JENNIFER WILLIS ARLEDGE
Nevada Bar No. 8729
WILSON, ELSER, MOSKOWITZ,
EDELMAN & DICKER LLP
300 South 4th Street, 11th Floor
Las Vegas, NV 89101-6014
(702) 727-1400; Fax (702) 727-1401
jennifer.arledge@wilsonelser.com
Attorneys for Defendants
XL AMERICA, INC., XL INSURANCE AMERICA, INC.,
XL SELECT PROFESSIONAL, PEARL INSURANCE GROUP, LLC,
AND GREENWICH INSURANCE COMPANY

UNITED STATES DISTRICT COURT

DISTRICT OF NEVADA

VICTORIA NELSON, In Her Capacity As The Chapter 7 Trustee Of AMERI-DREAM REALTY, LLC,

Plaintiff,

v.

XL AMERICA, INC., XL INSURANCE AMERICA, INC., XL SELECT PROFESSIONAL, PEARL INSURANCE GROUP, LLC, AND GREENWICH INSURANCE COMPANY

Defendants.

Case No.: 2:16-cv-00060-JAD-GWF

DEFENDANT GREENWICH INSURANCE COMPANY'S REPLY IN SUPPORT OF MOTION TO DISMISS PURSUANT TO FED. R. CIV. PRO. 12(b)(6)

ORAL ARGUMENT REQUESTED

NOW COMES Defendant Greenwich Insurance Company ("Greenwich") by and through its counsel, for its Reply in Support of Its Motion to Dismiss Pursuant to Fed. R. Civ. Pro. 12(b)(6) hereby states as follows:

I. INTRODUCTION

The Trustee attempts to confuse the issues regarding Greenwich's coverage obligations. The analysis in this insurance coverage dispute is two-fold. First did Greenwich have a duty to defend and indemnify Ms. Peladas-Brown in connection with the Adversary Action and the $1,174,373.63 judgment against her for embezzling security deposits. The answer to that inquiry is "no" pursuant to the application of Exclusion D and the prior knowledge provision of the insuring agreement. The second issue is whether Greenwich had a duty to defend and indemnify Mr. Brown and Ameri-

Dream in connection with the Peladas-Brown Adversary Action. The answer to this inquiry is "no" because no claim or lawsuit was ever brought against Mr. Brown and Ameri-Dream, therefore the duty to defend was never triggered. Furthermore, Mr. Brown and Ameri-Dream were adjudicated by a court as having no liability in connection with the $1,174,373.62 loss of security deposits. Moreover, neither Mr. Brown nor Ameri-Dream has any judgment entered against them for which to indemnify as is required by the policy. Simply put, the third-party liability policy issued by Greenwich does not provide first party reimbursement of the lost security deposits as sought by the Trustee. As such, the Trustee's claims for breach of contract, declaratory judgment, bad faith, breach of fiduciary duty and violations of NRS 686A.310 are without merit and should be dismissed.

II. ARGUMENT

A. The Third Party Liability Errors & Omissions Policy Precludes Coverage to Ms. Peladas-Brown for the $1,174,373.63 Judgment Entered in the Peladas-Brown Adversary Action.

The Complaint is clear that the Trustee asserted four claims for relief solely against Ms. Peladas-Brown in her Adversary Action, Adversary Case No. 14-01087-LED. As argued at length in Greenwich's opening brief, coverage for the claims against Ms. Peladas-Brown are not covered under the Greenwich Policy by virtue of the application of Exclusion D of the Policy. As a result of the application of these exclusions, denial of defense and indemnity to Ms. Peladas-Brown was correct and justifiable.

The Trustee's Opposition Brief either intentionally or otherwise confuses the issue of coverage for Ms. Peladas-Brown with the question of whether there is an obligation to provide third-party liability coverage to other insureds who were never sued. Before that argument can be addressed, however, this Court must first consider whether Greenwich's denial of coverage to Ms. Peladas-Brown was appropriate.

Exclusion D of the Policy precludes coverage, both defense and indemnity, for any claims "based on or arising out of":

> **1.** the conversion, commingling, defalcation, misappropriation or improper use of funds or other property;
>
> **2.** the gaining of any personal profit or advantage to which the **Insured** is not legally entitled; or
>
> **3.** the inability or failure to pay, collect or safeguard funds held for others, unless the **insured** is acting in the capacity of a **short term escrow agent**.

///

The allegations in the Peladas-Brown Adversary Action explicitly allege that Ms. Peladas-Brown converted and misappropriated approximately $1.2 million in security deposits that Ameri-Dream was holding for its clients' tenants. The Peladas-Brown Adversary Complaint further alleges that Ms. Peladas-Brown was adjudicated by the Nevada Real Estate Commission to have admitted that the misappropriated funds "were used to support Ms. Peladas-Brown's family and friends in the Philippines…." The Peladas-Brown Adversary Complaint also asserted that Ms. Peladas-Brown "orchestrated various unauthorized transactions … which included the wire transfers of the majority of the Security Deposits to the Philippines."

Furthermore, the Bankruptcy Court entered Findings of Fact and Conclusions of Law in the Peladas-Brown Adversary Action which expressly found that Ms. Peladas-Brown failed to safeguard funds. Specifically, the Bankruptcy Court found, "Under Nevada law, [Ms. Peladas-Brown] is required to safeguard the Security Deposits on behalf of tenants." Ex. C to Motion at ¶10. "The tortious conduct of [Ms. Peladas-Brown] proximately caused the damage to the Company, because the Security Deposits were transferred for no consideration, and [Ms. Peladas-Brown] knew it." Ex. C to Motion at ¶7.

The Trustee argues that Exclusion D of the Policy does not preclude coverage by Greenwich for the claims asserted against Ms. Peladas-Brown. In attempting to now resurrect coverage from her own pleadings, the Trustee ignores that her own complaint sets forth all requisite facts for the application of Exclusion D, i.e. misappropriation of funds and personal profiting. Rather the Trustee now argues that Exclusion D is ambiguous and its application would essentially make the policy illusory. Both of these arguments fail.

First, courts have found the language of Exclusion D unambiguous and applied the exclusion to preclude coverage where the damages arose from the misappropriation of funds, regardless of whether the conduct was negligent or intentional. *See e.g. in Northland Ins. Co. v. Stewart Title Guaranty Co., 327 F.3d 448 (6th Cir.2003)(* court's finding "that any damages sustained as a result of the ... conversion, commingling, defalcation, [or] embezzlement, ... fell within the exclusions of the policy regardless of whether the conduct was negligent or intentional."*); Chicago Title v. Northland Ins. Co.*, 31 So.3d 214 (Fla. App. 2010)(holding that exclusion in errors and omissions policy for losses arising out of the handling of funds applied to title insurer's lawsuit against insured title company arising out of attorney's misappropriation of funds released to him by title company during a real estate transaction, even though the complaint alleged counts for negligence and

negligent supervision; semantics could not avoid the fact that title insurer's damages arose from the misappropriation of funds, and the exclusion did not rely on the identity of the actor).

In *Westport Ins. Co. v. Hanft*, 523 F.Supp.2d 444 (M.D. Penn. 2007), the Court was asked to determine whether a similar exclusion applied to claims against an attorney who misappropriated client funds. In *Hanft,* Exclusion H of the Westport Policy provided that coverage did not apply to "any Claim based upon, arising out of, attributable to, or directly or indirectly resulting from any conversion, misappropriation or improper commingling of client funds." The *Hanft* court specifically analyzed whether the exclusion was ambiguous. The *Hanft* court noted "The terms conversion, misappropriation, and commingling are not defined in the policy. Where a policy uses technical terms, those words are construed in their technical sense unless a contrary intention clearly appears." *Id.* at 459 (citing *Blue Anchor Overall Co. v. Pa. Lumbermens Mut. Ins. Co.*, 385 Pa. 394, 123 A.2d 413, 415 (1956)). The *Hanft* Court found that the exclusion was unambiguous and applied it to preclude coverage for the underlying complaint. *Id.* at 460.

In order to purportedly establish the ambiguity in Exclusion D, the Trustee makes a tortured argument regarding the alleged intertwining of Exclusion C, Exclusion D and the Innocent Insured provision of the Greenwich Policy. The Trustee appears to argue that because Ms. Peladas-Brown's conduct was the ***intentional*** misappropriation of client funds, the Peladas-Brown Adversary Complaint would be precluded by both Exclusion C and Exclusion D, the Greenwich Policy cannot preclude coverage for the Peladas-Brown Adversary Action. This argument is both illogical and offers a tortured reading of the Policy in an attempt to create ambiguity where none exists. Nevertheless, at least one other court has had the opportunity to review this very argument.

In *Fidelity National Title Ins. Co. of New York v. OHIC Ins. Co.*, 275 Ga.App. 55(Ga. App. 2005) a professional liability insurer sought declaratory judgment against title insurance company and title attorney that insurer had no obligation to defend and indemnify attorney, Snead, against claims involving alleged misappropriation of client funds. OHIC relied on Exclusion 4 to deny coverage, which provided that the Policy does not apply to "claims based upon or arising out of conversion, misappropriation, or improper commingling of client funds." The appellate court held that Exclusion 4 unambiguously excludes coverage for all claims arising out of conversion, misappropriation, or improper commingling of client funds.

Like the Trustee here, Fidelity, which was making claims against Snead, argued that two other exclusions of the OHIC policy relating to wrongful conduct conflict with such an absolute reading of Exclusion 4. Exclusion 14 of the OHIC policy excluded coverage for "dishonest,

fraudulent, criminal, malicious or intentionally wrongful acts, but coverage remains applicable for any of you who didn't personally commit or participate or fail to report any such acts", i.e. containing an innocent insured provision for that exclusion. In addition, the OHIC policy contained Exclusion 21 that excluded from coverage "violations by you of any law or regulation imposing criminal penalties or liability arising out of the violation by others, with your consent, of any law or regulation imposing criminal penalties." Fidelity argued, like the Trustee here, that while Exclusion 4 excludes coverage for all acts arising out of conversion, misappropriation or improper commingling of funds, Exclusions 14 and 21 indicate that, even if the claims arise out of such wrongful acts, the individual Fidelity employee nevertheless had coverage under the OHIC policy if she did not personally participate in any such wrongful acts or if she did not consent to criminal violations by others.

The *Fidelity* court held that Fidelity was misreading the OHIC policy. The *Fidelity* court held that the express language of "Exclusion 4 clearly excludes coverage for all claims-with no exceptions-arising out of conversion, misappropriation, or improper commingling of client funds. The fact that the Policy contains additional exclusionary clauses that qualify or limit the exclusions for the more general misconduct described in those particular clauses does not diminish the fact that the exclusion for the misconduct described in Exclusion 4 is unqualified. These other separate clauses do not refer to or attempt in any way to limit the absolute language in Exclusion 4; they simply focus on a type of excluded misconduct that is broader than that described in Exclusion 4."

The *Fidelity* Court went further to note a long line of coverage cases stand for the proposition that each exclusion is meant to be read with the insuring agreement, independently of every other exclusion. *Weedo v. Stone-E-Brick, Inc.*, 81 N.J. 233, 405 A.2d 788, 795(III) (1979)(New Jersey); *Fresard v. Michigan Millers Mut. Ins. Co.*, 414 Mich. 686, 327 N.W.2d 286, 290(III) (1982) (Michigan); *Kay Bee Builders v. Merchant's Mut. Ins. Co.*, 10 A.D.3d 631, 781 N.Y.S.2d 692, 693 (N.Y.App.Div.2004) (New York); *Dodson v. St. Paul Ins. Co.*, 812 P.2d 372, 377 (Okla.1991) (Oklahoma); *John J. Curry & Son v. Harleysville Mut. Ins. Co.*, 11 Pa. D. & C.4th 521, 527 (Pa.Commw.1991) (Pennsylvania); *Nahan v. Pan American Grain Mfg. Co.*, 62 F.Supp.2d 419, 423-424(I) (D.P.R.1999)(Puerto Rico); *Standard Fire Ins. Co. v. Chester-O'Donley & Assoc.*, 972 S.W.2d 1, 8(V) (Tenn.App.1998) (Tennessee); *Heaton v. Mountain*, 233 Wis.2d 154, 607 N.W.2d 322, 325(12) (2000) (Wisconsin); *Qualls v. Country Mut. Ins. Co.*, 123 Ill.App.3d 831, 78 Ill.Dec. 934, 462 N.E.2d 1288, 1291 (1984) (Illinois: exclusions each have an independent purpose); *Harrison Plumbing, etc. v. New Hampshire Ins. Group*, 37 Wash.App. 621, 681 P.2d 875, 880

(1984) (Washington: "Each exclusion refers to the risks insured against in the coverages and not to the other exclusions.").

The *Fidelity* court also pointed out that two other professional malpractice cases involving realtors have addressed exclusionary clauses very similar to those here and have determined that the absolute exclusion regarding claims arising from misappropriation or conversion of funds clearly excluded coverage, despite language in another exclusionary clause that excluded coverage for dishonest, intentional, or criminal acts only if the insured was personally involved or knowledgeable. *See Bankers Multiple Line Ins. Co. v. Pierce*, 20 F.Supp.2d 1004, 1008 (S.D.Miss.1998); *PNA, L.L.C. v. Interstate Ins. Group*, 2003 WL 21488120, 2003 U.S. Dist. LEXIS 11431(II) (E.D.La.2003).

The *Fidelity* court further noted that an "innocent insured" exception applicable to the criminal/dishonesty exclusion is irrelevant to the application of the misappropriation exclusion. The *Fidelity* court noted that the *PNA* case stated:

> Nor does the existence of the "innocent insured" exception to Exclusion B [(the criminal exclusion] make Exclusion C [the misappropriation exclusion)] ambiguous or otherwise unenforceable. Quite simply, although [the insurance company] chose to include such an exception for the conduct encompassed in Exclusion B, it did not choose to do the same with Exclusion C. Accordingly, there are no "multiple interpretations" for Exclusion C.

Id. at *4(II). *See Bankers Multiple Line Ins. Co.*, supra at 1008.

The Trustee argues that if any person or entity that qualifies as an "Insured" did not specifically participate in the alleged dishonest conduct, then the Greenwich Policy would be triggered and required to pay its policy limits regardless of whether any claims were ever made against the purported innocent insured. This argument is illogical and unsupported by the express policy language and the spirit of the third party liability policy.

The *Fidelity* case further explained why the misappropriation of funds exclusion and the criminal/dishonesty exclusion are consistent. In explaining, the *Fidelity* court stated:

> Moreover, these three exclusionary clauses are quite consistent with one another and make sense. As one might expect, the broader range of conduct described in Exclusions 14 and 21 (dishonest, criminal, or intentionally wrongful acts) is not excluded unless the insured personally participated in or consented to the conduct. The more specific conduct described in Exclusion 4 (stealing clients' money), which is a subset of the general conduct described in the other exclusionary clauses, is so reprehensible and far beyond the type of conduct normally covered by legal malpractice insurance that the insurance company understandably sought (and the insured understandably agreed to) its complete exclusion, with no exceptions. In other words, even though criminal or dishonest conduct generally is excluded only if the insured personally participated or consented to the conduct, that subset of criminal or

dishonest misconduct which involves the theft or misappropriation of client funds is so abhorrent and beyond the pale of ethics that it is not covered under any circumstances.

Based on its thorough analysis of the very same ambiguity arguments made by the Trustee here, the *Fidelity* court held that the misappropriation of funds exclusion was unambiguous and applied to preclude coverage. The *Fidelity* court precluded coverage "It is undisputed that Fidelity's claims against Snead "arose out of" the conversion, misappropriation, and commingling of client funds, because the funds were not used for their intended purposes and because but for those actions, there could be no claim against Snead." Likewise, the claims against Ms. Peladas-Brown, as well as the non-existent claims against Mr. Brown and Ameri-Dream, are precluded by Exclusion D of the Policy.

Second, the application of the unambiguous language of Exclusion D would not render the policy illusory. The Trustee argues that because Ameri-Dream was a real estate management company in the business of collecting and safeguarding deposits and rents applying Exclusion D would "cause coverage to be denied in every instance." Opposition Brief at p. 13. The Trustee misconstrues the doctrine of illusory insurance coverage. Insurance coverage is deemed illusory when the insured "receives no benefit" under the policy. *Md. Cas. Co. v. Reeder*, 221 Cal.App.3d 961, 978, 270 Cal.Rptr. 719 (1990); *Mt. Hawley Ins. Co. v. Fed. Sav. & Loan Ins. Corp.*, 695 F.Supp. 469, 484–85 (C.D.Cal.1987) (coverage not illusory where policy covered customer and government claims, but not the underlying action).

The Greenwich Policy provides coverage for a variety of acts or omissions in the performance of "real estate services," which are defined by the policy as services in the insured's capacity as " a real estate agent, real estate broker, leasing agent, property manager, real estate auctioneer, real estate appraiser, real estate consultant or counselor, short term escrow agent, referral agent, notary public, or member of a real estate accreditation, standards review or similar real estate board or committee." There are an innumerable number of acts, errors and omissions in these various capacities that could be covered under the Greenwich policy, that are unrelated to the misappropriation of funds and gaining of personal profit.

B. The Greenwich Third-Party Policy Does Not Provide Defense or Indemnity Coverage For Mr. Brown and Ameri-Dream When Those Insureds Were Never Sued, Have Been Adjudicated That No Liability Attaches to Their Action and No Judgment Was Entered Against Them.

The Trustee argues that even though no claim was made against Mr. Brown or Ameri-Dream and no judgment was entered against them, the claims made and reported third party liability policy

issued by Greenwich is nevertheless required to "reimburse" Ameri-Dream for its loss of security deposits. This argument shows a lack of understanding between first party and third party liability insurance.

A first-party insurance policy, such as life, disability, health, fire, theft, and casualty insurance, provides coverage for loss or damage sustained directly by the insured. A third-party liability policy, such as a comprehensive general liability policy, a directors' and officers' liability policy, or an errors and omissions policy, in contrast, provides coverage for liability of the insured to a third party. In the usual first-party policy, the insurer promises to pay money to the insured upon the happening of an event, the risk of which has been insured against. In the typical third-party liability policy, the carrier assumes a contractual duty to pay judgments that the insured becomes legally obligated to pay as damages because of bodily injury or property damage caused by the insured. The Greenwich Policy is a third-party liability policy by its express and unambiguous terms. *Montrose Chemical Corp. v. Admiral Ins. Co.*, 10 Cal. 4th 645, 42 Cal. Rptr. 2d 324, 913 P.2d 878 (1995), as modified on denial of reh'g, (Aug. 31, 1995); *McKinley v. XL Specialty Ins. Co.*, 131 Cal. App. 4th 1572, 33 Cal. Rptr. 3d 98 (3d Dist. 2005); *San Diego Housing Com'n v. Industrial Indem. Co.*, 68 Cal. App. 4th 526, 80 Cal. Rptr. 2d 393 (4th Dist. 1998), as modified, (Dec. 23, 1998).

The difference in the nature of the risks insured against under first-party property policies and third-party liability policies is also reflected in the differing causation analyses that must be undertaken to determine coverage under each type of policy. The right to coverage in the third-party liability insurance context draws on traditional tort concepts of fault, proximate cause, and duty. This liability analysis differs substantially from the coverage analysis in the first-party property insurance context, which draws on the relationship between perils that are either covered or excluded in the contract. In liability insurance, by insuring for personal liability, and agreeing to cover the insured for his or her own negligence, the insurer agrees to cover the insured for a broader spectrum of risks. Normally, in the third party context, it is the injured third party who initiates the action against the insured. If coverage is ultimately established, it is the insurer that in turn must indemnify the insured. *Montrose Chemical Corp. v. Admiral Ins. Co.*, 10 Cal. 4th 645, 42 Cal. Rptr. 2d 324, 913 P.2d 878 (1995), as modified on denial of reh'g, (Aug. 31, 1995); *San Diego Housing Com'n v. Industrial Indem. Co.*, 68 Cal. App. 4th 526, 80 Cal. Rptr. 2d 393 (4th Dist. 1998), as modified, (Dec. 23, 1998).

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The Complaint sets forth allegations asserting that the Greenwich Policy is a first party policy requiring Greenwich to reimburse Ameri-Dream and Mr. Brown for the lost security policies. For example, the Complaint contains the following allegations:

> 44. To date, the Defendants have not reimbursed the Company for the loss of Security Deposits are required under the Policy.
>
> * * *
>
> 45. The Defendants breached the Policy by not reimbursing the Company for the loss of the Security Deposits.
>
> * * *
>
> 61. The tortious conduct of the Defendants proximately caused damage to the Company because the Company was not reimbursed for the loss of Security Deposits as required by the Policy.
>
> * * *
>
> 72. There exists between the Plaintiff and Defendants a justiciable controversy regarding the rights and obligations of the parties under the Policy, specifically, but not limited to, whether the Policy requires the Defendants to reimburse the Company for the actions of Ms. Peladas-Brown and the loss of the Security Deposits.

The Greenwich Policy is not a first party policy that reimburses the insured directly for loss. As a third party liability policy, the Greenwich Policy provides a defense to an Insured against whom a claim is made and provides indemnity coverage for any "loss" as defined by the Policy. The only claim brought by the Chapter 7 Trustee is the adversary action brought solely against Ms. Peladas-Brown. An objective reading of the Peladas-Brown Adversary Action demonstrates that no claim was made or judgment entered against Mr. Brown or Ameri-Dream Realty. Therefore, Greenwich never had any defense obligation to either Mr. Brown or Ameri-Dream.

Similarly, Greenwich had no indemnity obligation to Ameri-Dream or Mr. Brown. By virtue of the Findings of Fact and Conclusions of Law entered in the Peladas-Brown Action, Mr. Brown and Ameri-Dream Realty are not and cannot be "legally obligated to pay damages" for Ms. Peladas-Brown's activities, which is required to trigger coverage under the Greenwich Policy.

By virtue of the Findings of Facts and Conclusions of Law requested by the Chapter 7 Trustee and entered by the Bankruptcy Court, neither Ameri-Dream Realty and/or Mr. Brown are "legally obligated to pay" the approximate $1.2 million in funds converted by Ms. Peladas-Brown. In addition, the Bankruptcy Court concluded and held that the divorce decree between Ms. Peladas-Brown and Mr. Brown requires Ms. Peladas-Brown to indemnify Mr. Brown and Ameri-Dream Realty against any claims relating to the loss of the Security Deposits. Exhibit C at ¶14. Therefore, because Mr. Brown and Ameri-Dream are not and could not be "legally obligated to pay" the

judgment in the Peladas-Brown Adversary Action, the Insuring Agreements of the Greenwich Policy is not triggered.

Tacitly recognizing her mistake, the Trustee again attempts a tortured reading of the Greenwich Policy in hopes of converting it to a first party policy. The Trustee admits that the only "Insured" sued and for which a judgment was entered is Ms. Peladas-Brown. However, the Trustee argues that the judgment against Ms. Peladas-Brown is a judgment that Mr. Brown and Ameri-Dream are "legally obligated to pay" even though they were expressly adjudicated innocent of any involvement in Ms. Peladas-Brown's activities. The Trustee argues that while no judgment was entered against them and Mr. Brown and Ameri-Dream were adjudicated innocent of any and all liability associated with the embezzlement of the security deposits, this Court should find that they are nevertheless "legally obligated to pay" Ms. Peladas-Brown's judgment and should be insured by Greenwich for that judgment because they are "innocent insureds." This argument is simply illogical.

Similarly, the Trustee's argument that the "Innocent Insured" provision of the Policy would be illusory because you cannot be "legally obligated to pay" and an innocent insured simultaneously. This, again, shows a fundamental misunderstanding of the Policy. The "Innocent Insured" provision of the Policy applies only to the application of the criminal/dishonest exclusion (Exclusion C) and Condition B of the Policy (reporting provision). Thus, in a situation, for example, where multiple insureds are sued in an action, but one insured is accused of engaging in the criminal/dishonest act and the other insured is sued for claims such as negligent supervision the "innocent insured" would be provided coverage. Similarly, the innocent insured provision would provide coverage to an insured that was sued but was unaware that the potential claim was known by other insureds/co-defendants who failed to timely notify Greenwich.

The Peladas-Brown Adversary Complaint could have brought suit against Ms. Peladas-Brown and Mr. Brown and/or Ameri-Dream. It did not. The suit was brought solely against the fraudfeasor who converted and misappropriated security deposits of customers of Ameri-Dream. No claim was brought against Ameri-Dream or Mr. Brown. Therefore, the Greenwich third party liability policy did not respond on behalf of Mr. Brown and Ameri-Dream because there was quite simply nothing to respond to on their behalf.

For the first time, the Trustee now asserts that 931 claims are currently pending against Ameri-Dream in the bankruptcy court, for which no objections are currently pending. The Greenwich Policy is a claims made and reported policy, which expired June 14, 2014. These

purported 931 claims were not tendered to Greenwich during the policy period. More importantly, these purported 931 claims are not at issue in the Trustee's Complaint.

C. Exclusion I, the Insured Versus Insured Exclusion, Precludes Any Coverage for Claims Against Ameri-Dream or Mr. Brown by the Ameri-Dream Chapter 7 Trustee.

The Trustee's Opposition Brief spends a significant amount of time arguing that Exclusion I of the Greenwich Policy, the Insured v. Insured Exclusion, does not apply because the Trustee does not "stand in the shoes" of Ameri-Dream. This argument fails to take into account the Trustee's own allegations in the Complaint. In the Trustee's Fourth Claim for Relief for Violations of NRS 686A.310, the Trustee asserts that Greenwich has violated 686A.310 by "Compelling insureds to institute litigation to recover amounts due under the Policy." The only Plaintiff in this action is "Victoria Nelson, In Her Capacity As The Chapter 7 Trustee of Ameri-Dream Realty, LLC."

The Trustee alleges that she is in fact the "Insured" in Paragraph 67(d) of her own Complaint and seeks recover under a statute that only applies to claims by the Insured. It is dubious at best that the Trustee asks this Court to ignore her own allegations regarding her status of an "Insured" in order to draw very fine distinctions in the cases cited about whether a Chapter 7 Trustee "stands in the shoes" of the Insured. The Complaint itself establishes that the Trustee herein is suing on behalf of the Insured.

Moreover, if the Trustee does not stand in the shoes of Ameri-Dream that begs the question as to the standing she has to her claims against Greenwich in the first place. In Nevada, liability for bad faith is strictly tied to the implied covenant of good faith and fair dealing created by the contractual relationship between the insured and the insurer. *United Fire Ins. Co. v. McClelland*, 780 P.2d 193, 197 (Nev. 1989). An insurer's duty to negotiate settlements in good faith arises directly from the insurance contract. *Allstate Ins. Co. v. Miller*, 212 P.3d 318, 330 (Nev. 2009). Therefore, a party who lacks a contractual relationship with an insurer does not have standing to bring a claim of bad faith. *Gunny v. Allstate Ins. Co.*, 830 P.2d 1335, 1335-36 (Nev. 1992). In Nevada, "[w]here no contract relationship exists, no recovery for bad faith is allowed." *McClelland*, 780 P.2d at 197. Other states may recognize a duty to negotiate in good faith between insurers and third parties, however, Nevada does not recognize such a duty. *Tweet v. Webster*, 610 F. Supp. 104, 105 (D. Nev. 1985); see also Bergerud v. Progressive Cas. Ins., 453 F. Supp. 2d 1241, 1247 (D. Nev. 2006). This holds true for claims under NRS 686A.310A as well. *See Gunny v. Allstate Ins. Co.*, 108 Nev. 344, 436, 830 P.2d 1335 (1992).

Furthermore, while the Trustee cites to several distinguishable cases, her analysis fully ignores the plain language of the Greenwich Policy. Exclusion I of the Policy expressly states that Greenwich will not defend or pay any **claim** "by or on behalf of any **Insured** against any other **Insured.**" The Greenwich Policy defines "**Insured**", in pertinent part, as follows: "4. the estate, heirs, executors, administrators, assigns and legal representatives of an Insured in the event of such Insured's death, incapacity, insolvency or bankruptcy, but only for liability arising out of real estate services performed by or on behalf of the Named Insured prior to such Insured's death, incapacity, insolvency or bankruptcy."

Pursuant to Paragraph 4 of the Greenwich Policy's definition of "Insured", the Chapter 7 Trustee of Ameri-Dream Realty is an "**Insured"** under the Greenwich Policy. The Chapter 7 Trustee is a legal representative of Ameri-Dream Realty as a result of its bankruptcy. The Trustee argues that a Chapter 7 Trustee is " the sole representative of the bankruptcy estate."

D. Coverage for the Peladas-Brown Adversary Action Is Precluded By the Prior Knowledge Provision of the Insuring Agreement.

The Greenwich Policy is a ***claims made and reported policy***, which provides coverage for claims "first made" against the Insured and reported in writing to Greenwich during the period of insurance or extended reporting period. Accordingly, "a predicate to claims-made coverage is that the insured neither knew of a claim nor could have reasonably foreseen that a known circumstance, act or omission might reasonably be expected to be the basis of a claim or suit." Ronald E. Mallen & Jeffrey M. Smith, Legal Malpractice, § 35:14, at 84 (2008 ed.) ("Mallen"). This is the express and unambiguous intent of subparagraph 4 of the Insuring Agreement of the Greenwich Policy.

The Trustee is correct that Greenwich issued two annual claims made and reported policies: policy year June 14, 2012 through June 14, 2013 and policy year June 14, 2013 through June 14, 2014. However, the existence of two annual policies does not negate the prior knowledge provision found in the Insuring Agreement. The purpose of the prior knowledge provision is so an Insured cannot be aware of an act, error or omission but wait for several policy years until the claim is made in order to report it. An insurer issuing a claims made policy, such as the one at issue here, acts reasonably in excluding from coverage, losses which are known at the time the policy incepts or which are so "probable or imminent" that they are "not proper subjects of insurance." Leo R. Russ, Couch on Insurance § 102:8 (3d ed. 2009). *See also Truck Ins. Exch. v. Ashland Oil, Inc.*, 951 F.2d 787, 791 (7th Cir. 1992) (use of prior knowledge exclusions in claims made policies is common and "uncontroversially proper"). Here, the Prior Knowledge Provision of the Insuring Agreement

provides coverage only if "prior to the inception date of this policy, no **Insured** had a basis to believe that such act or omission, or any related act or omission, might reasonably be expected to be the basis of a **claim.**"

Courts repeatedly have held that the language of the prior knowledge provision is unambiguous, proper and applies an objective standard. For example, the United States Court of Appeals for the Ninth Circuit, applying California law and interpreting nearly identical policy language, adopted an objective reasonable person standard for evaluating whether an insured was aware of acts that might be expected to be the basis of a claim. *Weddington v. United National Insurance Co.*, 2009 WL 3028237, at *1-2 ("[T]he use of the phrase 'or could have reasonably foreseen' indicates that coverage is excluded where a claim was foreseeable from a reasonable, objective viewpoint"). The existence of a previously issued claims made and reported policy can not and does not negate the existence and application of the prior knowledge provision in the later issued insurance policy.

Ms. Peladas-Brown was aware of her activities prior to the inception of the 2013-2014 Policy. As such, the prior knowledge provision of the Insuring Agreement applies to preclude coverage.

V. CONCLUSION

WHEREFORE, Defendant Greenwich Insurance Company respectfully request that this Court dismiss the claims against them with prejudice pursuant to Federal Rules of Civil Procedure 12(b)(6) and award any and all other relief this Court deems just and proper.

DATED this 20th day of January, 2017.

WILSON ELSER MOSKOWITZ
EDELMAN & DICKER LLP

Jennifer W. Arledge

JENNIFER WILLIS ARLEDGE
Nevada Bar No. 8729
300 South 4th Street, 11th Floor
Las Vegas, NV 89101-6014
Attorneys for Defendants

CERTIFICATE OF SERVICE

Pursuant to FRCP 5(b), I certify that I am an employee of WILSON ELSER MOSKOWITZ EDELMAN & DICKER LLP, and that on this 20th day of January, 2017, I served a true and correct copy of the foregoing **GREENWICH INSURANCE COMPANY'S REPLY IN SUPPORT OF ITS MOTION TO DISMISS PURSUANT TO FED. R. CIV. PRO. 12(B)(6)** as follows:

☐ by placing same to be deposited for mailing in the United States Mail, in a sealed envelope upon which first class postage was prepaid in Las Vegas, Nevada;

☒ via electronic means by operation of the Court's electronic filing system, upon each party in this case who is registered as an electronic case filing user with the Clerk;

Samuel A. Schwartz, Esq.
Schwartz Flansburg PLLC
Email: sam@nvfirm.com
Attorney for Chapter 7 Trustee, Victoria L. Nelson

☐ via hand-delivery to the addressees listed below;

☐ via facsimile;

☐ by transmitting via email the document listed above to the email address set forth below on this date:

BY: _____
An Employee of
WILSON ELSER MOSKOWITZ EDELMAN & DICKER LLP