

**New Hampshire Ins. Co. v Clearwater Ins. Co.**

2013 NY Slip Op 32812(U)

October 31, 2013

Sup Ct, New York County

Docket Number: 653547/2011

Judge: Ellen M. Coin

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

PRESENT: HON. ELLEN M. COIN

PART 63

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New Hampshire Insurance Company,  
Plaintiff,

INDEX NO. 653547/2011  
MOTION DATE Aug. 28, 2013  
MOTION SEQ. NO. 005  
E-FILED  
DECISION AND ORDER

-against-

Clearwater Insurance Company,  
Defendant.

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The following papers, numbered 1, were read on this motion for summary judgment:

<u>Papers</u>	<u>Papers Numbered</u>
Order to Show Cause-Affidavits-Exhibits	1
Answering Affidavits-Exhibits	2
Reply Affidavits	3
<b>Cross-Motion</b> <b>X No</b>	

Plaintiff New Hampshire Insurance Company (New Hampshire) issued a \$50 million Commercial Excess Umbrella Liability policy to Kaiser Aluminum & Chemical Corporation (Kaiser) in 1973. Defendant Clearwater Insurance Company (Clearwater) reinsured<sup>1</sup> portions of New Hampshire's policy for Kaiser for 1973, 1974 and 1975. (Compl ¶¶5,6,9).<sup>2</sup>

<sup>1</sup>"[R]einsurance is a device whereby an insurance company that has assumed uncomfortable levels of risk buys insurance from another insurance company to assume some of those risks." (*Continental Cas. Co. v Stronghold Ins. Co.*, 77 F3d 16, 19 [2d Cir 1996]). The basic insurer is referred to as the "reinsured", the "ceding insurer" or the "cedent." (*Travelers Cas. & Sur. Co. v Gerling Global Reinsurance Corp.*, 419 F3d 181, 183 n2 [2d Cir 2005]; *Continental Cas. Co.*, 77 F3d at 19).

<sup>2</sup>The original certificate of reinsurance, dated July 10, 1973, named Insurance Company State of Pennsylvania as the ceding

New Hampshire is an affiliate of American International Group, Inc. (AIG). (Nirenberg Aff. ¶1). In the 1970-1985 period AIG-affiliated companies provided insurance coverage to Kaiser totaling approximately \$575 million, including the New Hampshire policy. (Nirenberg Aff. ¶2). Clearwater reinsured the New Hampshire policy as well as other Kaiser policies issued by other AIG-affiliated companies. (Id. ¶3).

Kaiser was the subject of more than 247,000 asbestos bodily injury claims and lawsuits in state and federal courts, alleging that Kaiser designed, manufactured, distributed, marketed and/or sold products containing asbestos. (Ex C to O'Sullivan Aff., ¶41 at 12; Sorkowitz Aff., Ex. 1 at CLGS 0407). After its insurers disputed coverage, Kaiser sued New Hampshire and other AIG-affiliated insurers in California state court. In 2006, New Hampshire and the other AIG-affiliated insurers settled with Kaiser. Since that time, the AIG-affiliated insurers have paid asbestos losses under their policies to Kaiser, based on a ground-up, rising bathtub approach. (Harnadek Aff. 7 at 2).<sup>3</sup>

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company and Skandia Insurance Company Ltd., United States Branch, as reinsurer. An endorsement dated August 8, 1973, amended the ceding company to be New Hampshire. (Ex A to Nirenberg Aff.). Clearwater is formerly known as Odyssey Reinsurance Corporation, Skandia America Reinsurance Corporation, and Skandia Reinsurance Company Ltd., U.S. Branch. (Compl.).

<sup>3</sup>The "rising bathtub" allocation method calls for payments to be allocated on the basis of horizontal exhaustion, which means losses are allocated to the lowest layer of coverage first, and, like a bathtub, fill from the bottom layer up. Under that

When the payment level reached New Hampshire's policy, New Hampshire began to bill Clearwater for its share of New Hampshire's liability.<sup>4</sup> Upon Clearwater's failure to pay, New Hampshire commenced this action.

New Hampshire now moves for summary judgment on its two causes of action: (1) for breach of contract, on the ground that Clearwater has breached the reinsurance agreement by failing to make payment for New Hampshire's losses billed thus far, and (2) for a declaratory judgment that Clearwater is obligated to indemnify New Hampshire for its losses billed and to be billed in the future.

In response, Clearwater urges that this motion is premature. Alternatively, it contends that summary judgment must be denied because (1) New Hampshire failed to give it timely notice as required by the agreement; (2) there are triable issues of fact regarding allocation of the Kaiser settlement; and (3) there are triable issues of fact as to whether New Hampshire retained \$2 million of loss under the policy it issued to Kaiser.

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approach, a given layer of coverage is not implicated until the layer beneath it is completely exhausted. (See e.g. *North River Ins. Co. v Ace Am. Reins. Co.*, 361 F3d 134, 138 n 6 [2d Cir 2004]).

<sup>4</sup>The billings that are the subject of this action commenced on July 20, 2011 (Ex 4 to the Sorkowitz Aff). The parties apparently settled their dispute over billings issued prior to 2011 (Compl ¶12; Plaintiff's Memorandum of Law dated Feb. 15, 2013, n5 at 6).

**LATE NOTICE**

Clearwater's Casualty Facultative Reinsurance Certificate provides that New Hampshire "agrees that it will promptly investigate and will settle or defend all claims under the policy reinsured hereunder **and that it will notify [Clearwater] promptly** of any event or development which [New Hampshire] **reasonably believes might result in a claim against [Clearwater].**" (Ex A to Nirenberg Aff, ¶3(a); emphasis added). The Certificate further provides: "[Clearwater] shall have the right at its own expense to be associated with [New Hampshire] in the defense or control of any claim, suit or proceeding involving or which may involve the reinsurance provided under this Certificate and [New Hampshire] and [Clearwater] agree to cooperate in every respect in the defense and control of each such claim, suit or proceeding." (Id. ¶3(b)).

Clearwater contends that although New Hampshire first received notice from Kaiser referencing its policy in September 1991 (Ex E to Nirenberg Aff), it failed to send notice to Clearwater until April 10, 1997, when its agent sent Clearwater a first notice of claim enclosing a copy of a Notice of Loss dated 02/08/94.<sup>5</sup> (Ex. I to O'Sullivan Aff). Clearwater claims that

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<sup>5</sup>Although the Notice of Loss purports to emanate from "Ins Co Of The State Of PA", it references reinsurance certificate no. 0567, the subject reinsurance policy, originally issued to The Insurance Company of the State of Pennsylvania. (Ex A to Nirenberg Aff.).

even this April 1997 notice was vitiated by New Hampshire's letter three months later, stating, "At this time, it does not appear that our policy will be impacted." (Letter dated July 15, 1997; Ex C to Nierenberg Aff at CLNH 0785). Clearwater argues that since New Hampshire's subsequent communications failed to retract this statement, Clearwater did not receive notice of the claim until March 2010. (Ex L to O'Sullivan Aff.; Chavez Aff ¶5 at 2).

New Hampshire contends that its notice to Clearwater was timely. It points to the Notice of Loss dated 02/08/94 (Nierenberg Aff ¶6 at 3; Ex B)<sup>6</sup> and claims that Clearwater received a report of the Kaiser asbestos exposure in 1997. (Nierenberg Aff, Ex C). Further, in a letter dated April 5, 2000, the Toxic Tort Claims Department of AIG Technical Services, Inc. advised that Kaiser had paid over \$47 million in settlements of asbestos claims and had expended more than \$74 million defending such claims. (Nierenberg Aff, Ex D).

Clearwater submits the affidavit of Theresa A. Chavez, claims manager for Clearwater for the Kaiser claims billed by New Hampshire. She contends that Clearwater does not use information provided by a ceding company under one reinsurance contract to determine whether Clearwater may have exposure under a different

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<sup>6</sup>Significantly, Nierenberg's carefully-worded affidavit does not allege that New Hampshire actually sent the notice to Clearwater in 1994.

reinsurance contract. Thus, Clearwater's position is that unless AIG's notices referred specifically to the New Hampshire policy, they could not constitute notice under the instant reinsurance policy.

New Hampshire's claims manager, Judith A. Harnadek, counters that Chavez told her that Clearwater had one claims person with day-to-day responsibility for all reinsurance claims related to Kaiser. (Harnadek Aff ¶5 at 2). Thus, AIG's notices regarding the status of the Kaiser claim applied to all AIG-affiliated excess carriers, and Clearwater cannot claim ignorance of the notices.

While there appears to be an issue of fact as to whether Clearwater received the 02/08/94 Notice of Loss timely, there is no dispute that it received the April 14, 1997 claim enclosing it. Clearwater fails to provide any support, legal or factual, for its contention that New Hampshire's July 1997 letter vitiated the April notice.

Moreover, a reinsured's breach of a reinsurance agreement's notice provision "will excuse performance only if it is material or demonstrably prejudicial." (*Unigard Sec. Ins. Co. v North Riv. Ins. Co.*, 79 NY2d 576, 584 [1992])). The burden of proving such prejudice is on the reinsurer. (*Id.*).

Prejudice is limited to economic injury. (*Unigard Security Ins. Co., Inc. v North River Ins. Co.*, 4 F3d 1049, 1069 [2d Cir.

1993]; *Matter of Midland Ins. Co.*, 18 Misc3d 1117(A) \*14 n24 [Sup Ct, New York County 2008]). Clearwater argues that it has suffered prejudice because prior to March 2010 (when Clearwater claims that New Hampshire first gave notice), it had commuted outward retrocession contracts that covered the Kaiser claims. (Chavez Aff ¶6 at 2).<sup>7</sup> Clearwater contends that "at least one of Clearwater's retrocessionaires has reserved its right to deny the Kaiser losses based on late notice grounds." (Chavez Aff ¶7 at 3).

It is incumbent upon the party opposing a motion for summary judgment to produce evidentiary proof in admissible form sufficient to require a trial of a material question of fact. (*People v Grasso*, 50 AD3d 535, 545 [1<sup>st</sup> Dept 2008], quoting *Zuckerman v City of New York*, 49 NY2d 557, 562 [1980]). Lacking from Clearwater's submission are any detailed facts to support its claims of prejudice, such as the dates of its commutations, the identity of the retrocessionaires whose contracts it commuted, or the date when Clearwater gave notice to the retrocessionaire now reserving its right of denial. (*Munich*

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<sup>7</sup>In a retrocession agreement a reinsurer cedes all or part of its reinsurance policies to another reinsurer. (*Muhl v Vesta Fire Ins. Corp.*, 288 AD2d 108, 108-109 [1<sup>st</sup> Dept 2001]). "A commutation agreement is a type of settlement agreement through which the retrocessionaires' reinsurance obligations are terminated in return for the retrocessionaires agreeing to pay a stipulated amount to the first level reinsurer...." (*Insurance Co. of State of Pennsylvania v Argonaut Ins. Co.*, 2013 WL 4005109 \*5 [SD NY 2013]).

*Reins. Am., Inc. v American Natl. Ins. Co.*, 2013 WL 1314730 \*12 [D NJ 2013][applying New York law][summary judgment granted dismissing untimely claim submission defense in absence of evidence of prejudice; retrocessionaire failed to demonstrate that it actually took into account number of claims submitted at the time it decided to commute contracts with own retrocedent]; *cf. Insurance Co. of State of Pennsylvania v Argonaut Ins. Co.*, 2013 WL 4005109 at \*12 [reinsurer raised genuine issue of fact as to whether, had it received timely notice from cedent, it would have charged higher prices to its retrocessionaires for commutation agreements]). Thus, Clearwater has failed to meet its burden on this motion to establish prejudice.

Clearwater contends that prejudice is not required to successfully assert a late notice defense when the ceding company (here, New Hampshire) fails to implement routine practices and controls that ensure prompt and timely notification of material facts and developments during the claims handling process. This principle has been enunciated in federal cases. (See *e.g. Unigard Sec. Ins. Co., Inc. v North River Ins. Co.*, 4 F3d 1049, 1069 [2d Cir 1993]; *Christiania Gen. Ins. Corp. v Great Am. Ins. Co.*, 979 F2d 268, 281 [2d Cir 1992]). However, it has not been implemented by the courts of this state.

To the extent that *Christiania* relied on New York law, its citations were not in the reinsurance context or in the context

of notice. Instead, they involved primary insurers placing their interests above those of excess insurers. (*St. Paul Fire & Mar. Ins. Co. v U.S. Fid. & Guar. Co.*, 43 NY2d 977 [1978] [primary carrier refusing to settle claim in excess of its policy limits after liability determined by jury, putting excess carrier alone at further risk]; *Hartford Acc. & Indem. Co. v Michigan Mut. Ins. Co.*, 93 AD2d 337 [1<sup>st</sup> Dept 1983] [primary insurer's failure to proceed against employer, avoiding additional liability under its separate employer's liability coverage, at expense of interests of excess carrier]).

In the reinsurance context, in contrast, the interests of a reinsurer and the primary insurer with respect to a pending claim are generally identical. (*Unigard Sec. Ins. Co.*, 79 NY2d at 583). "[T]he interests of both parties are furthered through the primary insurer's efficient investigation and defense of the claim and through the resolution of the claim on the best terms possible." (*Id.*). Were this Court to apply the federal bad faith exception, Clearwater has failed to produce any evidence of New Hampshire's bad faith. Nor has Clearwater shown through affidavits submitted in opposition to the instant motion that facts essential to justify its contention may exist (CPLR 3212(f)).

Accordingly, Clearwater's Second Affirmative Defense (alleging the absence of practices and procedures to ensure

timely notice) and Third Affirmative Defense (untimely notice) are dismissed.

#### **RETENTION**

Clearwater contends that there are issues of fact regarding whether New Hampshire met an alleged retention warranty under the reinsurance contract. However, it fails to support its contention with any facts. Moreover, Clearwater's contention is rebutted by the sworn allegation that New Hampshire retained more than \$2 million of liability on the Kaiser policy (Harnadek Aff ¶6 at 2). Thus, there is no issue of fact regarding retention, and Clearwater's Seventh Affirmative Defense of breach of the retention warranty must be dismissed.

#### **THE SETTLEMENT**

The subject Reinsurance Certificate provided:  
"[Clearwater]'s liability under this Casualty Facultative Reinsurance Certificate...shall follow the ceding Company's...liability in accordance with the terms and conditions of the policy reinsured hereunder except with respect to those terms and/or conditions as may be inconsistent with the terms of this Certificate." (Ex A to the Nierenberg Aff., ¶1). Clearwater claims that this clause is a "follow the form" clause, not a "follow the fortunes" or "follow the settlements" provision.<sup>8</sup>

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<sup>8</sup>The terms "follow the fortunes" and "follow the settlements" are synonymous. (See e.g. *U.S. Fidelity & Guar. Co. v American Re-Insurance Co.*, 20 NY3d 407, 418 [2013]).

Clearwater made the same contention as to this exact language in another case brought by an AIG-related cedent against Clearwater as reinsurer, *Lexington Ins. Co. v Clearwater Ins. Co.* (2011 WL 3715546 [Super Ct Mass 2011]). The Massachusetts court squarely held that "the [certificate] can be reasonably interpreted as including a 'follow the fortunes' or 'follow the settlements' provision." (2011 WL 3715546 at \*3). Under principles of collateral estoppel Clearwater cannot relitigate the import of the identical language at issue here. (*Ryan v New York Tel. Co.*, 62 NY2d 494, 500-501 [1984]).

A "follow the settlements" clause requires deference to a cedent's decisions on allocation. (*U.S. Fidelity & Guar. Co. v American Re-Insurance Co.*, 20 NY3d 407, 419 [2013]). Clearwater concedes that the doctrine is designed to protect the cedent by prohibiting the reinsurer, its contractual partner, from second guessing the cedent's reasonable and good faith settlement and allocation decisions. However, it argues that it should not apply to such decisions made by AIG at the corporate level rather than by New Hampshire itself.

Clearwater fails to cite any authority for this contention. Moreover, its argument ignores another basis for the deference required by a "follow the settlements" clause: "To review each decision de novo would invite long litigation over complex issues that courts may not be well equipped to resolve, creating cost

and uncertainty and making the reinsurance market less efficient." (*Id.*, 20 NY3d at 419).

However, a cedent's allocation decisions, while entitled to deference, are not immune from scrutiny. A reinsurer is bound only by a cedent's "good faith" decisions. (*Id.*, 20 NY3d at 420). (See e.g. *Travelers Cas. & Sur. Co. v Certain Underwriters at Lloyd's of London*, 96 NY2d 583, 596-597 [2001][follow the settlements clause will not permit cedent to allocate to reinsurer losses not covered by reinsurance treaty]).

A cedent's allocation of a settlement for reinsurance purposes will be binding on a reinsurer if, but only if, it is objectively reasonable. To be "reasonable," "[t]he reinsured's allocation must be one that the parties to the settlement of the underlying insurance claims might reasonably have arrived at in arm's length negotiations if the reinsurance did not exist."

(*U.S. Fidelity & Guar. Co.*, 20 NY3d at 420)

Clearwater does not dispute the bathtub method of allocation, but rather the nature of the claims to which the settlement was allocated. Thus, it argues that AIG allocated the entire settlement to asbestos products claims, but nothing to (1) the bad faith claims asserted by Kaiser against AIG affiliates Lexington Insurance Company ("Lexington") and the Insurance Company of the State of Pennsylvania ("ICOP"), (2) the asbestos premises claims which could implicate Lexington, (3) defense

costs under the ICOP policy, and (4) other claims expressly released in the Kaiser settlement.

New Hampshire urges that the issue here is whether the payments it made are binding on Clearwater under the reinsurance contract that covers the New Hampshire policy. However, the settlement of the California Kaiser actions was a global settlement between Kaiser, on the one hand, and the "AIG Parties," on the other. The AIG Parties are defined in the agreement as including New Hampshire and six other AIG member companies, plus AIG. (Settlement Agreement, ¶1 D, E; Ex L to the O'Sullivan Aff at CLNH 1105). Significantly, the settlement agreement gave the AIG member companies the right to allocate the lump sum settlement amount solely for "its" own purposes in "its" own books and records. (Settlement Agt, ¶II F at CLNH 1116).

Clearwater offers an undated New Hampshire Memorandum requesting authority to settle the Kaiser claims (Ex T to the O'Sullivan Aff) in support of its argument that New Hampshire's allocation to it of the global AIG settlement may not have been reasonable. The Memorandum indicates that all claims, including non-products exposure through operations and/or premises claims (which "would not be subject to aggregate limits"), would be eliminated by the settlement. In addition, it notes that the settlement avoids payment under "certain" policies of defense costs in addition to policy limits. (Ex T to the O'Sullivan Aff

at CHARTIS - GS0027285).

The settlement agreement, giving the AIG member companies carte blanche to allocate the gross settlement amount, coupled with the memorandum requesting authority to settle, are evidence from which a factfinder could conclude that the allocation of the settlement to Clearwater was unreasonable. Significantly, New Hampshire has failed to come forth with affidavit proof sufficient to establish that the allocation of the settlement did not unduly burden Clearwater with amounts attributable to policies of other AIG carriers. Discovery, although stayed by this motion, is in its infancy. Clearwater's contentions regarding components of the Kaiser-AIG settlement raise triable issues of fact sufficient to warrant denial of summary judgment on this issue. (See e.g. *United States Fid. & Guar. Co.*, 20 NY3d at 425, 426).

In accordance with the foregoing, it is

ORDERED that the motion for summary judgment is granted to the extent that defendant's Second, Third and Seventh Affirmative Defenses are dismissed, and the motion is otherwise denied; and it is further

ORDERED that counsel are directed to appear for a preliminary conference in Room 311, 71 Thomas Street, on November 12, 2013 at 2:00 P.M.

Dated: October 31, 2013

*EMC*

Ellen M. Coin, A.J.S.C.

**Non-final disposition**