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United States District Court
For the Northern District of California

IN THE UNITED STATES DISTRICT COURT
FOR THE NORTHERN DISTRICT OF CALIFORNIA

AMERICAN MOTORISTS INSURANCE COMPANY,
an Illinois corporation, as
successor-in-interest to Specialty
National Insurance Company, an
Illinois corporation,

Plaintiff,

v.

AMERICAN RE-INSURANCE COMPANY, a
Delaware corporation,

Defendant.

No. C 05-5202 CW

ORDER GRANTING IN
PART DEFENDANT'S
MOTION FOR
PARTIAL SUMMARY
JUDGMENT AND
DENYING
PLAINTIFF'S
CROSS-MOTION FOR
SUMMARY JUDGMENT

_____ /

Defendant American Re-Insurance Company (American Re) moves for partial summary judgment on two issues: (1) that the retrocession agreement¹ entered into by American Re and Plaintiff American Motorists Insurance Company (AMICO) is not subject to a "follow the fortunes" clause; and (2) that AMICO's bad faith claim fails as a matter of law. Plaintiff opposes the motion and cross-moves for summary judgment on all claims.² Defendant opposes

¹Retrocession coverage is the reinsurance of a reinsurance policy.

²AMICO's motion is captioned as a cross-motion for partial summary judgment, but states that it seeks summary judgment "on all counts of the Second Amended Complaint." Plaintiff's Opposition and Cross-Motion at 1.

1 Plaintiff's cross-motion.³ The matter was heard on April 20, 2007.
2 Having considered all of the papers filed by the parties, the
3 evidence cited therein and oral argument on the motions, the Court
4 grants in part Defendant's motion for partial summary judgment and
5 denies Plaintiff's cross-motion for summary judgment.

6 BACKGROUND

7 This dispute arises out of a certificate of facultative
8 reinsurance⁴ (the American Re agreement) issued by Defendant
9 American Re to Specialty National Insurance (SNIC), the predecessor
10 in interest to Plaintiff AMICO. The American Re agreement was
11 issued to provide 100% reinsurance for a certificate of insurance
12 issued by SNIC (the SNIC certificate) to the Montana Municipal
13 Insurance Authority (MMIA), a municipal insurance pool that
14 provides insurance to its member entities, including the city of
15 Great Falls, Montana.⁵

16 _____
17 ³Defendant argues that Plaintiff's cross-motion should be
18 limited to the claims Defendant raised in its original motion for
19 summary judgment, citing In re Rothery, 143 F.3d 546, 549 (9th Cir.
20 1998). In the alternative, Defendant seeks leave to file
21 additional briefing and evidence in opposition to Plaintiff's
22 cross-motion. However, Rothery requires only that the opposing
23 party have a "full and fair opportunity to ventilate the issues in
24 the motion," which Defendant has had. Id. If Defendant required
25 additional time or pages in which to respond to Plaintiff's cross-
26 motion it should have moved for such prior to the date its
27 reply/opposition brief was due.

28 ⁴"There are two basic types of reinsurance policies--
29 facultative and treaty. . . . In facultative reinsurance, a ceding
30 insurer purchases reinsurance for a part, or all, of a single
31 insurance policy. Treaty reinsurance covers specified classes of a
32 ceding insurer's policies." Unigard Sec. Ins. Co., Inc. v. North
33 River Ins. Co., 4 F.3d 1049, 1053-54 (2d Cir. 1993).

34 ⁵MMIA obtained its policy with SNIC through the National
35 Public Entities Excess Program (NPX), a liability reinsurance risk
36 purchasing group. The parties note that another policy, the

1 The underlying MMIA policy provides cities with coverage for
2 their statutory liability of \$750,000 for each claim and \$1.5
3 million for each occurrence for tort actions against them, and up
4 to \$10 million for claims that do not fall within the Montana state
5 tort cap, but otherwise fall within the scope of coverage under the
6 policy. Montana Code § 2-9-108 provides, "The state, a county,
7 municipality, taxing district, or any other political subdivision
8 of the state is not liable in tort action for damages suffered as a
9 result of an act or omission of an officer, agent, or employee of
10 that entity in excess of \$750,000 for each claim and \$1.5 million
11 for each occurrence." Mont. Code Ann. § 2-9-103(1). Further, the
12 code states, "An insurer is not liable for excess damages unless
13 the insurer specifically agrees by written endorsement to provide
14 coverage to the governmental agency involved in amounts in excess
15 of a limitation stated in this section, in which case the insurer
16 may not claim the benefits of the limitation specifically waived."
17 Id. at § 2-9-108(3).

18 Defendant states that the SNIC policy provides reinsurance for
19 MMIA's \$10 million "non-tort cap related" exposure in excess of
20 MMIA's \$750,000 per person and \$1.5 million per occurrence
21 retention for claims falling within Montana's statutory cap. As
22 discussed below, Defendant's position is that the SNIC policy was a
23 reinsurance policy that did not provide any excess liability
24 coverage; thus, the policy was not sufficient to waive the

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26 American Protective Insurance Company (AMPICO) policy, might also
27 have been in effect, providing coverage to MMIA through NPX at the
28 time of the underlying claim.

1 statutory tort cap pursuant to Montana Code § 2-9-108. Plaintiff
2 concedes that the insurance policy it issued to MMIA was on a
3 reinsurance form but claims that it was an excess policy.

4 On March 10, 2001, when all of the agreements mentioned above
5 were in effect, Jeremy Parsons suffered a severe brain injury at
6 the Cascade County Fairgrounds in Great Falls, Montana, when a
7 steel beam fell off of a concrete pillar, crushing his head and
8 face. Parsons filed a claim with MMIA in April, 2001, alleging
9 that the beam was maintained by the City of Great Falls. On August
10 13, 2001, MMIA provided its "first report of potential excess
11 claim" to its reinsurer, SNIC.

12 On July 23, 2002, Parsons filed a complaint for declaratory
13 relief in Montana state court, seeking damages in excess of the
14 Montana statutory cap and challenging the constitutionality of the
15 cap. On August 13, 2002, Parsons' attorney informed SNIC that
16 because it had repeatedly failed to respond to Parsons' requests
17 seeking confirmation that SNIC provided excess liability coverage
18 to the City of Great Falls, he would amend the complaint joining
19 SNIC as a defendant. The amended complaint also sought a
20 declaration of the nature and extent of coverage under the SNIC
21 policy. At that point, MMIA had paid Parsons \$750,000, exhausting
22 its \$750,000 policy limit.

23 After receiving the amended complaint, SNIC sought a coverage
24 opinion from Curtis Drake, the attorney representing the City of
25 Great Falls, asking whether the statutory cap on damages applied to
26 the SNIC certificate. On September 10, 2001, Drake stated that the
27 cap likely would not apply to SNIC because its policy "specifically
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1 provides coverage for damages in excess of" the statutory
2 limitations. Craig Declaration, Exhibit M. However, Drake noted
3 that he had not received or reviewed any of the correspondence
4 between the parties or the SNIC certificate before offering his
5 opinion. On October 21, 2001, Drake filed an answer on behalf of
6 SNIC, admitting that the SNIC policy provided coverage of up to \$10
7 million in excess of the coverage provided by MMIA.

8 In June, 2002, SNIC prepared a Major Loss Report (MLR) for the
9 Parsons claim. In December, 2002, SNIC prepared a second MLR.
10 Defendant alleges that it first learned of the claim when it
11 received the December, 2002 MLR on March 31, 2003. However,
12 Plaintiff provides evidence that it faxed the Parsons complaint to
13 Defendant's claims representative as early as February 6, 2002.
14 Further, one of Defendant's own exhibits clearly states, "American
15 Reinsurance has been aware of this claim since approximately August
16 2001" and "Drake forwarded the Answer for review before it was
17 filed. Therefore, American Reinsurance had an opportunity to
18 consider this issue when the Answer was filed in October 2002."
19 Craig Declaration, Exhibit S at 1.

20 On May 15, 2003, Defendant notified Plaintiff that it believed
21 that Drake had a conflict of interest in representing both the City
22 of Great Falls and SNIC, and that SNIC should retain coverage
23 counsel. Therefore, SNIC retained Susan Roy to answer the Second
24 Amended Complaint filed May 1, 2003. Roy was instructed by SNIC
25 and American Re that the SNIC certificate "is a reinsurance policy
26 to MMIA and not an excess policy for claims against members in the
27 MMIA pool." Id. However, Roy expressed concerns about SNIC

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1 changing its position with respect to its policy. She stated,

2 It's our opinion that no amount of tweaking or word
3 smithing will mitigate the inconsistency which will be
4 apparent. [SNIC] made a judicial admission that it is
5 excess insurance and is now changing that admission. . .
6 Since excess insurance and reinsurance are completely
7 different, Specialty National cannot argue in good faith
8 that its reference to excess insurance actually meant
9 reinsurance.

10 Id. at 2-3. Further, Roy stated, "It is not as if we are
11 considering the policy without a context . . . At no time has
12 anyone asserted that this policy is reinsurance to reimburse MMIA
13 for any amounts it might pay above the self-insured retention,
14 which it would not because its limits match the self-insured
15 retention. Rather, the file is replete with references to excess
16 insurance." Id. at 3-4. Therefore, Roy recommended that SNIC not
17 change its position and stated that it likely would face bad faith
18 exposure if it did so. This same letter indicated that American Re
19 had been aware of the claim since at least August, 2001 and that it
20 had an opportunity to respond to the answer to the original
21 complaint drafted by Drake.

22 On August 26, 2003, Defendant notified Plaintiff that it
23 reserved its rights to disclaim any liability that Plaintiff
24 incurred due to its decision to "handle the claim as if it provided
25 direct excess liability coverage." Craig Declaration, Exhibit T.
26 Defendant also asserted that it "received first notice of this
27 matter on March 30, 2003." Id. Defendant asserts that Plaintiff
28 decided to stop communicating with it regarding the litigation.
Plaintiff asserts that it explained to Defendant that this decision
was based on concerns that communications between the two would not

1 be protected by the attorney-client privilege. In December, 2003,
2 on the advice of several attorneys who predicted a significantly
3 worse result at trial, Plaintiff settled with Parsons for \$4.5
4 million. Defendant denied Plaintiff's claim for indemnification.

5 Plaintiff initially filed this case on December 15, 2005,
6 after attempts to resolve the dispute without litigation. On
7 December 22, 2005, Plaintiff filed an amended complaint as a matter
8 of right and on February 2, 2006, the Court granted Plaintiff's
9 motion for leave to file an amended complaint after Plaintiff
10 obtained new counsel. Plaintiff alleges that "American Re is
11 obligated to indemnify Plaintiff for the Parsons Loss under the
12 AmRe Agreement, 'follow the fortunes' doctrine, and duty of good
13 faith and fair dealing." SAC ¶ 35. Therefore, Plaintiff seeks
14 relief on three causes of action: (1) declaratory relief regarding
15 the respective rights and obligations of the parties under the
16 American Re agreement; (2) breach of contract; and (3) breach of
17 the covenant of good faith and fair dealing.

18 LEGAL STANDARD

19 Summary judgment is properly granted when no genuine and
20 disputed issues of material fact remain, and when, viewing the
21 evidence most favorably to the non-moving party, the movant is
22 clearly entitled to prevail as a matter of law. Fed. R. Civ. P.
23 56; Celotex Corp. v. Catrett, 477 U.S. 317, 322-23 (1986);
24 Eisenberg v. Ins. Co. of N. Am., 815 F.2d 1285, 1288-89 (9th Cir.
25 1987).

26 The moving party bears the burden of showing that there is no
27 material factual dispute. Therefore, the court must regard as true
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1 the opposing party's evidence, if supported by affidavits or other
2 evidentiary material. Celotex, 477 U.S. at 324; Eisenberg, 815
3 F.2d at 1289. The court must draw all reasonable inferences in
4 favor of the party against whom summary judgment is sought.
5 Matsushita Elec. Indus. Co. v. Zenith Radio Corp., 475 U.S. 574,
6 587 (1986); Intel Corp. v. Hartford Accident & Indem. Co., 952 F.2d
7 1551, 1558 (9th Cir. 1991).

8 Material facts which would preclude entry of summary judgment
9 are those which, under applicable substantive law, may affect the
10 outcome of the case. The substantive law will identify which facts
11 are material. Anderson v. Liberty Lobby, Inc., 477 U.S. 242, 248
12 (1986).

13 Where the moving party does not bear the burden of proof on an
14 issue at trial, the moving party may discharge its burden of
15 production by either of two methods. Nissan Fire & Marine Ins.
16 Co., Ltd., v. Fritz Cos., Inc., 210 F.3d 1099, 1106 (9th Cir.
17 2000).

18 The moving party may produce evidence negating an
19 essential element of the nonmoving party's case, or,
20 after suitable discovery, the moving party may show that
21 the nonmoving party does not have enough evidence of an
22 essential element of its claim or defense to carry its
23 ultimate burden of persuasion at trial.

24 Id.

25 If the moving party discharges its burden by showing an
26 absence of evidence to support an essential element of a claim or
27 defense, it is not required to produce evidence showing the absence
28 of a material fact on such issues, or to support its motion with
evidence negating the non-moving party's claim. Id.; see also

1 Lujan v. Nat'l Wildlife Fed'n, 497 U.S. 871, 885 (1990); Bhan v.
2 NME Hosps., Inc., 929 F.2d 1404, 1409 (9th Cir. 1991). If the
3 moving party shows an absence of evidence to support the non-moving
4 party's case, the burden then shifts to the non-moving party to
5 produce "specific evidence, through affidavits or admissible
6 discovery material, to show that the dispute exists." Bhan, 929
7 F.2d at 1409.

8 If the moving party discharges its burden by negating an
9 essential element of the non-moving party's claim or defense, it
10 must produce affirmative evidence of such negation. Nissan, 210
11 F.3d at 1105. If the moving party produces such evidence, the
12 burden then shifts to the non-moving party to produce specific
13 evidence to show that a dispute of material fact exists. Id.

14 If the moving party does not meet its initial burden of
15 production by either method, the non-moving party is under no
16 obligation to offer any evidence in support of its opposition. Id.
17 This is true even though the non-moving party bears the ultimate
18 burden of persuasion at trial. Id. at 1107.

19 Where the moving party bears the burden of proof on an issue
20 at trial, it must, in order to discharge its burden of showing that
21 no genuine issue of material fact remains, make a prima facie
22 showing in support of its position on that issue. UA Local 343 v.
23 Nor-Cal Plumbing, Inc., 48 F.3d 1465, 1471 (9th Cir. 1994). That
24 is, the moving party must present evidence that, if uncontroverted
25 at trial, would entitle it to prevail on that issue. Id.; see also
26 Int'l Shortstop, Inc. v. Rally's, Inc., 939 F.2d 1257, 1264-65 (5th
27 Cir. 1991). Once it has done so, the non-moving party must set

1 forth specific facts controverting the moving party's prima facie
2 case. UA Local 343, 48 F.3d at 1471. The non-moving party's
3 "burden of contradicting [the moving party's] evidence is not
4 negligible." Id. This standard does not change merely because
5 resolution of the relevant issue is "highly fact specific." Id.

6 DISCUSSION

7 I. Follow the Fortunes Doctrine

8 "Under the 'follow the fortunes' doctrine, a reinsurer is
9 required to indemnify for payments reasonably within the terms of
10 the original policy, even if technically not covered by it. A
11 reinsurer cannot second guess the good faith liability
12 determinations made by its reinsured, or the reinsured's good faith
13 decision to waive defenses to which it may be entitled."
14 Christiania Gen. Ins. Corp. v. Great Am. Ins. Co., 979 F.2d 268,
15 280 (2d Cir. 1992), as quoted by National Am. Ins. Co. v. Certain
16 Underwriters at Lloyd's London, 93 F.3d 529, 535 (9th Cir. 1996).
17 Included in the "follow the fortunes doctrine" is the "follow the
18 settlements doctrine," which "prevents facultative reinsurers from
19 second guessing good-faith settlements and obtaining de novo review
20 of judgments of the reinsured's liability to its insured."
21 National Am. Ins., 93 F.3d at 535. Explicit "follow the
22 settlements" language is included in many reinsurance contracts,
23 but Defendant asserts that no such language is included in the
24 agreement between SNIC and American Re.

25 Plaintiff counters that, while the term "follow the
26 settlements" is not included in the American Re agreement, other
27 language in the policy is sufficient to constitute an agreement to
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1 follow the settlements. Therefore, Plaintiff argues, the contract
2 should be read to include such an obligation under California law,
3 citing Pacific Mutual Life Insurance Company of California v.
4 Pacific Surety Company, 69 Cal. App. 730 (1924). Plaintiff contends
5 that Pacific Mutual provides that where a reinsurer agrees to "(1)
6 follow the same terms of the [reinsured's] contract; (2) give the
7 reinsured the right to settle the claim; and (3) then agree to pay
8 the settlement made by the reinsured," a "follow the settlements"
9 agreement should be found. Plaintiff's Opposition and Cross-Motion
10 at 16-17. Plaintiff further argues that Defendant agreed to each
11 of these three things, citing various provisions of the agreement
12 between Defendant and SNIC.

13 Plaintiff mischaracterizes Pacific Mutual. The contract in
14 that case read, "The 'Pacific Mutual' alone shall settle all claims
15 and such settlements shall be binding on the 'Reinsurance Company'
16 in proportion to its participation, whether the settlement be in
17 full or in compromise." 69 Cal. App. at 733. This language is
18 itself an express "follow the settlements" provision. The Pacific
19 Mutual court had only to decide that this language, though
20 different from language found to be a "follow the settlements"
21 provision in another case, was in fact such a provision. No such
22 language appears in the American Re agreement.

23 Similarly, the court in Royal Insurance Co. v. Caledonian
24 Insurance Co, 182 Cal. 219 (1920), relied on specific policy
25 language when it required the reinsurer to "follow the settlements"
26 of the insured. There, the policy stated that it was "subject to
27 the same risks, valuations, conditions, and adjustments as are or
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1 may be taken by the reinsured, and loss if any thereunder is
2 payable pro rata with the reinsured at the same time and place."
3 Id. at 221. In particular, the court noted that the policy
4 included the word "adjustments," which made "clear that the
5 adjustment and settlement of losses, when made by the original
6 insurer after proper investigation conducted upon good faith,
7 should be binding upon the reinsurer." Id. at 225. Again, no such
8 language appears in the American Re agreement. Therefore,
9 Plaintiff has not demonstrated that a "follow the settlements"
10 provision can be read into the contract as a matter of law.

11 Defendant also moves for summary judgment on this issue,
12 arguing that a "follow the settlements" provision would be contrary
13 to the written policy which provides that Defendant will indemnify
14 Plaintiff "against losses or damages which [Plaintiff] is legally
15 obligated to pay with respect to which Insurance is afforded during
16 the terms of this Certificate under the policy reinsured," that it
17 "will not indemnify [Plaintiff] for liability beyond circumscribed
18 policy provisions," and that Plaintiff's settlement of claims must
19 be "in accordance with the terms and conditions" of the
20 certificate. Craig Declaration, Ex. D.

21 Based on these provisions, the Court grants Defendant's motion
22 for summary judgment on Plaintiff's claim for declaratory relief.
23 Although Plaintiff contended in discovery that it based its
24 position on "custom and practice" in the reinsurance industry, it
25 has not presented any argument or evidence to support its "custom
26 and practice" theory either in its own motion or in support of its
27 opposition to Defendant's motion.

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United States District Court
For the Northern District of California

1 Because Plaintiff has not established that the SNIC
2 certificate contains a "follow the settlements" provision as a
3 matter of law, the Court also denies Plaintiff's motion to the
4 extent it seeks summary judgment on the claims for declaratory
5 judgment and breach of contract. Plaintiff's arguments on those
6 claims are based entirely on its claim that American Re is obliged
7 to follow the settlements of SNIC.

8 II. Breach of the Covenant of Good Faith and Fair Dealing

9 A covenant of good faith and fair dealing is implied in every
10 insurance contract. Egan v. Mutual of Omaha Insurance Co., 24 Cal.
11 3d 809, 818 (1979), cert. denied, 445 U.S. 912 (1980); see also,
12 Gourley v. State Farm Mutual Auto. Insurance Co., 53 Cal. 3d 121,
13 127 (1991). "An insurer, like any other party to a contract, owes
14 a general duty of good faith and fair dealing. . . . There are at
15 least two separate requirements to establish breach of the implied
16 covenant: (1) benefits due under the policy must have been
17 withheld; and (2) the reason for withholding benefits must have
18 been unreasonable or without proper cause." Love v. Fire Ins.
19 Exch., 221 Cal. App. 3d 1136, 1147, 1152 (1990).

20 Defendant moves for summary judgment on Plaintiff's claim for
21 breach of the implied covenant of good faith and fair dealing,
22 arguing that Plaintiff cannot establish that it unreasonably
23 withheld policy benefits. Plaintiff opposes Defendant's motion and
24 cross-moves for summary judgment on the claim. Plaintiff's cross-
25 motion necessarily fails because it has not been determined that
26 Defendant withheld benefits due under the policy.

27 Defendant argues that this claim must fail because, even if it
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1 was obliged to pay the underlying settlement, there was a genuine
 2 dispute regarding that obligation. "Because the key to a bad faith
 3 claim is whether denial of a claim was reasonable, a bad faith
 4 claim should be dismissed on summary judgment if the defendant
 5 demonstrates that there was a genuine dispute as to coverage."
 6 Feldman v. Allstate Ins. Co., 322 F.3d 660, 669 (9th Cir. 2003)
 7 (internal quotations omitted). However, Plaintiff has produced
 8 evidence that Defendant might have acknowledged liability for such
 9 claims under an earlier, substantially similar policy. The Court
 10 finds that this is sufficient to create a triable question of fact
 11 that Defendant acted in bad faith if there is a finding that
 12 Defendant withheld benefits due. Therefore the Court denies
 13 Defendant's motion for summary judgment on this claim. Because
 14 Plaintiff has not established that benefits were improperly
 15 withheld, the Court also denies its motion for summary judgment on
 16 this claim.

17 CONCLUSION

18 For the foregoing reasons, the Court GRANTS in part
 19 Defendant's motion for partial summary judgment (Docket No. 75) and
 20 DENIES Plaintiff's motion for summary judgment (Docket No. 83).⁶

21 IT IS SO ORDERED.

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23 Dated: 5/29/07



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CLAUDIA WILKEN
United States District Judge

26 ⁶Defendant's objection to evidence submitted by Plaintiff
27 (Docket No. 96) is DENIED as moot. The Court did not consider any
28 improper or inadmissible evidence in deciding these motions.

United States District Court
For the Northern District of California

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