the scope of the risk beyond that which the insurer agreed to cover. But once the insured-against loss has occurred, a later assignment of the insurance rights—at that point an insurance asset—does not affect the insurer's liability because once the loss has occurred, the insurer's liability is fixed.

The Supreme Court of New Jersey will soon have the opportunity to address the enforceability of non-assignment clauses. In *Givaudan Fragrances Corp. v. Aetna Cas. & Sur. Co.*, the New Jersey Superior Court, Appellate Division, consistent with New Jersey case law, ruled that Givaudan Fragrances had received a valid assignment of rights under its affiliate's insurance policies and could pursue roughly $500 million in pollution-claims coverage relating to pre-assignment losses, even without insurer consent.

At least one New Jersey court appears to have issued a ruling in conflict with *Givaudan Fragrances*. In 2014, a New Jersey trial court, in the context of a bankruptcy sale, denied a policyholder's right to assign liability coverage absent insurer consent because the ongoing environmental loss had not matured into a chose in action—because the loss did not require an immediate, fixed obligation to pay.[15] The New Jersey Supreme Court is expected to hear the Givaudan Fragrances case later this year.

Looking Forward

When we last wrote about the enforceability of non-assignment clauses, it appeared that the Henkel decision might be the start of a trend toward the minority rule. But in light of the decision in *Fluor Corp.*, it now appears that courts are trending back toward the post-loss exception rule followed by a majority of jurisdictions.

New York courts have continued to show no sign of moving away from the majority rule. Corporate policyholders and their counsel await the Supreme Court of New Jersey's decision in *Givaudan Fragrances*. While the law seems to be trending back to the majority, because there are few recently published New York cases on this subject, it remains prudent to seek insurer consent where possible to avoid uncertainty with regard to the assignment of insurance rights.

1. Howard B. Epstein and Theodore A. Keyes, "Enforceability of Non-Assignment Clauses in Asset Purchase Deals," N.Y.L.J., Vol. 247, No. 125, June 29, 2012.
2. *Henkel Corp. v. Hartford Accident & Indem. Co.*, 29 Cal. 4th 934 (2003).
3. *Fluor Corp. v. Superior Court*, 61 Cal. 4th 1175 (2015).
4. This column only addresses the right to transfer insurance rights in the context of an asset purchase deal.
5. *Henkel Corp.*, 29 Cal. 4th at 944.
6. *Givaudan Fragrances Corp. v. Aetna Cas. & Sur. Co.*, 120 A.3d 959 (N.J. Super. Ct. App. Div. 2015).
7. *Henkel Corp.*, 29 Cal. 4th at 944.
8. *Travelers Cas. & Sur. Co. v. United States Filter Corp.*, 895 N.E.2d 1172, 1180 (Ind. 2008); see also *Cont'l Ins. Co. v. Wheelabrator Techs.*, 960 N.E.2d 157, 163 (Ind. Ct. App. 2011), transfer denied, 974 N.E.2d 476 (Ind. 2012).
9. Cal. Ins. Code §520 (West 2015).
10. *Fluor Corp.*, 61 Cal. 4th at 1195.
11. Id. at 1199.
12. Id. at 1224.
13. Id. at 1182, 1219.
14. See, e.g., *Globecon Grp. v. Hartford Fire Ins. Co.*, 434 F.3d 165 (2d Cir. 2006); *Northern Ins. Co. of N.Y. v. Allied Mutual Ins. Co.*, 955 F.2d 1353 (9th Cir.1992); *Egger v. Gulf Ins. Co.*, 588 Pa. 287 (2006); *Pilkington N. Am., Inc. v. Travelers Cas. & Sur. Co.*, 112 Ohio St. 3d 482, 2006-Ohio-6551, 861 N.E.2d 121.
15. *Haskell Props. v. Am. Ins. Co.*, No. BER-L-5396, 2014 LEXIS 2428 (N.J. Super. Ct. Law Div. June 6, 2015) ("[T]he law does not recognize the assignment of an inchoate claim from a casualty insurance policy of a bankrupt debtor.").

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