

INSURANCE
COVERAGE &
REGULATION

Anthony J. Piazza, Chair
585.295.4420
apiazza@hblaw.com

Gary H. Abelson
David B. Cabaniss
John R. Casey
William C. Foster
Alexandra M. George
Dennis R. McCoy
Thomas J. O'Connor
Judith M. Sayles
Mark T. Whitford
Joseph A. Wilson

Federal Court Questions New York Contractual Limitations Period

On April 6, 2010, the United States Court of Appeals for the Second Circuit of New York decided *Fabozzi vs. Lexington Insurance Company*. Paul and Annette Fabozzi sued Lexington Insurance Company in Federal District Court for the Eastern District of New York to recover under a homeowner's policy of insurance issued to them covering their ocean-side home on Staten Island. On May 13, 2002, the Fabozzis notified Lexington of structural deterioration of their home, which was allegedly in danger of collapsing. Lexington commenced an investigation, including a request for documents, an engineer's evaluation and an examination under oath of the Fabozzis. On July 29, 2004, Lexington denied coverage, stating that the damage was attributable to "wear and tear, deterioration, inherent vice, latent defect, wet and/or dry rot, as well as earth movement***." On October 29, 2004, the Fabozzis commenced suit.

The policy contained a contractual limitations clause, which read:

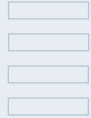
SUIT AGAINST US. No action can be brought unless the policy provisions have been complied with, and the action is started within two years after the date of loss.

Lexington contended that the policy contractual limitations period had expired, and moved to dismiss the suit. The District Court granted Lexington's motion dismissing the action. On appeal, the Fabozzis argued that New York law relating to the contractual limitations was incorrectly applied by the District Court, and, in the alternative, that there were factual issues regarding equitable estoppel.

The Second Circuit Court of Appeals reversed, and held that under New York law, the contractual limitations period did not begin to run at the time of the occurrence. The Court reviewed the history of the first-party contractual limitations in New York beginning with *Steen vs. Niagara Fire Insurance Company*, 89 N.Y. 315, (1882), which "held that generic language setting a contractual limitations period, should be interpreted to start the clock not at the time of the accident itself, but only once 'the right to bring an action exists' - that is, once all conditions precedent have been met***."

The Second Circuit also noted that New York's legislature adopted a standard fire insurance policy in 1887 and again in 1918 which provided that an action had to be commenced "within 12 months next after the fire." Thereafter, in 1943 the standard

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fire insurance policy was modified by the legislature to provide that the limitations period would expire twelve months “after inception of the loss,” in order to accommodate policies which covered risks in addition to fire. In 1966, the New York Court of Appeals construed the standard fire policy limitations period to begin to run upon the occurrence of the insured peril. *Proc vs. Home Insurance Company*, 17 N.Y.2d 239 (1966).

The Second Circuit held:

The phrase ‘after the inception of the loss’ is regarded, in essence, as a term of art which fixes the limitations period to the date of the accident. Other generic language, such as that in the *Fabozzis’* policy, does not carry the same meaning; instead, it ties the limitations period to the moment when a claim accrues.

The Court declined to follow more recent New York Appellate Division decisions which had denied any distinction between the phrase “date of loss” and “after inception of the loss.” The Court noted that *Myers, Smith & Granady, Inc. vs. New York Property Insurance Underwriting Association*, 85 N.Y.2d 832 (1995) involved “highly specific limitations language” which required that the action must be brought “within two years after the date on which the direct physical loss or damage occurred” and was, therefore, consistent with the standard fire policy language.

This Federal Court ruling represents a deviation from New York State courts which have since the enactment of the standard fire insurance policy, consistently applied the two-year contractual limitations as running from the date of loss, regardless of whether the language tracked the standard fire policy, or utilized language such as the “date of loss.” This divergence of opinion between the Federal courts and lower New York courts will likely force the issue to be brought before the New York Court of Appeals for final interpretation. In the meantime, the application of the contractual limitation in New York will depend upon the forum chosen by the plaintiff. ■

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