

**Federal Ins. Co. v North Am. Specialty
Assur. Co.**

2008 NY Slip Op 33349(U)

December 5, 2008

Supreme Court, New York County

Docket Number: 603926/05

Judge: Charles E. Ramos

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

PRESENT: CEP

PART 3

Index Number : 603926/2005
FEDERAL INS. CO.
VS.
ALLIED WORLD ASSURNACE CO.
SEQUENCE NUMBER : 002
SUMMARY JUDGMENT

INDEX NO. _____
MOTION DATE _____
MOTION SEQ. NO. _____
MOTION CAL. NO. _____

this motion to/for _____

PAPERS NUMBERED

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

Cross-Motion: Yes No

FILED

DEC 15 2008

COUNTY CLERK'S OFFICE
NEW YORK

Upon the foregoing papers, it is ordered that this motion

IS DISPOSED OF
IN ACCORDANCE WITH THE ACCOMPANYING
MEMORANDUM DECISION

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

Dated: 12/15/08

9
HON. CHARLES E. RAMOS *c.*

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

SUPREME COURT OF THE STATE OF NEW YORK
COUNTY OF NEW YORK:COMMERCIAL DIVISION

-----X
FEDERAL INSURANCE COMPANY, individually and
as subrogee of GALAXY CONTRACTING CORP.,

Plaintiffs,

Index No. 603926/05

- against -

NORTH AMERICAN SPECIALTY ASSURANCE COMPANY,
ALLIED WORLD ASSURANCE COMPANY (U.S.), INC.,
BRUCE A. BENDIX, and RIVKIN RADLER, LLP.,

Defendants.

DEC 15 2008
FEDERAL INSURANCE COMPANY
SPECIALTY INSURANCE
NEW YORK

-----X
Charles Edward Ramos, J.S.C.:

The remaining defendants, North American Specialty Insurance Co. and Allied World Assurance Company (U.S.) Inc. (collectively, "CUIC") move for summary judgment dismissing the complaint, pursuant to CPLR 3212. Plaintiff Federal Insurance Company ("Federal"), individually and as subrogee of Galaxy General Contracting Corp. (individually "Galaxy," and together with Federal, "Plaintiff") cross-moves for summary judgment on its second cause of action, alleging that CUIC acted in bad faith when defending Galaxy in the underlying action.

Federal was the excess insurer for Galaxy in another action (hereinafter, the Bermejo action). Federal claims that CUIC, Galaxy's primary insurer in the Bermejo action, manipulated that case so as to enrich the primary insurer at Federal's expense. In so doing, Federal alleges, that the primary insurer, CUIC, acted in bad faith when it violated the antissubrogation rule, the purpose of which is to prevent an insurer from acting against the interests of its insured. Defendants' primary insurer, which the parties refer to as CUIC, had moved previously to dismiss the

claims against it.

The Appellate Division sustained Federal's claim of bad faith against CUIC, which is now the subject of summary judgment motions by both sides. All other claims were dismissed by this Court or the Appellate Division. See *Federal Ins. Co. v North American Specialty Ins. Co.*, 47 AD3d 52 (1st Dept 2007).

Upon being hired to act as contractor for a construction project, Galaxy purchased two insurance policies from CUIC and one from Federal. One CUIC policy provided Galaxy with primary insurance of up to \$1 million per occurrence. The other CUIC policy provided the owner of the site and two other parties (hereinafter, all will be referred to as the Owners) with primary insurance, also with a limit of \$1 million per occurrence. Both CUIC policies insured against the same risks. The Federal policy provided Galaxy with excess insurance of up to \$10 million per occurrence, once Galaxy's damages exceeded the primary coverage provided by CUIC. For the purposes of this decision, this Court considers CUIC to be the primary carrier for both Galaxy and the Owners.

Rafael Bermejo, an employee of a subcontractor on the project, was injured at work and commenced the Bermejo action against Galaxy and the Owners, alleging violations of Labor Law §§ 240 and 241 (6) and common-law negligence. CUIC undertook to defend Galaxy and the Owners, and assigned their defense to the same law firm, which is not a party here. In February 2002, Bermejo filed a note of issue indicating that his case was ready

for trial.

In June 2002, CUIC requested that Rivkin represent Galaxy in the Bermejo action. Allegedly, the reason for changing attorneys was that CUIC realized that there was a conflict of interest between the Owners and Galaxy.

In December 2002, the Owners moved to amend their answers in the Bermejo action to add cross claims for common-law and contractual indemnification and breach of contract against Galaxy. At the same time, the Owners moved for summary judgment on the indemnity claims. Galaxy, through its counsel, Rivkin, opposed the motion. By order dated March 18, 2003, that court allowed the amendment and awarded the Owners a conditional grant of summary judgment. That court determined that Galaxy, not the Owners, controlled and supervised Bermejo's work and that the Owners did not cause Bermejo's accident. Pursuant to the Labor Law, any liability for Bermejo's accident imputed to the Owners would necessarily be vicarious. Therefore, if a jury determined that the Owners owed Bermejo damages pursuant to the Labor Law statutes, Galaxy would have to indemnify the Owners.

Shortly after that court's decision, Galaxy/Rivkin moved to reargue or renew the Owners' motion on the ground that the antisubrogation rule barred Galaxy from indemnifying the Owners. That court denied the motion because Galaxy should have, but did not, raise the antisubrogation argument in its opposition to the Owners' motion. That court stated that Galaxy had no reasonable excuse for failing to raise the antisubrogation issue at the

appropriate time.

After some negotiations, Bermejo agreed to a \$3 million settlement. Galaxy was the only defendant to enter into the settlement with Bermejo. The Owners' cross claims against Galaxy were not settled. CUIC paid Bermejo \$1 million, the limit of the primary policy it issued for Galaxy. Federal paid \$2 million, pursuant to the excess policy it issued for Galaxy.

According to Federal, it agreed with CUIC that a settlement of \$3 million was reasonable, that if Bermejo's case were tried, the jury would find the Owners and Galaxy liable under the Labor Law statutes, and that the settlement was without prejudice to Federal's right to recover from CUIC. Federal decided not to oppose the settlement when it was made, but to recoup its alleged losses from CUIC in this action.

The gist of Federal's complaint is that CUIC manipulated the litigation in the Bermejo Action so that the settlement was against Galaxy only. If the \$3 million settlement had been against the Owners and Galaxy, CUIC would have paid Bermejo \$2 million: \$1 million on behalf of Galaxy and \$1 million on behalf of the Owners. Federal's excess coverage would have applied to the extent of \$1 million only. But as the settlement involved Galaxy alone, CUIC only had to pay \$1 million and Federal had to pay \$2 million in excess coverage. Federal seeks to recover the \$1 million that it paid on behalf of Galaxy.

Federal also alleges that defendant failed to take any measures to avoid or limit Galaxy's liability to the Owners in

the Bermejo Action. For instance, defendant made no effort during discovery to find evidence that would contribute to Galaxy's defense. Federal argues that CUIC engaged in these practices during the time that the Owners and Galaxy had the same attorneys, as well as after Rivkin became Galaxy's counsel.

Federal further alleges that the settlement was unfair to Galaxy. CUIC caused Galaxy to bear the entire brunt of the settlement. CUIC thus violated the antisubrogation rule, by acting against the interests of its insured, Galaxy. If Rivkin had argued the antisubrogation rule at the proper time, the Owners' claims for indemnity against Galaxy would have been barred, and the settlement would have included the Owners, along with Galaxy.

In order to determine whether Federal has made out a *prima facie* case of bad faith against CUIC, the court must first address subrogation. Subrogation is the equitable doctrine that "allows an insurer to stand in the shoes of its insured and seek indemnification from third parties whose wrongdoing has caused a loss for which the insurer is bound to reimburse" its insured (*Kaf-Kaf, Inc. v Rodless Decorations*, 90 NY2d 654, 660 [1997]; see also *Winkelmann v Excelsior Ins. Co.*, 85 NY2d 577, 581 [1995]). But where the same insurance company provides coverage for the injured and the wrongdoer for the same risk, the insurance company may not recover from the wrongdoer. This is the antisubrogation exception to subrogation. An insurer has no right of subrogation against its own insured for a claim arising

from the very risk for which the insured was covered (*Pennsylvania General Ins. Co. v Austin Powder Co.*, 68 NY2d 465, 471 [1986]). The antisubrogation rule bars the insurer from recovering from its insured up to the policy limits (*Federated Dept. Stores, Inc. v Twin City Fire Ins. Co.*, 28 AD3d 32, 40 [1st Dept 2006]).

The antisubrogation rule is commonly triggered when the insurer provides coverage to both sides of a third-party action for the same incident. Typically, the third-party plaintiff seeks indemnity from the third-party defendant on the ground that the latter actually caused the incident and the former's liability is vicarious (*see Blanco v CVS Corp.*, 18 AD3d 685, 686 [2d Dept 2005]; *Fitch v Turner Constr. Co.*, 241 AD2d 166, 170 [1st Dept 1998]; *Valentin v City of New York*, 187 AD2d 343, 344 [1st Dept 1992], *affd sub nom. North Star Reinsurance Corp. v Continental Ins. Co.*, 82 NY2d 281 [1993]).

The third-party defendant objects that the antisubrogation rule bars the indemnity claim. Given that the insurer may not recoup from the third-party defendant a payment it makes on behalf of the third-party plaintiff, the third-party action will be barred (*id.*). If a third-party plaintiff were permitted to maintain an action against the third-party defendant, it would be compelling their common insurer to demand subrogation from the third-party defendant (*see Valentin*, 187 AD2d at 344).

Important public policy considerations underlie the antisubrogation doctrine. It prevents an insurance company from

passing its loss to its own insured, and thus avoiding the coverage which the insured purchased and paid premiums for (*Jones Lang Wootton USA v LeBoeuf, Lamb, Greene & MacRae*, 243 AD2d 168, 181 [1st Dept 1998]). It also prevents the insurer from encountering a conflict of interest which may inhibit the insurer's incentive to provide a vigorous defense for an insured (*id.*). An insurer able to recover from the third-party defendant-insured will have no incentive to determine the merits of that insured's defense to the claims of the third party-plaintiff-insured (16 Couch on Insurance, § 224:3 [Westlaw 3d ed]). Instead, the insurer has an incentive to fashion the litigation so as to minimize its liability under the policy, and trigger coverage under other policies held by the insured (see *North Star*, 82 NY2d at 296).

Federal asserts that CUIC conducted itself in the litigation so as to ensure that Galaxy, through Federal's policy, paid what the Owners should have paid. CUIC thus avoided paying from the Owners' policy and saved itself \$1 million.

The Appellate Division set forth the state of the law in its opinion sustaining Federal's cause of action for bad faith:

The first cause of action presents a collision of two competing principles: antisubrogation and the right of a party, such as a premises owner, which is only vicariously responsible by virtue of the absolute liability imposed for a violation of Labor Law § 240 (1) (see.g. *Songui v City of New York*, 2 AD3d 706 [2003]), to indemnification from the party actually responsible for the accident (see *Kelly v City of New York*, 32 AD3d 901 [2006]), such as general contractor Galaxy in the instant situation. Even though CUIC issued two separate policies (one to Galaxy and the other to the Owners), the antisubrogation rule is

applicable (*North Star Reins. Corp. v Continental Ins. Co.*, 82 NY2d 281 [1993], *supra*). As the Court of Appeals has made clear, "a potential conflict of interest arises where the insurer that issued both policies seeks indemnification against [one of the parties to which it issued a policy]" (*id.* at 295-296). As relevant here, the Court observed that an insurer could manipulate the litigation in such a way as to "trigger coverage under other insurance policies held by the contractor such as a workers' compensation or excess policy."

Thus, the antisubrogation rule, if asserted, would have defeated the Owners' claims for indemnification from Galaxy. (*Federal Ins. Co. v North American Specialty Ins. Co.*, 47 AD3d 52, 63 [1st Dept. 2007]).

It is clear that by failing to abide by the antisubrogation rule, CUIC kept the Owners out of the settlement, thus reducing the amount of money that CUIC had to pay Bermejo, and increasing the amount that Federal had to pay Bermejo under the excess policy.

Federal may assert a bad faith claim on its own and as subrogee even though the claim rests on the same allegations as the antisubrogation claim. A primary carrier owes its insured and the excess insurer a duty to exercise good faith in handling a claim (*Hartford Acc. and Indem. Co. v Michigan Mut. Ins. Co.*, 93 AD2d 337, 341 [1st Dept 1983], *affd* 61 NY2d 569 [1984]). A *prima facie* case of bad faith must include allegations that the insurer deliberately or recklessly failed to place its insured's interests on an equal footing with its own interests (*see Pavia v State Farm Mut. Auto. Ins. Co.*, 82 NY2d 445, 453 [1993]). The complaint and the moving affidavits sufficiently demonstrate bad faith, *Federal* at 64, in so far as CUIC violated the antisubrogation doctrine by acting against the interests of its

insured Galaxy.

The only question left is to determine if CUIC alleges facts sufficient to establish a defense. The defense appears to be that the events that led up to the settlement of the Bermejo Action happened without any active participation by CUIC. This ignores the fact that CUIC, by taking a position contrary to the antissubrogation doctrine, violated its duty to Federal. It is not required, as CUIC suggests, that its failure to abide by its duty was directed by it.

Nor is a defense established by merely appointing independent counsel. When a primary insurer appoints counsel to defend an excess insurer involved in a suit, the primary insurer is a fiduciary of the excess insurer. *Hartford Acc & Indem Co v Michigan Mut. Ins. Co.*, 93 AD2d 337, 341 (1st Dept 1983), *aff'd*, 61 NY2d 569 (1984) ("the primary carrier owes to the excess insurer the same fiduciary obligation which the primary insurer owes to its insured, namely, a duty to proceed in good faith and in the exercise of honest discretion"). After such appointment has been made, the primary insurer's obligation is not necessarily satisfied. *Feliberty v Damon*, 72 NY2d 112, 117 (1988) ("when an insured has been sued, the insurer does not satisfy its duty to defend merely by designating independent counsel to defend the litigation").

Therefore, although Federal has no claim under the antissubrogation doctrine itself, because of its failure to appeal, the violation of the doctrine is sufficient evidence of

bad faith to warrant entry of judgment, absent an affirmative defense, which is neither effectively pled nor proven.

As the record fails to rebut the prima facia case and otherwise does not contain any extrinsic evidence that would establish a defense, the motion by plaintiff for summary judgment is granted and the cross-motion is denied.

Accordingly, it is;

ORDERED that the clerk is hereby directed to enter judgment in favor of plaintiff against defendants North American Specialty Insurance Co. and Allied World Assurance Company (U.S.) Inc. as prayed for in the complaint.

Dated: December 5, 2008



J.S.C.

HON. CHARLES E. RAMOS

FILED
DEC 15 2008
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