

**Capital Z Fin. Servs. Fund II v Health Net, Inc.**

2007 NY Slip Op 34428(U)

February 23, 2007

Supreme Court, New York County

Docket Number: 603375/03

Judge: Helen E. Freedman

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SUPREME COURT OF THE STATE OF NEW YORK — NEW YORK COUNTY

PRESENT: Hon Helen E. Freedman  
Justice

PART 39

CAPITAL 2  
- v -  
HEATH NET

INDEX NO. 603375/03  
MOTION DATE \_\_\_\_\_  
MOTION SEQ. NO. 004  
MOTION CAL. NO. \_\_\_\_\_

The following papers, numbered 1 to \_\_\_\_\_ were read on this motion to/for \_\_\_\_\_

Notice of Motion/ Order to Show Cause — Affidavits — Exhibits ...  
Answering Affidavits — Exhibits \_\_\_\_\_  
Replying Affidavits \_\_\_\_\_

PAPERS NUMBERED

Cross-Motion:  Yes  No

Upon the foregoing papers, it is ordered that this motion **IS DECIDED**  
**IN ACCORDANCE WITH ACCOMPANYING MEMORANDUM DECISION**

**FILED**  
FEB 23 2007  
NEW YORK  
COUNTY CLERK'S OFFICE

Dated: February 23, 2007

H E Freedman  
Hon. Helen E. Freedman *s.c.*

Check one:  FINAL DISPOSITION  NON-FINAL DISPOSITION  
Check if appropriate:  DO NOT POST

MOTION/CASE IS RESPECTFULLY REFERRED TO JUSTICE \_\_\_\_\_ FOR THE FOLLOWING REASON(S):

SUPREME COURT OF THE STATE OF NEW YORK  
COUNTY OF NEW YORK: PART 39

----- X

CAPITAL Z FINANCIAL SERVICES FUND II,  
L.P., a Bermuda limited partnership, CAPITAL Z  
FINANCIAL SERVICES PRIVATE FUND II, L.P.,  
a Bermuda limited partnership, INSURANCE  
PARTNERS, L.P., a Delaware limited partnership,  
and INSURANCE PARTNERS OFFSHORE  
(BERMUDA), L.P., a Bermuda limited partnership,

Index No. 603375/03

Plaintiffs,

- against -

HEALTH NET, INC., a Delaware corporation,

Defendant.

----- X

**FILED**  
FEB 23 2007  
NEW YORK  
CLERKS OFFICE

**HELEN E. FREEDMAN, J.:**

Plaintiffs Capital Z Financial Services Fund II, L.P., Capital Z Financial Services Private Fund II, L.P., Insurance Partners, L.P., and Insurance Partners Offshore (Bermuda), L.P. allege that Foundation Health Systems, Inc. (FHC), the predecessor of defendant Health Net, Inc. (Health Net) (collectively, Cap Z) breached a contract in connection with Cap Z's financing the purchase by Superior National Insurance Company (Superior) of Business Insurance Group (BIG), a collection of four worker's compensation carriers. Cap Z also alleges that Health Net misrepresented the extent of BIG's reserves to cover anticipated worker's compensation claims, and that these misrepresentations caused them to sustain monetary damages.

**Factual Background and Allegations**

Originally, the complaint contained four causes of action for breach of contract, breach of the covenant of good faith and fair dealing, fraudulent inducement, and fraud. Health Net made a pre-answer motion to dismiss the complaint. In a decision dated May 4, 2006 (Prior Decision),

this court dismissed the latter three causes of action, and struck the request in the complaint for punitive damages. Health Net now moves, pursuant to CPLR 3212, for summary judgment dismissing the remaining (breach of contract) cause of action.

That cause of action alleges that Health Net breached express warranties and covenants of the operative Purchase Agreement, executed on May 5, 1998, by intentionally understating BIG's liabilities and the financial health of BIG's "Captive Programs." Paragraph 5.1 of the Purchase Agreement requires Health Net to indemnify Cap Z, as an affiliate of Superior, and hold it harmless with respect to any losses sustained because of the breach of a representation contained in the agreement.

According to the complaint, prior to the execution of the Purchase Agreement, Health Net or BIG obtained a "Reserve Cover" from American Reinsurance Company (American Re). Subsequently, American Re refused to honor its obligations under the Reserve Cover because of Health Net's misrepresentations and omissions. By 2000, BIG's reserve deficiency at the time of the December 1998 closing exceeded \$400 million, and Superior was forced to settle with American Re. On March 3, 2000, California insurance regulators seized Superior's insurance companies, including BIG, after BIG and Superior became insolvent.

In the Prior Decision, this court dismissed the fraud causes of action (third and fourth) on the ground that the "disclaimer" provisions of the Purchase Agreement barred the prosecution of those claims, and documentary evidence entitled Health Net to a pre-answer dismissal. Health Net had not moved for dismissal of the breach of contract cause of action on that ground. It now so moves, arguing that this cause of action should be dismissed because of the agreement's disclaimer provisions, and, for the additional reason that it is time-barred.

## Discussion

The breach of contract/indemnification claim is based solely upon representations regarding the amount of the reserves, as were the now-dismissed fraud causes of action. As previously determined in this action, Delaware law governs the interpretation of the terms of the Purchase Agreement. Under Delaware law, the elements of a breach of contract claim are (1) a contractual obligation, (2) a breach of that obligation by defendant, and (3) resulting damage to plaintiff (*H-M Wexford LLC v Encorp, Inc.*, 832 A2d 129, 140 [Chancery Ct, Del 2003]). Here, the breach of contract is untenable because the Purchase Agreement has not created any contractual obligation predicated upon information regarding the reserves (*id.*).

Section 2.6 (c) of the Agreement (i.e., the “disclaimer clause”) provides that Health Net is making:

“no representation or warranty with respect to . . . the reserves of the Seller Subsidiaries for losses or loss adjustment expenses (including, without limitation, whether such reserves or liabilities are adequate or sufficient).”

When the language of a contract is plain and unambiguous, binding effect should be given to its evident meaning (*Allied Capital Corp. v GC-Sun Holdings, L.P.*, 910 A2d 1020 [Chancery Ct, Del 2006]). Nevertheless, Cap Z argues that this disclaimer is not dispositive in Health Net’s favor, because it applies solely to the December 31, 1997 financials (“12/31/97 Financials”), and this action is based upon claims-related liabilities (i.e., reserve shortfalls) that Cap Z discovered only after the execution of the Purchase Agreement in May 1998, and prior to the closing of the transaction in December 1998. However, the relevant portion of section 2.6 (c) is not limited to the 12/31/97 Financials. It states, in its entirety:

“Notwithstanding any other provision of this Agreement (including Sections 2.6 and 2.7), Seller makes no representation or warranty with respect to (i) the items

set forth in Section 2.6 of the Disclosure Schedule (the 'Listed Items') or (ii) the reserves of the Seller Subsidiaries for losses or loss adjustment expenses (including, without limitation, whether such reserves or liabilities are adequate or sufficient). Purchaser acknowledges that nothing in this Agreement (including Sections 2.6 and 2.7) is intended to, or shall be construed to, provide a guaranty of the adequacy of (i) the Listed Items or (ii) the loss and loss adjustment expense reserves of Seller as shown in the Financial Statements of the STAT Financial Statements."

Cap Z contends that the first sentence impliedly limits the disclaimer to the 12/31/97 Financials, because the second sentence does so. However, the first sentence pertains to representations and warranties, whereas the second sentence pertains to guaranties. The sentences serve different purposes, and there is no basis to construe the first sentence as being limited to the Financials referenced in the second sentence.

While Cap Z argues that Health Net's interpretation is unreasonable because it is reading language that "simply does not exist," the language that does not exist in the first sentence is the words "December 31, 1997 financials." In the absence of ambiguity, contract language is not to be distorted or twisted under the guise of contract construction (*Allied Capital Corp. v GC-Sun Holdings, L.P.*, 910 A2d 1020, *supra*).

Moreover, a contract must be considered as a whole (*Eugene A. Delle Donne & Son, L.P. v Applied Card Sys.*, 821 A2d 885 [Del 2003]). Other sections of the Purchase Agreement support Health Net's interpretation of section 2.6 (c). For example, section 3.6 (a) provides that Superior acknowledged, in entering into the Purchase Agreement, that Health Net has not made:

"any representation or warranty, either express or implied, as to the accuracy or completeness of any of the information (including, without limitation, *any reserve estimates*, projections, forecasts or other forward-looking information) provided or otherwise made available to Purchaser . . . (including, without limitation, in any management presentations, information or offering memorandum, the actuarial report entitled 'An Actuarial Analysis of the Loss and Loss Adjustment Expense Reserves of Business Insurance Group as of December 31, 1997,'

prepared by Milliman & Robertson, Inc. (the 'M&R Report'), supplemental information or other materials or information with respect to any of the above);” (emphasis added).

Section 3.6 (b) provides that Superior agrees that:

“Seller . . . shall not have any liability or responsibility whatsoever to Purchaser . . . on any basis in respect of the specific representations and warranties of Seller set forth in Article II, except as and only to the extent expressly set forth herein with respect to such representations and warranties and subject to the limitations and restrictions contained herein.”

Thus, sections 2.6 (c), 3.6 (a), and 3.6 (b), read both separately and together, manifest the parties’ intent that Health Net would not be liable based upon information supplied as to the amount of the reserves. As stated in the Prior Decision, Cap Z expressly agreed that it was not relying upon any representations as to BIG’s reserves in entering into the acquisition, and that Health Net would not be liable based upon any representations as to BIG’s reserves.

Cap Z also argues that it would be unreasonable to assume that the disclaimer refers to the period after the signing of the Purchase Agreement, because Health Net continued to operate the BIG companies until the closing in December 1998. However, in section 6.3 (a), the purchaser’s representations and warranties are deemed true as of the closing date. That would include section 3.6 (a) of the Purchase Agreement that acknowledges that, in entering into the Purchase Agreement, Health Net has not made any representation or warranty, either express or implied, as to the accuracy or completeness of, among other things, any reserve estimates.

Health Net is entitled to dismissal on its alternate theory that the breach of contract/indemnification claim is time-barred. Under Delaware law, a claim for breach of contract has a three-year statute of limitations (*Certainfeed Corp. v Celotex Corp.*, 2005 WL 217032 [Chancery Ct, Del 2005]; *Fike v Ruger*, 754 A2d 254 [Chancery Ct, Del 1999], *affd* 752

A2d 112 [Del 2000]). Health Net contends that the breach of contract claim accrued in December 1998, when the transaction closed, and Cap Z commenced this action in October 2003.

Cap Z does not opine as to the date of accrual, but argues, that New York law governs, and that, under New York law the breach of contract action is timely. This argument is unpersuasive. Section 8.1 of the Purchase Agreement provides that the laws of Delaware shall govern:

“all issues concerning the validity of this Agreement, the construction of its terms and the interpretation *and enforcement* of the rights and duties of the parties” (emphasis added).

Where the language in an agreement provides that the law of a particular jurisdiction will govern the agreement *and its enforcement*, then the law of that jurisdiction also governs statute of limitations issues (*see Matter of Diamond Waterproofing Sys. v 55 Liberty Owners Corp.*, 4 NY3d 247 [2005]; *Matter of Smith Barney, Harris Upham & Co. v Luckie*, 85 NY2d 193, *rearg denied* 85 NY2d 1033, *cert denied* 516 US 811 [1995]). That New York provides a longer statute of limitations is unavailing to Cap Z because of the specific agreement to proceed under Delaware law (*Boss v American Express Fin. Advisors*, 15 AD3d 306 [1<sup>st</sup> Dept 2005], *affd* 6 NY3d 242 [2006]).

Finally, Health Net argues that if the court does not grant the motion on either the disclaimer or statute of limitations grounds, it should, at a minimum, find that the claim by plaintiff Insurance Partners, L.P. is time-barred, because that entity is a Delaware limited partnership with its principal place of business in Fort Worth, Texas, and thus, the cause of action accrued in either of these two states, thereby implicating New York’s borrowing statute (CPLR 202). Cap Z contends that Health Net’s alleged fraudulent concealment tolled the

limitations periods in this action, and that it did not learn of the full extent of the concealment until the discovery process during Superior's actions against Health Net, which discovery concluded in 2003. As stated in the Prior Decision, the fraudulent concealment argument is belied by paragraph 24 of the complaint itself, which states that Superior and Cap Z questioned the report by the independent actuarial service, Milliman & Robertson, Inc. (M&R Report). Cap Z and it commissioned four opinions regarding its conclusions, and the additional opinions suggested that the M&R Report had underestimated BIG's anticipated liabilities for claims and expenses.

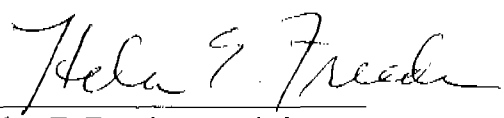
Accordingly, it is

ORDERED that the motion by Health Net, Inc. for summary judgment is granted and the complaint is dismissed with costs and disbursements to Health Net, Inc. as taxed by the Clerk of the Court upon the submission of an appropriate bill of costs; and it is further

ORDERED that the Clerk is directed to enter judgment accordingly.

Dated: February 23, 2007

ENTER:

  
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 Helen E. Freedman, J.S.C.

**FILED**  
 FEB 23 2007  
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