

New Jersey Supreme Court Holds That Defined Term “Money Damages” In Errors And Omissions Policy Does Not Include “In-Kind” Services Rendered And Assets Surrendered As Part Of Settlement, And Also That Insurer That Reserves Its Rights And Provides

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On June 21, 2011, the New Jersey Supreme Court decided Passaic Valley Sewerage Commissioners v. St. Paul Fire & Marine Ins. Co., ___ N.J. ___ (2011), A-97-09, and held that (a) the defined term “money damages” in an errors and omissions policy encompassed only monetary compensation and not “in-kind” services provided or assets surrendered by an insured as part of a settlement and (b) an insurer that properly reserves its rights can offer to pay the costs of defending covered claims while refusing to pay the cost of uncovered claims without violating its duty to defend.

The principal issue on appeal in Passaic Valley Sewerage Commissioners was whether a settlement reached between Spectraserv, Inc., (“Spectraserv”) and the Passaic Valley Sewerage Commission (“PVSC”) in an underlying action brought by Spectraserv constituted “money damages” under an errors and omissions policy that defined “money damages” as “monetary compensation for past harms or injuries.” The settlement involved what the Court identified as “three discrete agreements to resolve six claims” made by Spectraserv against PVSC. The first agreement called for PVSC to accept \$100,000 in lieu of all civil penalties that PVSC could have assessed against Spectraserv. The second agreement required PVSC to accept, treat and dispose of sludge for a period of up to five years that Spectraserv in turn accepted from a third party. The third agreement required PVSC to assign to Spectraserv the right to dispose of sludge on property owned by a third party.

The Court held that the term “money damages” did not include “the value of the services rendered and assets surrendered” in the Spectraserv settlement. The Court concluded that the defined term was clear and unambiguous in its requirement that there be some “monetary compensation” paid in order for there to be “money damages.” Looking at the settlement between Spectraserv and PVSC as a whole, the Court noted that the settlement “was a business agreement involving the performance of services, designed to benefit the parties” and did not involve “money damages.”

The Court also had to determine if the errors and omissions insurer breached its duty to defend PVSC when it offered to defend only the covered claims in the underlying action brought by Spectraserv while contesting any obligation to defend or indemnify PVSC for what it contended were uncovered claims. The Court held that the insurer “acted appropriately in proffering a defense while preserving its rights through the issuance of reservation of rights letters.” It noted that an insurer “fulfills its defense obligations” to the insured when it issues an appropriate reservation of rights letter, provides a defense on covered claims and refuses to defend uncovered claims while disputing its obligations as to such claims. The Court specifically stated that: “[w]hen a complaint includes both covered and uncovered counts the carrier may refuse defense on the uncovered counts and dispute coverage.” The purpose of this rule is to “protect both parties by ensuring that the insurer does not incur responsibility for uncovered claims, and that the insured is entitled to both defense and indemnity if the dispute is

resolved in its favor.”

The decision was written by Judge Carchman of the Appellate Division who was temporarily assigned to the Court. Joining in the opinion were Justices LaVecchia, Rivera-Soto and Hoens, and Judge Parrillo who was also temporarily assigned from the Appellate Division. Chief Justice Rabner and Justices Long and Albin did not participate in the decision.

The more significant part of the decision may be that which addresses the duty to defend and permits an insurer to provide defense costs only on covered claims while contesting its obligation to defend or indemnify for uncovered claims. Provided the insurer has properly reserved its rights, the Court’s decision seemingly validates an insurer’s decision to pay only for the costs of defending covered claims while leaving uncovered claims to be dealt with by the insured until such time as a judicial determination is made about the respective obligations of the insurer and the insured as to the uncovered claims. For additional information regarding the holding in Passaic Valley Sewerage Commissioners, please contact Kevin E. Wolff or Vincent E. Reilly.