

Allstate Insurance Co. v American Home Assurance Co.

2006 NY Slip Op 30320(U)

February 22, 2006

Supreme Court, New York County

Docket Number: 0602594/2003

Judge: Karla Moskowitz

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2-24-06
(14)

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

PRESENT: Hon. KARLA MOSKOWITZ PART 03
Justice

ALLSTATE INSURANCE CO.,
Plaintiff,

-against-

AMERICAN HOME ASSURANCE CO.,
Defendant.

INDEX NO 602594/2003
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	
_____	_____
_____	_____
_____	_____

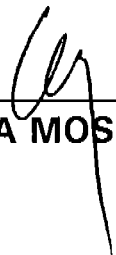
Cross-Motion: Yes No

Upon the foregoing papers, it is

ORDERED that this motion is decided in accordance with the accompanying Decision and Order.

FILED
FEB 22 2006
COUNTY CLERK'S OFFICE
NEW YORK

Dated: February 22, 2006



KARLA MOSKOWITZ J.S.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 : IAS PART 3

-----X
ALLSTATE INSURANCE CO.,

Index No. 602594/2003

Plaintiff,

-against-

DECISION and ORDER

AMERICAN HOME ASSURANCE CO.,

Defendant.
-----X

Moskowitz, J.:

Motion Sequence Numbers 004 and 005 are consolidated for disposition and disposed of in accordance with the following decision and order.

Plaintiff Allstate Insurance Co. (Allstate) moves for partial summary judgment on its first cause of action in the amended complaint for a declaratory judgment (motion sequence 004). It is seeking a declaration that it is not obligated to honor defendant's request for payment under their facultative reinsurance certificates, because defendant's allocation of the settlement proceeds of its underlying insurance policies violates the terms of their reinsurance contracts and is not reasonable or in good faith.

Defendant American Home Assurance Co. (American Home) moves for partial summary judgment on the declaratory judgment cause of action, declaring that its settlement allocation was reasonable and in good faith (motion sequence 005).

This is an insurance dispute between a reinsurer and its insured over the application of the follow-the-fortunes doctrine upon settlement of the underlying case between the reinsured and its insured. The reinsurer's, plaintiff Allstate's, liability is not triggered until the insurer's, American Home's, payment under the commercial property insurance policies issued to its

insured, United Technologies Corp. (UTC), relating to coverage for environmental pollution damages, exceeds \$1 million for any single occurrence or loss. UTC had filed suit against American Home in the early 1990s, and in 2002 the parties reached a comprehensive settlement regarding the insurance coverage for a number of UTC sites. Upon the settlement of that claim, American Home allocated the settlement loss among its primary and reinsurance policies according to a single occurrence per site method. Plaintiff Allstate contends that American Home's allocation of the settlement violated the terms of the reinsurance contracts, because it allocated one occurrence per site, in contrast to the position it took in the underlying litigation, that there were multiple occurrences at a certain site. In response, American Home argues that Allstate is required to follow American Home's post-settlement allocation, whether or not the allocation reflects a position it initially took as to a particular coverage issue, i.e., the number of occurrences, in the underlying insurance dispute. Thus, it contends that the follow-the-fortunes, also known as the follow-the-settlements, doctrine should apply.

BACKGROUND

American Home issued two property insurance policies, IMB 4505377 (the 1975 UTC Policy) and IMB 4512484 (the 1978 UTC Policy), to UTC for the period of 1975-1978 and 1978-1981 respectively (Allstate's Statement of Facts, ¶ 3; exhibits D and E to Affirmation of R. James DeRose, III). The 1975 UTC Policy provided for a UTC self-insured retention of \$200,000, i.e. a deductible, for "any one occurrence," and a limit of liability to American Home of \$6 million for "any one loss, disaster or casualty" (exhibit D to DeRose Affirm., §§ 3 and 4 to UTC Policy Attachment). The policy does not contain any further definition of "occurrence," or "loss, disaster or casualty." The 1978 UTC Policy also provided for a \$200,000 self-insured

retention, but with a \$10 million limit of liability to American Home for “any one loss, disaster or casualty” (exhibit E to DeRose Affirm., §§ 3 and 4 to UTC Policy Attachment). Again, there is no further definition for these terms.

On November 17, 1975, Allstate and American Home entered into a facultative reinsurance agreement, for the same term as the 1975 UTC Policy, pursuant to which Allstate agreed to reinsure American Home for part of the 1975 UTC Policy (1975-78 Allstate Certificate). The policy limit for the 1975 UTC Policy was \$6 million, with two layers for purposes of reinsurance: a \$1 million primary layer, and a \$5 million excess of \$1 million layer (Allstate’s Statement of Facts, ¶ 5). Allstate reinsured 22% of the \$5 million excess of the \$1 million layer (id.; exhibit G to De Rose Affirm.). The 1975-78 Allstate reinsurance certificate states that the “unqualified word ‘loss’ shall mean only such amounts as are actually paid in cash by the Reinsured in settlement of claims” (exhibit G to DeRose Affirm.). It does not contain any other definition of loss or occurrence.

The 1975-78 Allstate Certificate provided, in a combination follow-the-forms and follow-the-fortunes clause, that:

This Certificate is issued as reinsurance and is subject to the same risks, valuations, privileges, clauses and conditions, endorsements (except changes in location), assignments, adjustments and mode of settlement, as are, or were, or may be assumed or adopted by the Reinsured.

Exhibit G to DeRose Affirm., at 2. The 1975-78 Allstate Certificate further provided:

Allstate shall reimburse the Reinsured or its legal representative promptly for loss against which indemnity is herein provided, upon receipt of satisfactory evidence of payment of such loss.

Id.

With respect to the 1978 UTC Policy, Allstate agreed to reinsure American Home for 25% part of the \$5 million per occurrence excess of the \$1 million per occurrence layer (1978-81 Allstate Certificate) (Allstate's Statement of Facts, ¶ 6; exhibit I to DeRose Affirm.). The 1978-81 Allstate Certificate provided, in its follow-the-forms clause, in part:

The liability of Allstate shall follow that of the Company [American Home] and, except as otherwise specifically provided in this certificate, shall be subject to the terms and conditions of the policy(ies) reinsured.

(Exhibit I to DeRose Affirm. at 2). This certificate further provided, in relevant part, in a follow-the settlements clause, that:

All claims involving this reinsurance, when settled by the Company, shall be binding on Allstate, which shall be bound to pay its proportion of such settlements...

Id. As with the 1975-78 Allstate Certificate, this reinsurance certificate does not contain any definition for loss or occurrence.

The UTC Litigation and Settlement

On April 15, 1992, UTC filed an environmental insurance coverage action against American Home in the United States District Court for the District of Connecticut under the 1975 UTC Policy and the 1978 UTC Policy. UTC sought indemnification for environmental pollution claims relating to numerous sites, including UTC's plants in Windsor Locks and Stratford, Connecticut; West Palm Beach, Florida, and Santa Clara County, California, where UTC allegedly sustained property damage (exhibit A to DeRose Affirm., ¶¶ 11-12). The court broke the litigation into phases in view of the numerous sites. A jury trial occurred in 1998 for the Windsor Locks site along with another site. The jury rendered a verdict finding that UTC

proved that it sustained damage to covered property during the policy periods under the 1975 UTC Policy and the 1978 UTC Policy at seven different areas at the Windsor Locks site (exhibit J to DeRose Affirm.).

Following the trial, the parties sought summary judgment regarding the number of occurrences to use to determine the application of the \$200,000 deductibles the insured would have to pay (Allstate's Statement of Facts, ¶ 12). In its motion papers to the District Court, American Home urged that there were multiple occurrences of contamination at the Windsor Locks site for which an additional deductible had to be applied for each separate policy period covered (exhibit 11 to Affirmation of John M. Nonna; see also exhibit k to DeRose Affirm.). On February 10, 1999, the court issued its opinion, finding that "for purposes of calculating deductible amounts under the two American Home policies at issue, seven occurrences of damage or loss took place at the Windsor Locks site consistent with the jury's Phase I verdict" (exhibit K to DeRose Affirm., at 9-10).

American Home filed a motion for a new trial and a petition for interlocutory appeal. The Second Circuit denied the petition and, before the court decided the motion for a new trial, the parties settled.

In January 2002, American Home and UTC settled their coverage dispute, entering into a comprehensive Settlement Agreement and Release in which American Home agreed to pay \$112 million to UTC (exhibit L to DeRose Affirm.) for coverage for environmental losses to various UTC sites identified in Attachment B to the Settlement Agreement. The Settlement Agreement specifically provided that it was a "compromise of disputed claims," and that it did "not constitute an admission by American Home" or by "UTC regarding the claims it has asserted"

(id., ¶ 11). The parties mutually released each other as to any known or unknown claims against each other under or concerning the policies (id., ¶¶ 8-9).

Following the settlement, American Home had its lead coverage counsel in the UTC litigation, William Hassler, perform an analysis for allocating the lump sum settlement amount among the years that the UTC policies covered and the various sites where the alleged damage took place (exhibit M to DeRose Affirm.; exhibit 30 to Nonna Affirm.). Mr Hassler developed a spreadsheet to allocate the UTC settlement, that American Home sent to Allstate with an accompanying letter in which he explained the settlement analysis. The analysis indicates that it evaluated 74 sites, separated into categories for “Tried Sites [from 1998 trial],” “Pending 2nd Trial Sites [sites that had been scheduled for trial in March 2002],” “Dropped Sites in 2nd Amended Complaint [sites dismissed without prejudice in September 1999 in the underlying coverage action],” “Pending Claims vs. American Home [other sites specified in an Attachment A to a letter from UTC purportedly giving notice of claims at those sites],” “Other Sites [specified in Attachment B to same UTC letter],” and “Zero Claim Sites [sites at which UTC’s claimed past and future costs are \$0, but for which it provided notice]” (exhibit 30 to Nonna Affirm., at MIL 00160). The analysis contains a table indicating the amount of UTC’s claims in millions of dollars with respect to each category of sites and the percentage of UTC’s overall claim that each category then represents (id. at MIL 00161). The notes to the table state that UTC’s counsel, who had been in charge of settlement negotiations, provided the numbers for UTC’s claims and that the verdict and court ruling on deductibles/number of occurrences were the basis for the figures for the Windsor Locks site. (id.). The analysis further modified the UTC amount based on the application of one deductible per site per policy year and adjusted the interest

proportionately so the amount of the interest UTC claimed relative to past costs remains constant after application of the deductibles (id. at MIL 00161-00162). The analysis explains the calculation of cost per year, indicating that it calculated the “Allocated Cost” for each site by multiplying the total claim for each site (as modified for deductibles and interest) times 18.4%, the ratio of the settlement (\$112 million) to UTC’s overall claims as modified (approximately \$608 million) (id. at MIL 00154-00155, 00162). The analysis determined the allocated cost per year for each site, as shown in the spreadsheet, by dividing the “Allocated Cost” by the number of years UTC owned or used the site (id. at MIL 00162). Examination of Attachment A-3 of the spreadsheet shows that only four sites exceeded \$1 million per year allocation (id. at MIL 00154-00155). Attachment A-4 of the spreadsheet gives the figures for the total portion of the settlement amount assigned to each policy year, broken down on a site-by-site basis (id. at MIL 00156-00157).

Thus, in its reinsurance allocation, American Home treated each site as one “occurrence” or one “loss, disaster or casualty,” and it ceded, or transferred, the proceeds of the settlement to Allstate as one of its reinsurers on this per site basis.

On March 11, 2003, American Home demanded payment of \$2,578,638.21 from Allstate for its share of American Home’s liability under the underlying policies (exhibit 31 to Nonna Affirm.; exhibit P to DeRose Affirm.). Patrick Parrington, Allstate’s Reinsurance Claim Analyst at the time, reviewed the demand for payment and the documents that American Home sent on the UTC litigation (Allstate Statement of Facts, ¶ 42). Allstate rejected the request for payments under the reinsurance certificates, on the ground that “no single occurrence impacts the excess of \$1M reinsurance layer in any given year” (exhibit O to DeRose Affirm.). Allstate further stated

that American Home's cession failed to reflect its position in the UTC litigation and the court's decision and therefore was unreasonable (*id.*).

In moving for partial summary judgment, Allstate argues that it is not obligated to honor American Home's request for payment, because the manner in which American Home allocated the settlement proceeds, pursuant to the 1975 UTC Policy and the 1978 UTC Policy, was not within the terms of the reinsurance certificates and was unreasonable. Allstate urges that the follow-the-fortunes or the follow-the-settlement clause in the reinsurance certificates does not require Allstate to follow American Home's settlement blindly and does not override the provisions of the reinsurance agreement. Thus, Allstate contends that it is only required to reimburse American Home for the type of loss that is covered by the reinsurance certificates. Allstate asserts that the reinsurance certificates provide that its liability is subject to the terms and conditions, including the definitions, of the underlying insurance policies. Allstate urges that its liability is not triggered until a single occurrence breaches the excess of \$1 million primary layer, and that American Home should have based the settlement allocation analysis on the District Court's 1999 determination of the number of occurrences at the Windsor Locks site and those American Home identified in discovery and pretrial preparation at the West Palm Beach, Stratford and Santa Clara sites. Allstate maintains that the number of occurrences was a core issue during the UTC litigation, and that American Home sought to maximize the number of occurrences per site in order to minimize its liability. Allstate contends that, if the analysis included these number of occurrences, American Home would have no basis to seek any amount from Allstate, because no individual occurrence would have exceeded the \$1 million attachment point of the 1975 and 1978 Certificates.

Allstate further argues that the settlement allocation is unreasonable because it violated the Windsor Lock's court ruling that there were seven occurrences at that site and contrasts with American Home's pretrial position on the other sites.

In opposition and in support of its motion for partial summary judgment, American Home argues that the follow-the-settlements doctrine applies to its post-settlement allocation decision and that the court should not consider Allstate's proposed alternative allocation methodologies. American Home contends that such a review would undermine the certainty required to foster settlements of underlying coverage litigation and would subject American Home to the risk of successive litigations with potentially inconsistent results.

American Home urges that its allocation was reasonable, because its methodology, of treating each site as an occurrence, was reasonable, and its decision to adopt that methodology was made in good faith. American Home asserts that it was reasonable, because treating each site as a single "loss, disaster or casualty" is consistent with industry custom and practice. In support, American Home offers the deposition of Allstate's Senior Claims Consultant, Mr. Parrington, who reviewed American Home's request for reinsurance payment, and who conceded that on other matters he had seen cedents allocating on the basis of one occurrence per pollution site, and that, more often than not, the cessions that he has worked on for pollution matters are done on a one occurrence per site basis (exhibit U to DeRose Affirm., Parrington Dep., at 30-31). American Home further offers the testimony of its Assistant Vice President Irwin Nirenberg, who attested that it was American Home's policy, for purposes of billing reinsurers in environmental claims, to treat each site as an occurrence (exhibit R to DeRose Affirm., Nirenberg Dep., at 103-04).

American Home also contends that its allocation is within the terms of the reinsurance certificates that follow the terms of the underlying policies. It maintains that this is not a case in which American Home is imposing liability on Allstate for risks not encompassed within the underlying policy or the reinsurance certificates, distinguishing Travelers Cas. & Sur. Co. v Certain Underwriters at Lloyd's of London (96 NY2d 583 [2001]). Neither of the reinsurance policies nor the underlying policies contain any definition of either "occurrence" or "loss, disaster or casualty." American Home asserts that its allocation is fully consistent with this policy language and, just because the allocation was not based on the trial court's interlocutory ruling in 1999 concerning the Windsor Locks site (not final before the global settlement and not involving any of the 73 other sites), is not a basis to find the final allocation unreasonable. Finally, American Home contends that there is no evidence of bad faith on its part.

DISCUSSION

The motions for partial summary judgment are granted to the extent that this court declares that American Home's allocation did not violate the terms of the reinsurance certificates and was reasonable and in good faith.

"Reinsurance is a contract by which one insurer insures the risk of another insurer" (Christiania Gen. Ins. Corp. of N.Y. v Great Am. Ins. Co., 979 F2d 268, 271 [2d Cir 1992] [quotations omitted]). It is essentially a contract of indemnity, and by the terms the reinsurer is obligated to indemnify its reinsured subject to the limits of the reinsurance policy (id.). Under a reinsurance contract, the reinsured agrees to pay a premium to the reinsurer, for which the reinsurer assumes the risk of a portion of the reinsured's potential financial exposure under certain direct insurance policies that it has issued to its own insured (North River Ins. Co. v Ace

Am. Reins. Co., 361 F3d 134, 137 [2d Cir 2004]). Insurers are known as cedents with respect to their reinsurance policies, because they transfer or cede their risk and some of their premiums, to the reinsurer (see Travelers Cas. & Sur. Co. v Gerling Global Reins. Corp. of Am., 419 F3d 181, 183 n2 [2d Cir 2005]; Christiania Gen. Ins. Corp. of N.Y. v Great Am. Ins. Co., *supra* at 271).

There are two types of reinsurance, treaty and facultative. "Treaty reinsurance obligates the reinsurer to accept in advance a portion of certain types of risks that the ceding company underwrites" (Christiania Gen. Ins. Corp. of N.Y. v Great Am. Ins. Co., *supra*). Facultative reinsurance, at issue here, "covers only a particular risk or a portion of it, which the reinsurer is free to accept or not" (*id.*, citing Matter of Midland Ins. Co., 79 NY2d 253, 258 [1992]). In facultative reinsurance, it is the underlying policy that defines the scope of the insurer's and the reinsurer's obligations.

Here, the parties entered into facultative reinsurance agreements and Allstate agreed to accept a portion of the risks under the underlying UTC policies.

American Home contends the follow-the-fortunes doctrine governs this dispute and this doctrine applies to its decision allocating the UTC settlement among its layers of reinsurance. Under the follow-the-fortunes doctrine, a reinsurer must indemnify the reinsured for payments reasonably within the terms of the original policy with its insured, even if technically not covered by it (see Christiania Gen. Ins. Corp. of N.Y. v Great Am. Ins. Co., *supra* at 280). Thus, it requires the reinsurer to pay where the insurer's good-faith payment to its insured "is at least arguably within the scope of the insurance coverage that was reinsured" (Mentor Ins. Co. (U.K.) v Brannkasse, 996 F2d 506, 517 [2d Cir 1993] [citation omitted]; North River Ins. Co. v Ace Am. Reins. Co., 361 F3d at 139-40; see also Commercial Union Ins. Co. v Swiss Reins. Am. Corp.

413 F3d 121, 127 [1st Cir 2005] [follow-the-fortunes doctrine “encompasses settlements that are arguably beyond the strict limits of the underlying cedent’s policy”]). Accordingly, a reinsurer can raise objections only where there is collusion or fraud or where the reinsured’s payment to its insured went beyond the scope of the insured’s underlying policy, in this case the policies with UTC.

This doctrine “applies to all outcomes, including settlements and judgments” (North River Ins. Co. v Ace Am. Reins. Co., 361 F3d at 140). The purpose or goal of the follow-the-fortunes doctrine, that sometimes is referred to as the follow-the-settlement doctrine in the settlement context (id. at 137 n2), is to prevent the reinsurer from “second guessing” the insurer’s settlement decisions (Travelers Cas. & Sur. Co. v Gerling Global Reins. Corp. of Am., 419 F3d at 186). The “main rationale for the [follow-the-settlements] doctrine is to foster the goals of maximum coverage and settlement and to prevent courts, through de novo review of the cedent’s decision-making process, from undermining the foundation of the cedent-reinsurer relationship” (id. at 188, quoting North River Ins. Co. v Ace Am. Reins. Co., 361 F3d at 140-41 [internal quotes and brackets omitted]). Without this doctrine, the ceding insurer would not settle with its insured because of a fear that the reinsurer would refuse to reimburse it for that settlement (id.).

In North River Ins. Co. v Ace Am. Reins. Co., supra, a case closely analogous to this one, the court extended the doctrine to prevent a reinsurer from “second guessing” the ceding insurer’s allocation after settlement among multiple reinsurers (id. at 139). North River involved facultative reinsurance certificates with a follow-the-settlements clause that is nearly identical to the one at issue here: “all claims involving this reinsurance, when settled by the Company shall be binding on the Reinsurer, which shall be bound to pay its proportion of such settlements” (id.

at 142). In that case, the cedent had based its allocation to the reinsurer on a different theory than it had relied upon in settlement negotiations with its insured (id.). The reinsurer contended that the insurer should have allocated its settlement to higher layers of insurance in accordance with the cedent's pre-settlement risk analysis, thereby minimizing the reinsurer's risk (id. at 138). The reinsurer claimed that the allocation had to at least be consistent with the theory of allocation that the reinsured used in negotiating the settlement with its insured. The Second Circuit rejected the reinsurer's request for re-allocation, because it would have required the type of "intrusive factual inquiry" into the cedent's settlement negotiations that the doctrine is intended to avoid (id. at 141; see also Travelers Cas. & Sur. Co. v Gerling Global Reins. Corp. of Am., 419 F3d at 189 (post-settlement allocation is subject to follow-the-fortunes, regardless of pre-settlement risk analysis or position implicit in the settlement with the underlying insured).

Allstate asserts three bases for challenging American Home's settlement allocation. First, Allstate claims that the allocation violates the terms of the reinsurance certificates; second, that the allocation was not reasonable; third, that the allocation was not done in good faith. The court addresses each argument in turn.

Allstate's argument that there was a violation of the policy terms is based on the contention that Allstate's liability was not triggered under the terms of the underlying UTC policies, incorporated into the reinsurance certificates, until a single "occurrence" breached the excess of \$1 million primary layer. Allstate further contends that the allocation of the settlement of one occurrence per site per year was not in accordance with the court determination with respect to the Windsor Locks site or with American Home's pretrial position as to three other sites.

Allstate, in moving for summary judgment on the ground that American Home violated the policy terms, bears the burden of making a prima facie showing of a violation and has failed to make this showing. Allstate does not argue that there is an ambiguity in the underlying UTC policies, and, in the context of the issues here, this court finds none. While the terms “occurrence” and “loss, disaster or casualty” have no further definition in either the underlying UTC policies or the reinsurance certificates, the allocation of one occurrence per site is reasonably within the terms of the original policy with UTC (see Christiania Gen. Ins. Corp. of N.Y. v Great Am. Ins. Co., 979 F2d at 280). This is not a case where the reinsurance policy contained a separate definition of loss or disaster and the claimed multiple occurrences occurred at geographically diverse locations, such as across the country, and spanning over decades (cf. Travelers Cas. & Sur. Co. v Certain Underwriters at Lloyd’s of London, 96 NY2d 583, supra [reinsurance treaties contained separate definition of loss/disaster, and allocation did not reasonably fall within that definition where geographically diverse locations, over many decades]; Excess Ins. Co. v Factory Mut. Ins. Co., 3 NY3d 577 [2004] [the courts cannot interpret the follow-the-fortunes clause to require reinsurers to reimburse beyond the stated liability cap in the policy]). Rather, here, there was no definition in the reinsurance certificates at all, and the certificates required Allstate to follow the decisions of American Home. In addition, each occurrence was at a particular geographic site, one of UTC’s plants. Absent a clear limitation in the facultative reinsurance certificates, the principle of congruent liability between American Home, as the cedent, and Allstate, as the reinsurer, that these parties adopted in the follow-the-form and follow-the-settlements clauses, suggests that Allstate’s liability should “follow the gloss (assuming it is reasonable and made in good faith) given to the underlying

policies by the settlement” (American Employers’ Ins. Co. v Swiss Reins. Am. Corp., 413 F3d 129, 137 [1st Cir 2005]). The allocation of one occurrence per site here is arguably within the scope of the reinsured insurance coverage and, therefore, is not a violation of the facultative reinsurance certificates.

American Home simply allocated the settlement loss to the policies that covered that loss, using one of several allocation methods. While clearly a reinsurer cannot be held accountable for a loss the reinsurance policy does not cover (North River Ins. Co. v Ace Am. Reins. Co., 361 F3d at 141), “if a loss is covered by several policies, a good-faith, reasonable allocation among those policies cannot violate their terms” (Travelers Cas. & Sur. Co. v Gerling Global Reins. Corp. of Am., 419 F3d at 194).

The court rejects Allstate’s contention that the allocation was not reasonable because it was contrary to the court decision regarding the Windsor Locks site and to American Home’s pretrial position with regard to three other sites. An allocation is reasonable if it is one of several reasonable allocation possibilities (Travelers Cas. & Sur. Co. v Gerling Global Reins. Corp. of Am., 419 F3d at 189, 194 [in order to trigger the deference due under the follow-the-fortunes doctrine, the settlement must be reasonable]) and is not irrational nor arbitrary (Dalton v Educational Testing Serv., 87 NY2d 384, 389 [1995]).

The Second Circuit Court of Appeals decisions in Travelers Cas. & Sur. Co. v Gerling Global Reins. Corp. of Am. (419 F3d 181) *supra* and North River Ins. Co. v Ace Am. Reins. Co. (361 F3d 134) *supra* are relevant and persuasive. In both cases, the Second Circuit held that the follow-the-settlements doctrine extended to post-settlement allocations and a reinsurer must follow the cedent’s post-settlement allocation, whether or not that allocation reflects a cedent’s

initial position as to the particular coverage issue, here the number of occurrences, in the underlying insurance dispute. In fact, in North River Ins. Co. v Ace Am. Reins. Co., the reinsurer made the identical argument that Allstate makes here, that the allocation must be consistent with the theory of allocation that the insurer used in negotiating the settlement with its insured (see North River Ins. Co. v Ace Am. Reins. Co., 2002 WL 506682, at *2 [SD NY 2002], affd in part, vacated in part on other grounds 361 F3d 134, supra). The court rejected that argument, reasoning that it would require an intrusive factual inquiry into the settlement process, that was precisely what the follow-the-settlements doctrine was designed to prevent (North River Ins. Co. v Ace Am. Reins. Co., 361 F3d at 141). Thus, the court held that the doctrine extended to a cedent's post-settlement allocation decisions, "regardless of whether an inquiry would reveal an inconsistency between that allocation and the cedent's pre-settlement assessments of risk" (id.).

In Travelers Cas. & Sur. Co. v Gerling Global Reins. Corp. of Am. (419 F3d 181, supra), the reinsurer's challenge relied on the difference between the concession the insurer presumably made in settling with its insured, that is, acceptance of a multiple-occurrence position and its post-settlement allocation on a single-occurrence basis. The court applied the follow-the-settlement doctrine, regardless of the cedent's pre-settlement position, "whether that position is articulated in a pre-settlement risk analysis, or implicit in the settlement with the underlying insured" (id. at 188). The court found that the insurer and its insured declined to resolve the occurrence issue in the settlement, and for the court to do so on a challenge to the allocation, it would be engaging in precisely the kind of intrusive factual inquiry the follow-the-settlements doctrine is meant to avoid (id. at 189).

Similarly, here, this court requires Allstate to follow American Home's post-settlement allocation regardless of American Home's pre-settlement position, both in the Windsor Locks site coverage dispute, tried in the district court and in American Home's pretrial position as to the other sites. Otherwise, this court would be engaging in the "intrusive factual inquiry" into American Home's settlement process that the doctrine is designed to prevent (see Travelers Cas. & Sur. Co. v Gerling Global Reins. Corp. of Am., 419 F3d 181, supra; North River Ins. Co. v Ace Am. Reins. Co., 361 F3d 134, supra).

Allstate's attempt to turn this court's attention from these two cases by relying upon Travelers Cas. & Sur. Co. v Certain Underwriters at Lloyd's of London (96 NY2d 583, supra) to contend that the doctrine does not apply to post-settlement decisions, is unavailing. That case is clearly distinguishable on the facts. It involved reinsurance treaties, rather than facultative certificates (id. at 587). In addition, the treaties contained their own definitions of "disaster" and "loss," that were different from the coverage terms in the underlying policies (id.; see Travelers Cas. & Sur. Co. v Gerling Global Reinsurance Corp. of Amer., 419 F3d at 190). Those treaties, therefore, were completely different from the reinsurance certificates here, that do not contain an independent definition of "occurrence." The holding in that case, that the allocation did not fall within the definition in the treaties of "disaster" (id. at 595), is inapposite here.

To the extent that Allstate argues that the jury verdict and the federal district court post verdict ruling in the underlying policy dispute about the Windsor Locks site requires American Home to allocate the settlement on a multiple-occurrence basis, this argument fails. As American Home argues, the district court's decision was subject to an interlocutory appeal (since denied), a pending motion for a new trial and an appeal after a trial decision. Then the parties

settled. That decision was not final under 28 USC § 1291 (see Lummus Co. v Commonwealth Oil Refining Co., 297 F2d 80, 89 [2d Cir 1961], cert denied 368 US 986 [1962]). It appears that the parties never finalized the verdict nor entered final judgment (see exhibit 15 to Nonna Affirm., Deposition of William Hassler, at 57). The verdict and ruling were on appeal and the parties settled them along with all the other sites, claims and issues in the litigation.

American Home's allocation of one occurrence per site per policy year is reasonable, and Allstate has failed to raise any triable issue of fact with respect to it. American Home presented the spreadsheet with its accompanying notes as well as the deposition testimony of William Hassler, who developed the spreadsheet and analysis. This evidence makes clear that the allocation evaluated all of the 74 sites and made an allocation that was one of several reasonable allocation possibilities (see Travelers Cas. & Sur. Co. v Gerling Global Reins. Corp. of Am., 419 F3d at 189). Mr. Hassler separated the sites into various categories based on whether they were tried, pending, dropped or had no claimed value (exhibit 15 to Nonna Affirm., Hassler Dep., at 16; exhibit 30 to Nonna Affirm.). He testified that he reviewed the reinsurance certificates, but that they did not contain any helpful language (exhibit 15 to Nonna Affirm., at 19-20). He assigned costs to the individual sites based on what UTC was claiming (id. at 15-16, 42; see exhibit 30 to Nonna Affirm., at MIL 00161). He stated that he avoided factoring in his own subjective judgments into the value of UTC's claims at the various sites and instead tried to use what he thought of as bright line tests for allocating values to the sites (exhibit 15 to Nonna Affirm., at 36-39). Thus, for example, where possible, he used numbers UTC provided to the Securities and Exchange Commission, where the law required UTC to estimate its past and future damages (id. at 38-39). In addition, where American Home had "iron clad defenses," such

as where UTC did not own the site in certain years, he did not allocate damages for those years (id.). The notes for the spreadsheet indicate that he took the figures for the Windsor Locks site from the verdict and court ruling (id.). This was entirely reasonable, even though American Home was moving for a new trial and planning to appeal the verdict and ruling, because it comported with Mr. Hassler's method of applying bright line tests, rather than his subjective judgment, as to the value and occurrences at that site (see exhibit 15 to Nonna Affirm., Hassler Dep., at 76-789).

Mr Hassler explained that, in the allocation, he first calculated an overall percentage ratio of 18.4% between the settlement amount and the total amount of damages that UTC claimed at all sites (exhibit 30 to Nonna Affirm., at MIL 00159-163). He applied this ratio to each site to get a per site cost, that he then divided evenly over each year of coverage, that is, 11 years (id.). The spreadsheet and accompanying notes indicate that American Home modified the amounts UTC was claiming, applying one deductible per site per policy year, and adjusting for interest proportionately so the amount of interest claimed relative to past costs remained constant after application of the deductibles (exhibit 30 to Nonna Affirm., at MIL 00161; exhibit 15 to Nonna Affirm., Hassler Dep., at 67). The purpose of his using one deductible per policy period was "to assume there would be at least one occurrence per site if there was a claim, and to apply that occurrence across the board to eliminate the smaller sites" (exhibit 15, Hassler Dep., at 67). Mr. Hassler attested that, in doing the analysis, he did not think that he could fairly break down all the sites where the annual per-site amount was in excess of a \$1 million on a per-occurrence basis, and that there were problems if he did that, so he recommended that all the sites be on the one occurrence per site basis (id. at 102-03). Allstate fails to demonstrate that this was unreasonable.

Indeed, Allstate's senior claims consultant, Mr. Parrington, who reviewed American Home's request for payment under these reinsurance certificates, admitted that he has seen cedents allocating on the basis of one occurrence per pollution site, and that, more often than not, the cessions he has worked on for pollution matters were on a one occurrence per site basis (exhibit U to DeRose Affirm., Parrington Dep., at 30-31). That American Home might have selected a different method of allocating the losses does not make the method it did select unreasonable. Accordingly, American Home's settlement allocation was reasonable as a matter of law.

Finally, Allstate has not demonstrated or even raised a triable issue as to American Home's good faith. To demonstrate that a cedent did an allocation in bad faith, the reinsurer must make an "extraordinary showing of a disingenuous or dishonest failure" (Travelers Cas. & Sur. Co. v Gerling Global Reins. Corp. of Am., 419 F3d at 191 [quotation omitted]; North River Ins. Co. v CIGNA Reins. Co., 52 F3d 1194, 1216 [3d Cir 1995]). Bad faith requires a showing of culpability akin to at least recklessness or gross negligence (see Travelers Cas. & Sur. Co. v Gerling Global Reins. Corp. of Am., 419 F3d at 192). A cedent choosing among reasonable allocations is not required to choose the one that minimizes its reinsurance recovery to avoid a finding of bad faith (id. at 193). "An allocation that increases reinsurance recovery – when made in the aftermath of a legitimate settlement and when chosen from multiple possible allocations – would rarely demonstrate bad faith in and of itself" (id.). Allstate's conclusory allegations of bad faith are too insubstantial to raise even a triable issue of fact requiring any further proceedings (id.).

Accordingly, it is

ORDERED that defendant American Home Assurance Co.'s motion (005) for partial

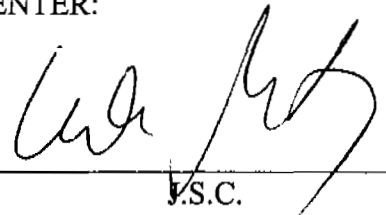
summary judgment on the first cause of action in the Amended Complaint is granted to the extent that it is adjudged, decreed and declared that defendant American Home Assurance Co.'s allocation of the settlement with its underlying insured United Technologies Corp. does not violate the terms of the parties' facultative reinsurance certificates, was reasonable and in good faith; and it is further

ORDERED that plaintiff Allstate Insurance Co.'s motion for partial summary judgment (004) is denied and it is adjudged, decreed and declared that Allstate Insurance is obligated to honor American Home Assurance Co.'s request for payment under the facultative reinsurance certificates.

ORDERED that the remainder of the action is severed and shall continue.

Dated: February 22, 2006

ENTER:



V.S.C.

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COUNTY CLERK'S OFFICE
NEW YORK