COMMONWEALTH OF KENTUCKY
SUPREME COURT
CASE NO. 2007-SC-00246

AMERICAN INTERNATIONAL SPECIALTY LINES INSURANCE COMPANY — APPELLANT

v.

APPEAL FROM JEFFERSON CIRCUIT COURT
CASE NO. NO. 05-CI-00771
APPEAL FROM KENTUCKY COURT OF APPEALS
NO. 2006-CA-002510

HON. EDDY COLEMAN, JUDGE
PIKE CIRCUIT COURT, ET AL. — APPELLEE

THE ESTATE OF IDA SWORD McCOWN, by and through JAMES McCOWN, Executor — REAL-PARTY-IN-INTEREST

BRIEF OF APPELLANT, AMERICAN INSURANCE SPECIALTY LINES INSURANCE COMPANY

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CERTIFICATE OF SERVICE

In accordance with CR 76.12(5), I hereby certify that a copy of this Brief was on this 30th day of April, 2007, served by First Class Mail, postage prepaid, upon Miller Kent Carter, Miller Kent Carter & Michael Lucas, PLLC, 131 Division Street, P.O. Box 852, Pikeville, KY 41502; Richard E. Circeo, Wilkes & McHugh, P.A., 2100 West End Ave., Suite 640, Nashville, TN 37203, Byron N. Miller, Kevin M. Murphy, Thompson, Miller & Simpson PLC, 600 West Main Street, Suite 500, Louisville, KY 40202Hon. Eddy Coleman, Judge, Pike Circuit Court, 435 Hall of Justice, 172 Division Street, Pikeville, KY 41501; and Kentucky Court of Appeals, 360 Democrat Drive, Frankfort, KY 40601-8209.

Edward H. Stopher

INTRODUCTION

This is an appeal by American Insurance Specialty Lines Insurance Company ("AISLIC") of the denial of a writ of prohibition and/or mandamus prohibiting the trial court from entertaining plaintiff's declaratory judgment action against AISLIC before plaintiff has obtained a judgment in its tort action against AISLIC's insured.

STATEMENT CONCERNING ORAL ARGUMENT

AISLIC desires oral argument of the present appeal. Oral argument would be helpful to the Court in deciding the issues presented because the Court of Appeals has created new law by breaking long-standing precedent, and finding a bankruptcy/insolvency exception—nonexistent in Kentucky law— to the rule prohibiting a lawsuit against a liability insurer prior to judgment against its insured. Oral argument would assist the Court in analyzing the legal precedent and the effect on the insurance industry of the Court of Appeals order denying AISLIC's requested writ.

STATEMENT OF POINTS AND AUTHORITIES

APPENDIX

Exhibit A - Court of Appeals Order Denying Writ of Prohibition and/or Mandamus

Exhibit B- Complaint

Exhibit C- AISLIC Healthcare Professional Liability and Healthcare General Liability Policy

Exhibit D- Plaintiff's Motion to Amend Complaint

Exhibit E- Amended Complaint

Exhibit F- Attorney Oldham's April 19, 2006 letter to McCown's counsel

Exhibit G- Attorney Sewell's September 29, 2005 letter to McCown's counsel with attachments

Exhibit H- Notice of Confirmation of Plan, Permanent Injunction, and Various Deadlines

Exhibit I- Documentation maintained by Centennial's notice agent confirming the Notice was sent to Ms. McCown on June 24, 2004

Exhibit J- McCown's Response to Petition for Writ

STATEMENT OF THE CASE

I. Introduction

The Court of Appeals' failure to grant AISLIC's writ of prohibition/mandamus breaks new legal ground in Kentucky and shatters the long-standing rule in Kentucky and the vast majority of jurisdictions that prohibits an injured party from directly suing the tortfeasor's liability insurer before obtaining a judgment against the tortfeasor. The Court's holding could also lead to unintended unlawful consequences, by permitting a plaintiff to discover other assets of a tortfeasor with no or little insurance coverage before obtaining a judgment that establishes the relevancy of such assets. While the Court of Appeals lastly relies on a so-called bankruptcy/insolvency exception to the rule against direct actions, Kentucky case law clearly shows there is no exception that permits a direct action before obtaining a judgment against the tortfeasor.

The estate of Ida Sword McCown ("McCown") initiated a negligence action in Pike Circuit Court against Parkview Nursing and Rehabilitation Center ("Parkview"), where Ms. McCown was a resident, alleging Parkview negligently caused Ms. McCown's death. While McCown asserted a prima facie claim against Parkview, McCown improperly amended its complaint to add Parkview's insurer, AISLIC, as a defendant. McCown seeks a declaration that the insurance policy AISLIC issued to Parkview, which is excess of Parkview's $1 million self-insured retention, provides coverage for its claims against Parkview.

AISLIC filed a motion to dismiss on the grounds that under well-established Kentucky law, McCown could not sue AISLIC until it obtained a judgment against

Parkview, which the trial court denied.[1] The Kentucky Court of Appeals denied AISLIC's subsequent writ of prohibition and/or mandamus, in which AISLIC sought to prohibit the trial court from maintaining McCown's declaratory judgment action. (Court of Appeals Order denying CR 76.36 relief, attached as Ex. A).

By denying AISLIC's writ of prohibition and/or mandamus, the Court of Appeals makes new law. Its Order directly contradicts well-established Kentucky precedent prohibiting direct actions against insurance companies by persons who are neither parties to, nor third party beneficiaries of, the insurance contract *unless and until* a judgment is rendered.

First, the underlying action, in which McCown seeks a determination that it timely filed its claim under the policy, *is* a direct action in the guise of a declaratory judgment action. Indeed, McCown seeks to recover from AISLIC damages that it is barred in the bankruptcy proceeding from recovering against Parkview. Regardless of whether McCown's action is a "direct action", if the rationale, as explained by the Court of Appeals, for permitting an injured party to seek a declaration of coverage under a liability policy is to save the plaintiff from incurring the cost of obtaining a worthless judgment, it follows that an injured person could discover the assets of a tortfeasor with no or insufficient insurance before prosecuting the tort action. This has never been the law in Kentucky, and would subject every defendant to potential discovery of the defendant's assets before the plaintiff obtains a judgment that establishes their relevancy.

Second, the Court of Appeals Order contradicts the rule, which both McCown and the Court recognize, that a plaintiff may not generally sue the defendant's insurer. The so-

[1] Under the terms of ASLIC's policy issued to Parkview the judgment or settlement would have to be in excess of Parkview's $1 million self insured retention in order to trigger coverage.

York Indem. Co. v. Ewell, 296 S.W. 182 (Ky. 1927), and the cases that emanate therefrom

called "bankruptcy/insolvency exception" to such rule, which the Court and McCown espouse, is non-existent. In fact, the case that purportedly established the exception, New York Indem. Co. v. Ewen, 298 S.W. 182 (Ky. 1927), and the cases that emanate therefrom, reaffirm the long-standing rule that a plaintiff must obtain a judgment against an insured before suing the insurer directly. Even if this Court were to create an exception, it should not apply here where the prospect that McCown may obtain a worthless judgment is not due to Parkview's bankruptcy petition, but to McCown's failure to file a post-petition administrative claim in the bankruptcy court. Had McCown not sat on its rights, it could have recovered its supportable damages in full from Parkview's self-insured retention of $1 million. Thus, McCown would not have needed to rely on a purported bankruptcy exception to recover, and the declaratory judgment action would have been unnecessary.

While relief by way of prohibition or mandamus is generally an extraordinary remedy, it is necessary to correct the trial court's erroneous exercise of jurisdiction over McCown's declaratory judgment action. Unless and until McCown obtains a judgment against Parkview, McCown lacks standing to bring a declaratory judgment action against AISLIC, and, therefore, there is no actual justiciable controversy. In the absence of a justiciable controversy, Kentucky law is clear that the trial court lacks jurisdiction to entertain McCown's declaratory judgment action, and the Court of Appeals erred in failing to grant a writ prohibiting such action.

Assuming the trial court has jurisdiction over McCown's declaratory judgment action, it is acting erroneously in entertaining it. Indeed, compelling an insurer to litigate an action which the law declares it should not have to defend effectively subverts the rule

prohibiting direct actions against insurers. This consequence leaves AISLIC with no adequate remedy by appeal and would cause it to suffer great and irreparable injury.

Accordingly, this Court should reverse the Court of Appeals denial of AISLIC's petition for a writ of prohibition and/or mandamus, thereby precluding the trial court from hearing the declaratory judgment action and requiring it to dismiss such action against AISLIC.

II. Facts

For a little more than a year, the decedent, Ida McCown, was an elderly resident of Parkview, a nursing home located in Pikeville, Kentucky that provides skilled nursing and custodial care to elderly and infirm residents. Ms. McCown was admitted to Parkview on November 5, 2003 after her family was no longer able to care for her without assistance. (Complaint, attached as Ex. B, at ¶17). Ms. McCown remained a Parkview resident until she was discharged on January 22, 2004. Id. Ms. McCown died almost six months later on June 2, 2004. Id. at ¶4.

Ms. McCown's estate filed the present tort action on January 7, 2005 alleging that Parkview and its employees negligently provided skilled nursing home services to her. Id. at ¶23. McCown alleges that such negligent care accelerated the deterioration of Ms. McCown's health and physical condition beyond that caused by the normal aging process, and resulted in physical and emotional pain and suffering and her ultimate death. Id. at ¶20. McCown sued Parkview, various parent entities of Parkview, and certain Parkview employees. As to the corporate defendants (collectively referred to herein as "Parkview"), McCown joined them in the action "for the purpose of implementing the insurance coverage available to the individual defendants and any insurance coverage available to the corporate defendants upon which this claim is based." Id. at ¶39.

McCown asserts claims of negligence, negligence *per se*, negligent hiring, gross negligence and the tort of outrage, and seeks compensatory and punitive damages.

On May 2, 2006, McCown filed a motion to amend its Complaint to assert a direct action against AISLIC in addition to the previously asserted claims against the individual and corporate defendants. AISLIC issued a Healthcare Professional Liability and Healthcare General Liability policy to Parkview.[2] (Policy No. 612-55-47, attached as Ex. C). The AISLIC policy is a "claims made" policy effective August 7, 2002 through August 7, 2004. More importantly, the ASLIC policy applies in excess to Parkview's self insured retention per occurrence. Thus, before AISLIC's coverage is implicated, McCown must recover more than $1 million in damages.

McCown alleges that it learned of a potential dispute as to whether the originally named defendants were insured at the time McCown asserted its claim. (Plaintiff's Motion to Amend Complaint, attached as Ex. D, at ¶3). McCown contends that defendants' counsel, William Oldham, advised in an April 19, 2006 letter there is no coverage under the policy for McCown's claims because McCown did not assert its claim until it filed the Complaint on January 7, 2005. Id.

In its Amended Complaint, McCown asserts allegations which only the insured seeking coverage under the applicable policy may assert. McCown requests that the policy be construed so as to provide coverage for a judgment against Parkview that it has yet to obtain. Specifically, McCown alleges that the complaints and allegations it made directly to Parkview and to state agencies, and its request for Parkview records, all made before August 7, 2004, constitute a "claim" under the policy such that it was made

[2] Hilltopper Holding Corporation is listed as the named insured, Parkview Nursing & Rehabilitation Center is listed as the certificate holder and the remaining corporate defendants are listed in Schedule A to the policy as additional insureds.

timely. (Amended Complaint, attached as Ex. E, at ¶9). McCown seeks a declaratory judgment that:

(1) the subject policy provides coverage for plaintiff's claims in the underlying wrongful death action;

(2) the formal and informal complaints and investigations occasioned by plaintiff's complaints and its records request constitute a "claim" under the policy; and

(3) AISLIC's alleged failure to define "claim" constitutes an ambiguity which should be resolved in favor of finding that plaintiff's actions and conduct constitute a "claim."

Id. at pp. 4-5. McCown is not entitled to request this or any construction of the AISLIC policy.

The AISLIC policy is one for indemnification which potentially provides liability coverage only after the insured is "legally required" to pay damages to a third party:

> ***I. INSURING AGREEMENTS***
>
> A. Healthcare Professional Liability
>
> . . . **[W]e** will indemnify **you** those amounts that **you** are *legally required to pay others as damages* resulting from a **medical incident** arising out of **professional services** provided by any Insured, including bodily injury arising out of the violation of **Rights of Residents**.

(Ex. C, Policy at p. HPL-1) (emphasis in italics added). The policy further prohibits direct actions against AISLIC by claimants who have also sued AISLIC's insured for damages:

> D. Legal Action Against Us
>
> *No person or organization has a right under this Policy*:
>
> 1. *To join **us** as a party or otherwise bring **us** into a **suit** asking for damages from **you**; . . . .*
>
> * * *

it. We note that the facts and circumstances of the instant cases are unlike any encountered in the authorities on which AISLIC relies in support of its argument that the trial court is without jurisdiction and that McCown and Fronto are without standing. The latter are not seeking any recovery from AISLIC at this time. Rather, because they have been advised that they may not recover from the Parkview Defendants directly due to their bankruptcy reorganization and are limited to liquidate damages, if any, against available insurance coverage, they are seeking a determination as to whether they made their claims within the coverage period provided under the policy before proceeding to expend additional resources into the prosecution of claims that would turn out to be worthless if there is no insurance coverage. Hence, we do not believe that the declaration of rights that they seek is hypothetical or advisory in nature. Neither do we believe that AISLIC has made a valid argument that there is no insolvency/bankruptcy exception to the rule that a plaintiff may not sue a defendant's insurer. The exception is clearly acknowledged in a line of cases, including *Harris, supra.*[4]

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[4] As noted by Fronto in her response, it was also acknowledged by this Court in *Ford v. Ratliff*, 183 S.W.3d 199, 203, n.10 (Ky. App. 2006), which is also citing *Cuppy, supra.*

11 Case No. 02-74974. (Attorney Sewell's September 29, 2005 letter to McCown's counsel with attachments, attached as Ex. G).

Attorney Sewell advised McCown's counsel that the Bankruptcy Court confirmed the debtors' Plan of Reorganization on June 22, 2004. Id.; Notice of Confirmation of Plan, Permanent Injunction, and Various Deadlines, attached as Ex. H; Documentation maintained by Centennial's notice agent confirming the Notice was sent to Ms. McCown on June 24, 2004, attached as Ex. I. The Notice advised that any claims against the debtors must be filed "within ninety (90) days after service of this Notice." (Ex.H, p. 3). The Notice further provided:

> Any such person who fails to file a timely proof of an Administrative Claim with the claims agent will be **FOREVER BARRED** from seeking payment of such Administrative Claim by the Debtors, their estates, or the reorganized Debtors.

Id. (emphasis in original). Attorney Sewell advised that "[h]ad a claim been filed with the Bankruptcy Court . . . , some coverage would be available for this claim", but that McCown's "failure to timely file a claim has resulted in both the claims against the corporate defendants being discharged from any liability to [the decedent's] estate." (Ex. G, p. 2).

The declaratory judgment action against AISLIC, therefore, is an improper attempt to cure McCown's potentially fatal failure to timely file its claim in the bankruptcy case. Until a determination is made regarding whether McCown's claim against Parkview is discharged or liability is determined on the merits, the declaratory judgment action is simply premature and should be dismissed.

ARGUMENT

THE COURT OF APPEALS ERRED IN FAILING TO GRANT AISLIC'S WRIT OF PROHIBITION AND/OR MANDAMUS DISMISSING THE DECLARATORY JUDGMENT ACTION AGAINST IT.

AISLIC is entitled to a writ under either of the two alternative classes of writs because the trial court is (1) acting without jurisdiction (which includes beyond its jurisdiction), or (2) acting erroneously within its jurisdiction. Newell Enterprises, Inc. v. Bowling, 158 S.W.3d 750, 754 (Ky. 2005).

It is clear from the case law that the trial court in this case is acting without jurisdiction by entertaining McCown's declaratory judgment action because there is no justiciable controversy and McCown – a stranger to the insurance policy – lacks standing to litigate coverage under it. Even accepting the Court of Appeals' erroneous holding that the improper declaratory judgment action is within the trial court's jurisdiction, AISLIC has no adequate remedy by appeal and will suffer great and irreparable injury if such action is litigated prior to judgment against Parkview.

I. The Trial Court Lacks Jurisdiction to Hear the Declaratory Judgment Action.

In determining whether to issue a writ of prohibition, courts frequently state that a writ is "an extraordinary remedy" which should be cautiously and conservatively entertained. See, e.g., Bender v. Eaton, 343 S.W.2d 799, 800 (Ky. 1961). However, the standard for granting a writ is relaxed where a petition seeks to prevent the trial court from erroneously exercising jurisdiction over an action. See Grange Mut. Ins. Co. v. Trude, 151 S.W.3d 803 (Ky. 2004); Hoskins v. Maricle, 150 S.W.3d 1 (Ky. 2004). Indeed, because whether a court has jurisdiction is a question of law, this Court's review

of the decision to grant or deny a writ of the first class is *de novo*. Trude, 151 S.W.3d at 810 (Ky. 2004).

Thus, the extraordinary nature of a writ stems from the discretion a court has in granting a writ of the second class after first finding there is no adequate remedy by appeal and great and irreparable injury would result to the petitioner. See Hoskins, 150 S.W.3d 1 (resolving an inconsistency in the case law and holding that a writ to prohibit the trial court from acting outside its jurisdiction is proper despite the existence of an adequate remedy by appeal). A trial court has *no* discretion to entertain a case in which it has no jurisdiction. Whether an appeal is an adequate remedy or the petitioner will suffer great and irreparable harm simply are not considerations for an appellate court where the trial court lacks jurisdiction to hear McCown's declaratory judgment action. In such situations where only questions of law are involved, writs are more commonly granted. To paraphrase the Court in Hoskins:

> If [Judge Coleman] lacks jurisdiction to [hear McCown's direct action against AISLIC], it would be a most inept ruling to deny the writ, require a trial on the merits, and then on appeal be forced to reverse the case on the very question which is now before us.

Id. at 11. As will be established below, the trial court lacks jurisdiction to hear the declaratory judgment action.

A. McCown's Declaratory Judgment Action Fails to Present an Actual Controversy Respecting a Justiciable Issue.

It is well-settled that "[r]elief by way of declaratory judgment is conditioned on the existence of an actual controversy." Alexander v. Hicks, 488 S.W.2d 336, 337 (Ky. 1972) citing KRS 418.040 (A plaintiff may request a declaration of rights where "an actual controversy exists."). Thus, the condition precedent to a declaration of rights is

"the existence of an actual controversy respecting a justiciable issue, rather than a prospective controversy." Id. at 337.

The Kentucky Supreme Court explained the actual controversy requirement as follows:

> An actual controversy for purposes of a declaratory judgment statute requires a controversy over present rights, duties and liabilities; it does not involve a question which is merely hypothetical or an answer which is no more than an advisory opinion.

Barrett v. Reynolds, 817 S.W.2d 439, 441 (Ky. 1991). A declaratory judgment cannot be rendered on questions "which may never arise or which are merely advisory, academic, hypothetical, incidental or remote, or which will not be decisive of a present controversy." Hughes v. Welch, 664 S.W.2d 205, 208 (Ky.App. 1984).

It is equally fundamental that "[i]n the absence of a justiciable controversy, the court has no jurisdiction." Ex parte Weyler, 252 S.W.2d 884, 885 (Ky. 1952). In Revis v. Daugherty, 287 S.W. 28 (Ky. 1926), the Court found that the declaratory judgment action filed by the plaintiff did not present a justiciable controversy. The Court thus held that "since there was no actual justiciable controversy presented by the petition, the [trial] court was without jurisdiction to entertain it or to attempt to adjudge the academic question submitted." Id. at 29.

In this case, there is currently no actual controversy respecting a justiciable issue. Rather, McCown's Amended Complaint presents merely a prospective controversy. Indeed, AISLIC's policy provides that coverage is not implicated until Parkview "shall become legally obligated to pay" McCown damages because of injury, and then only if such damages exceed $1 million. McCown filed its original Complaint against Parkview in January 2005, but has yet to receive a judgment against, or enter into a settlement with,

Parkview in excess of $1 million. Thus, Parkview is currently under no legal obligation to pay McCown damages for its alleged injuries. Until such time, determining whether coverage exists under the policy for McCown's claims would be merely advisory, academic, hypothetical, incidental or remote, and would not be decisive of a present controversy.

Other courts have examined the ripeness of a declaratory judgment action against an excess carrier, like AISLIC, where the liability of the primary carrier has not yet been determined. For example, in Rhone-Poulenc, Inc. v. International Ins. Co., 71 F.3d 1299, 1302 (7th Cir. 1995), the 7th Circuit held that "a suit against an excess insurer cannot proceed "until the primary carriers" have acknowledged their liability to the insured or have been determined by a court to be liable to him." In the present case, McCown has not even alleged, much less presented any evidence that its damages exceed Parkview's self-insured retention limit of $1 million. Until it is determined by a settlement with or judgment against Parkview whether AISLIC's excess coverage is implicated, McCown's declaratory judgment action is premature and there is no actual controversy.

In the absence of an actual justiciable controversy, the trial court is without jurisdiction to hear McCown's declaratory judgment action, and AISLIC is entitled to a writ prohibiting the court from entertaining such action. This result comports squarely with well-settled Kentucky law that an injured party lacks standing to bring a direct action against a tortfeasor's liability insurer prior to receiving a judgment against the tortfeasor.

1. McCown's Declaratory Judgment Action Violates the Rule Prohibiting Direct Actions Against Insurers.

As the Kentucky Court of Appeals in Kentucky Hosp. Ass'n Trust v. Chicago Ins. Co., 978 S.W.2d 754 (Ky.App. 1998) recognized, "In Kentucky it has long been held that generally suits against insurance carriers cannot be maintained until after a judgment fixing liability against their insured has been entered." Id. at 755. This rule is rooted in the plain language of liability policies pursuant to which "[a]n insured must become legally obligated to pay" before an injured party may claim a right to the insurance proceeds. Id. at 756.

In Kentucky Hosp. Ass'n Trust ("KHAT"), KHAT settled a medical malpractice claim on behalf of its insured pharmacist, Asher, and sought personal indemnification from Chicago Insurance Company ("CIC"), who also insured Asher under a separate policy. In determining the propriety of KHAT's direct action against CIC, the Court cited the CIC policy under which CIC agreed to pay on behalf of Asher "all sums which the insured shall become legally obligated to pay as damages because of injury . . . ." Id. Because the plaintiff had settled his claim against Asher, the Court held there was no finding that it was liable to the plaintiff as a result of Asher's actions or inactions, and, therefore, "CIC had no legal obligation as to Asher." Id. Thus, the Court upheld the dismissal of KHAT's action against CIC, because the condition precedent to coverage under the CIC policy, i.e. the insured's legal obligation to pay damages to the plaintiff, was never established.

Kentucky courts have repeatedly applied the rule prohibiting direct actions against insurers to suits brought by injured parties against tortfeasors' insurers. In Moores v. Fayette County, 418 S.W.2d 412 (Ky. 1967), a pedestrian, who was injured from a fall on an icy sidewalk at the Fayette County Courthouse, sued various County entities and

employees as well as the County's liability insurer, Cincinnati Insurance Company. Kentucky's highest court affirmed the dismissal of the action as to Cincinnati Insurance Company holding that "[a] claimant may not join the insured and the insurer in an action based on the insured's negligence." Id. at 413. The Court relied on the decision in Happy v. Erwin, 330 S.W.2d 412 (Ky. 1959) in which it was held that "the insurer is not liable until after a judgment has been rendered fixing liability against someone insured by the insurer." 418 S.W.2d at 403. The Court found that the Cincinnati Insurance policy similarly provided that Cincinnati Insurance Company is not obligated to pay until "the insured (the county) shall become legally obligated to pay." Id. See also Chambers v. Ideal Pure Milk Co., 245 S.W.2d 589, 591 (Ky. 1952) (in action for personal injuries resulting from a collision with a vehicle driven by one who was being pursued by the police, plaintiff could not maintain an action on the policemen's insurance policy until judgment had been entered against them).

Kentucky law on this issue comports with the modern and majority rule that "in the absence of a contractual or statutory provision allowing a direct action, the claimant has no right to a direct action against the liability insurer." Holmes' Appleman on Insurance 2D, §111.1 at 44 (2000). "Only after the third party claimant prevails in his or her suit against the insured and obtains the status of a judgment creditor" may the claimant file a direct action against the insurer. Id. at 45. In support of this rule, the Wisconsin Supreme Court aptly reasoned:

> To declare the existence of a cause of action in favor of the claimant against the insurer for these injuries would be to expose an insurer to liability for failure to satisfy a claim before the fundamental predicate to a duty to do so has been established – the determination of the insured's legal liability.

Kranzush v. Badger State Mut. Cas. Co., 307 N.W.2d 256, 263-65 (Wisc. 1981).

In this case, the Court of Appeals concluded that McCown's declaratory judgment action is not a true direct action because McCown is not seeking recovery "at this time" from AISLIC, but a determination that Parkview's insurance policy provides coverage for McCown's negligence action. (Order denying CR 76.36 relief, p. 7). This is a distinction without a difference. McCown let the time lapse in the bankruptcy proceeding for preserving its claim against Parkview. Now, McCown seeks to breathe new life into its claim by suing the only other potential money source, AISLIC, before there has been any determination that Parkview was negligent and that McCown's damages exceed $1 million. McCown's ultimate goal in filing the declaratory judgment action is to recover damages from AISLIC, which is simply premature until Parkview's liability is established or a determination is made that McCown's claim against Parkview is discharged.

2. The Rule Prohibiting Direct Actions Applies to Declaratory Judgment Actions.

While Kentucky courts have not yet specifically characterized declaratory judgment actions seeking a coverage determination as "direct actions", neither has any such court held that an injured party may litigate coverage issues under a liability policy issued to the tortfeasor. Numerous courts in other jurisdictions have addressed this precise issue and held plaintiffs lack standing to seek a declaration that coverage exists for claims against an insured tortfeasor.

The decision in Farmers Ins. Exchange v. The District Court for the Fourth Judicial District, 862 P.2d 944 (Colo. 1993) is directly on point. In that case, the Colorado Supreme Court granted a writ of prohibition to prohibit the trial court from

hearing a declaratory judgment action filed by the injured party against the tortfeasor's insurer. The plaintiff sought to challenge the insurer's position that due to the "other insurance" clause in the policy, the coverage limits were $25,000, not $100,000. The plaintiff contended an actual controversy existed because her counsel could not properly assess the insurer's settlement offer of $25,000, advise the plaintiff and negotiate with the other carriers without judicial construction of the policy. The trial court agreed and denied the insurer's motion to dismiss. It reasoned that "a declaratory judgment action is not only allowable, but desirable, to get the question settled quickly, because it will have an effect on the parties' rights and status, or it will be . . . removing an uncertainty." Id. at 946.

The insurer filed a writ of prohibition to prevent the trial court from proceeding with the declaratory judgment action. The Colorado Supreme Court noted that a declaratory judgment action "must be based on an actual controversy" and discussed this requirement in terms of standing. Id. at 947.

> A declaratory judgment action is only appropriate when the rights asserted by the plaintiff are present and cognizable ones. "It calls, not for an advisory opinion upon a hypothetical basis, but for an adjudication of present right upon established facts." Aetna Life Ins. Co. v. Haworth, 300 U.S. 227, 242, 57 S.Ct. 461, 465, 81 L.Ed. 617 (1937). If entered a declaratory judgment would effect a change in the plaintiff's present rights or status. "It is not the function of the courts, even by way of declaration, to adjudicate . . . in the absence of a showing that a judgment, if entered, would afford the plaintiff present relief." Taylor v. Tinsley, 138 Colo. 182, 183, 330 P.2d 954, 955 (Colo. 1958).

Id. The Court further held that declaratory judgment proceedings may not be invoked to resolve a non-existent question, "even though it can be assumed that at some future time such question may arise." Id. (citations omitted). To satisfy the standing requirement,

the plaintiff must show there is "an existing legal controversy, . . . not a mere possibility of a future legal dispute over some issue . . . . The court should refuse to answer speculative inquiries." Id. at 947-48.

The Court noted that the issue of whether a plaintiff, before obtaining a judgment against the defendant, may bring a declaratory judgment action against a defendant's insurance company which denied coverage to its insured, was one of first impression. Thus, the Court looked to decisions in other states in which the courts ruled that a plaintiff does not have standing to bring such an action to contest the insurer's denial of coverage. See id. at 948 citing Park v. Safeco Ins. Co., 162 S.E.2d 709, 710 (S.C. 1968) ("[Plaintiff] has no right to call upon McCall for payment of damages until he establishes liability, and accordingly, he has no right to call upon any insurance company alleged to protect McCall."). Hale v. Fireman's Fund Ins. Co., 302 P.2d 1010, 1014 (Or. 1956) (because plaintiff had not yet obtained a judgment against the insolvent defendant to whom insurer contended it owed no coverage, "the purported rights upon which the plaintiff depends are too remote and contingent to be appropriate for declaratory relief."); Rhodes v. Lucero, 444 P.2d 588, 589 (N.M. 1968) (holding that where plaintiffs sought declaratory judgment that insurance policy covers defendant, there is no justiciable controversy because plaintiffs hold no judgment against defendant and their rights against him are contingent).

The Court in Farmers Insurance held that the plaintiff lacks standing to seek declaratory relief because there is no legal existing controversy between him and the insurer "unless and until she has established [the defendant's] liability" through a judgment. Id. at 948. The Court concluded, "[b]ecause Neely does not have standing to

bring the declaratory judgment action, we hold that the trial court abused its discretion in assuming jurisdiction and not dismissing the declaratory judgment action." Id. at 949 (emphasis added).

Similarly, in Park, the plaintiff sought a declaration regarding whether Safeco Insurance Company successfully denied liability coverage to the underlying defendant, and that if so, the plaintiff is entitled to uninsured motorist benefits under his own policy. The South Carolina Supreme Court noted that "[t]he Declaratory Judgment Act should be liberally construed and applied, especially where litigation will be prevented, but there is a limit beyond which the courts should not go." 162 S.E.2d at 711.

The Court recognized that declaratory judgment actions may be filed by the insured or insurer to determine coverage, because a controversy obviously exists where the insurer refused the insured's demand to defend a lawsuit and/or pay a judgment. However, the Court rejected the same argument that McCown makes here, that the injured person "should have as much right to ask the court to determine the validity of a tortfeasor's liability insurance policy as the insurer or insured":

> We think the fallacy of this argument lies in the fact that the injured person is not a party to the contract and has, under the facts of this case, no primary standing to litigate a dispute between the insured and insurer until and unless he establishes liability against McCall. Before judgment is obtained on a tort claim, the standing of the parties to the policy and the standing of the injured party are greatly different.

Id.

The Court held there is presently no justiciable issue ripe for judicial pronouncement, "because the possible issues are not sufficiently immediate and real to warrant action by the court." Id. The Court noted that the plaintiff may lose his claim

against McCall, and "courts generally decline to pronounce a declaration in a suit wherein the rights of the plaintiff are contingent upon the happening of some event which cannot be forecast and which may never take place." Id.

Like the plaintiffs in Farmers Insurance and Park, McCown's rights under the policy are not present and cognizable ones, but are contingent on its successful litigation of the tort action against Parkview. Prior to obtaining a judgment in the underlying action in excess of $1 million, a declaratory judgment would not change McCown's legal rights or status. Because there is no legal controversy, McCown lacks standing to bring the declaratory judgment action, and the trial court erred in assuming jurisdiction and failing to grant AISLIC's motion to dismiss.

The Kentucky Court of Appeals held that McCown's declaratory judgment action is not hypothetical or advisory in nature because a determination of coverage under the AISLIC policy at the outset would save McCown from expending additional resources in prosecuting claims that would turn out to be worthless if there is no coverage. (Order denying CR 76.36 relief, p. 7). The fallacy in this reasoning is three-fold.

First, to the extent that a judgment McCown obtains against Parkview is worthless, it would be due to McCown's failure to file a post-petition administrative claim in the bankruptcy proceedings, despite Notice of the deadline. Had McCown timely filed such a claim, to the extent it was meritorious, it would have been paid in full. .This Court should not reward McCown with the ability to pursue a declaratory judgment action against AISLIC where McCown alone made any judgment against Parkview worthless because it missed the deadline for filing a claim in the bankruptcy court.

Second, the Court of Appeals erroneously presumes that a declaration by the trial court that McCown timely filed its claim within the claims-made period of the AISLIC policy would make a judgment against Parkview worthwhile. However, because the AISLIC policy is excess over Parkview's self-insured retention of $1 million, AISLIC's coverage would not be triggered unless McCown obtains a judgment against Parkview exceeding $1 million. There has been no allegation that McCown's damages implicate AISLIC's coverage, nor any evidence that they exceed $1 million. Thus, McCown's requested declaratory relief will be worthless where AISLIC's coverage would not be triggered.

Third, if the potential economical savings of first litigating a coverage matter justifies maintaining a declaratory judgment action, plaintiffs would be permitted in other instances to inquire into financial matters which otherwise would be unlawful.

For example, if a party is injured by the acts of a tortfeasor who has no insurance or only limited coverage, based on the Court of Appeals holding, the injured party would be able to discover the nature and extent of the tortfeasor's assets to determine whether it would be "worth it" to proceed with a lawsuit. No matter how destitute a defendant may or may not be, a plaintiff is not entitled to discover the defendant's assets before establishing liability. Indeed, the existence of means to satisfy a potential judgment is irrelevant before the judgment is obtained. Likewise, whether coverage exists to pay a judgment that a plaintiff seeks against the insured is irrelevant and fails to present a justiciable controversy before the plaintiff obtains the judgment.

Additionally, the courts in Farmers and Park properly rejected the same "economical" rationale employed by the Court of Appeals in this case. The fallacy in this

rationale is that it applies equally to *preclude* a declaratory judgment action before the insured's liability is determined—AISLIC would needlessly have incurred expenses to litigate the coverage issue if the insured is later found not to have been negligent.

In the face of such competing interests, the resolution of this issue must be governed by the principles of "actual controversy" and standing, on which the courts in the above cases relied to bar declaratory judgment actions by an injured party. Kentucky's rule prohibiting direct actions against insurers fits squarely within the universal rule prohibiting declaratory judgment actions where there is no actual controversy. Both rules require that the insured's legal liability must be established before the trial court may entertain an injured person's action seeking a declaration of rights under the policy. Without such condition precedent, there is no justiciable controversy, the injured person lacks standing to litigate coverage and the trial court lacks jurisdiction to hear the action. Because McCown has not yet obtained a judgment against Parkview in excess of $1 million, the trial court acted without jurisdiction when it denied AISLIC's motion to dismiss the declaratory judgment action.

3. McCown is Not a Third-Party Beneficiary of the AISLIC Policy, and Therefore Lacks Standing to Seek a Declaration of Rights Under It.

To assert a declaratory judgment action under KRS 418.040, the party seeking such judgment must have a "right or duties" under the contract. KRS 418.045. This Court recognized that this statute "confers standing on a party only where there is a specific right involved. There must be a real or justiciable controversy involving specific rights of particular parties." HealthAmerica Corp. of Kentucky v. Humana Health Plan, Inc., 697 S.W.2d 946, 948 (Ky. 1985). This Court further held in Associated Industries of Kentucky v. Commonwealth, 912 S.W.2d 947, 951 (Ky. 1995) that "[t]he assertion of

one's own legal rights and interests must be demonstrated and the claim to relief *will not rest upon the legal rights of third persons.*" (Emphasis added). Thus, standing to bring a declaratory judgment action requires that the plaintiff either be a party to the contract at issue or a third-party beneficiary of it. It is undisputed McCown is not a party to the AISLIC policy. McCown also fails to qualify as a third-party beneficiary of the policy.

Generally, only parties to a contract may bring an action under it. A third-party stranger to the contract may not enforce it unless it was made for the "actual and direct benefit" of the third party. Sexton v. Taylor County, 692 S.W.2d 808, 810 (Ky.App. 1985). To qualify as a third-party beneficiary, it is necessary "that there be consideration for the agreement flowing to the promisor and that the promisee intends to extract a promise directly benefiting the third party." Simpson v. JOC Coal, Inc., 677 S.W.2d 305, 309 (Ky. 1984). A third party is a creditor beneficiary "if the promisee's expressed intent is that the third party is to receive the performance of the contract in satisfaction of any actual or supposed duty or liability of the promisee to the beneficiary." Sexton, 692 S.W.2d at 810. A third party is an incidental beneficiary with no right to enforce the contract if the benefits to the third party under the contract "are merely incidental to the performance of the promise . . . ." Hendricks Mill & Lumber Co. v. Meador, 16 S.W.2d 482, 484 (Ky. 1929).

Kentucky's highest court in Brooks v. Clark County, 180 S.W.2d 300 (Ky. 1944) rejected the contention that an injured party is a third-party beneficiary of a liability policy. In that case, the plaintiff sued the liability insurer of Clark County for injuries he sustained in an automobile accident with a County employee. The plaintiff argued that he was a third-party beneficiary of the policy and he should not be required to obtain a

judgment against the County before suing the insurer. The plaintiff contended "it was the intention of the parties that the insurance was taken out for the sole purpose of benefiting the public who might be injured and not for the purpose of reimbursing the county for damages it might have to pay." Id. at 301.

The Court disagreed that the intent of the County and insurer was to actually and directly benefit the plaintiff or any injured party. The Court cited the policy which contained virtually the same language as in the AISLIC policy. The standard insuring clause in Clark County's policy obligated the insurer "to pay on behalf of the insured all sums which the insured shall become obligated to pay by reason of the liability imposed upon him by law for damages" arising out of an automobile accident. Id. A further provision stated that no action shall lie against the insurer until the amount of the insured's obligation to pay shall have been finally determined by judgment or agreement of the claimant, insured and insurer. Id.

The Court held that "[w]ords could not more clearly express the intention of the parties that the contract of insurance was one of indemnity only" and permits a third party to seek benefits under it only after securing a judgment against or settling with the insured. Id. Thus, the Court held the trial court properly dismissed the plaintiff's action against the insurer.

In this case, like the policy in Brooks, the AISLIC policy is for indemnity only. It clearly expresses the parties' intention that the contract of insurance obligates AISLIC to pay benefits only after a judgment has been entered against Parkview (assuming the other policy terms and conditions are met) or a settlement has been reached with AISLIC's consent. The policy cannot be construed under any interpretation that AISLIC and

Parkview made the insurance contract for the actual and direct benefit of McCown. Indeed, until a judgment has been entered or a settlement reached that exceeds $1 million, Parkview has no liability to McCown as to which the payment of the liability coverage (to the extent same is available to Parkview) is designed to satisfy. Sexton, 692 S.W.2d at 810. Thus, McCown is presently not a creditor beneficiary, but is instead – at best – merely a potential (if and only if damages exceed $1 million) incidental beneficiary with no right to seek a declaratory judgment regarding the construction of the AISLIC policy.

The Court in DeMent v. Nationwide Mut. Ins. Co., 544 S.E.2d 797 (N.C.App. 2001) reached the same conclusion in a situation similar to the present case. In that case, an automobile accident victim filed a declaratory judgment action against the tortfeasor's liability insurer on the right to recover the cost of emergency first aid under the supplementary payment provision of the policy. Nationwide filed a motion to dismiss contending DeMent was a stranger to the policy and lacked standing to seek a declaratory judgment construing the policy provisions. Id. at 798. The trial court denied the motion, and Nationwide appealed.

North Carolina's declaratory judgment statute is substantially similar to Kentucky's and provides:

> Any person interested under a . . . written contract . . . or whose rights, status or other legal relations are affected by a . . . contract . . . may have determined any question of construction or validity arising under the . . . contract . . . and obtain a declaration of rights, status, or other legal relations thereunder.

Id. at 799 citing N.C. Gen.Stat. § 1-254 (1999). Compare KRS 418.045. Construing this statute, the Court held "standing to seek a declaration as to the extent of coverage under

an insurance policy requires that the party seeking relief have *an enforceable contractual right under the insurance agreement*." Id. (emphasis added).

DeMent argued he was entitled to benefits under the supplementary payment provision which provides "we will pay on behalf of an insured . . . [e]xpenses for emergency first aid to others at an accident involving any auto covered by this policy." Id. at 800. DeMent contended that as an emergency first aid recipient, he is within the class of persons whom the provision was intended to benefit. He, therefore, claimed "an enforceable contractual right as a third-party beneficiary of the . . . policy, which right confers standing in him to seek declaratory relief." Id.

The Court disagreed, concluding that Nationwide's obligation to pay first aid expenses "on behalf of any insured" flows primarily and directly to the insured. Id. at 801. The Court held, "Because the benefit running to plaintiff by reason of the provision is merely incidental, he is without standing as a third party beneficiary to seek enforcement of the covenant or a declaratory judgment as to its terms." Id. See also, Long v. McAllister, 319 N.W.2d 256, 262 (Iowa 1982) (holding that "[b]ecause plaintiff relies only on the fact that he will benefit if the contract is carried out in accordance with its terms, he has alleged only a basis for finding that he is an incidental beneficiary."); Molina v. American Alternative Ins. Corp., 699 N.W.2d 415, 419 (Neb. 2005) (liability policy fails to create any rights enforceable by injured parties as third-party beneficiaries).

Like the policy in DeMent, the AISLIC policy, which provides indemnification to the insured when it is legally required to pay damages to others, flows primarily and directly to Parkview. McCown is merely a potential incidental beneficiary, if and only if

it obtains a judgment or settlement that exceeds $1 million. Such status is insufficient to confer standing to seek a declaratory judgment as to the terms of the AISLIC policy.

Because McCown lacks standing either as a party to the policy or a third-party beneficiary thereof, the Court of Appeals erred when it held that McCown's declaratory judgment action is proper.

B. The Court of Appeals Erred in Holding There is a Bankruptcy/Insolvency Exception to the Rule Prohibiting a Plaintiff From Suing a Defendant's Insurer.

McCown's counsel conceded in its response to AISLIC's writ that "a declaratory judgment action to determine insurance coverage is typically not available to an injured third party prior to judgment in the underlying action." (McCown's response to petition for writ, p. 5, attached as Ex. J). However, the Court of Appeals accepted McCown's contention that a line of cases recognize an exception to this rule in cases of insolvency or bankruptcy. Any reliance on such cases to conclude an exception exists is entirely misplaced, because such "exception" is a misnomer. A review of the case law clearly establishes there is no bankruptcy/insolvency exception to the rule against direct actions, and that a judgment even against bankrupt or insolvent insureds must be obtained before their insurer can be sued.

As will be demonstrated below, all of the cases on which McCown and the Court of Appeals rely to find a bankruptcy/insolvency exception emanate from New York Indem. Co. v. Ewen, 298 S.W. 182 (Ky. 1927). There, the Court did not hold an injured party could sue the liability insurer before obtaining a judgment against the insured. Rather, it followed the rule that a plaintiff can sue the insurer only *after* obtaining a judgment in the tort action. See id. at 185.

In Ewen, the plaintiff was injured in a car accident and sued the owners and operator of the vehicle in which she was a passenger. She also sued the defendants' insurer alleging the defendants were insolvent. The insurance policy contained the following provision:

> The insolvency or bankruptcy of the assured shall not relieve the company from the payment of the indemnity provided by the policy, but shall entitle the claimant to maintain an action against the company for the recovery of such indemnity.

298 S.W. at 183.[3] The Court construed this provision as providing indemnity "against loss from liability" and held that if after a judgment had been obtained against the insured and the injured party was unable to collect the judgment because of the insured's insolvency or bankruptcy, "then and only in that event the insurance company would be responsible to the injured party in a direct action." Id. at 184. The Court concluded:

> We are of the opinion, then, that under this policy the appellee had no right to join the insurance company with the assured, and that she had no direct cause of action against the insurance company until she had obtained a judgment against the assured and established the latter's insolvency or bankruptcy by having an execution issued on such judgment and a return of "no property found" made on such execution.

Id. at 185. Thus, far from creating an exception, the Court applied the rule prohibiting direct actions against insurers even where the insureds are insolvent or bankrupt.

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[3] Perhaps the courts in the subsequent cases gleaned an exception from this language. However, as set forth below, the Court in Ewen went on to hold that the insurer may be sued only *after* judgment was rendered against the insured. While the policy language in Ewen did not say when the claimant may maintain an action against the insurer, the AISLIC policy does contain a temporal component—it provides that an action can be brought against it only after an agreed settlement or a judgment following an actual trial. Thus, if the insurer in Ewen, with a policy that is silent as to the timing of an action against the insurer, can be sued by the claimant only post-judgment against the insured, the rule prohibiting direct actions applies more strongly to AISLIC whose policy explicitly bars a claim by the claimant until after an agreed settlement or judgment.

The Court in Cuppy v. General Accid. Fire & Life Assur. Corp., 378 S.W.2d 629, 632 (Ky. 1964) cited Ewen and other cases when it referred to a "possible exception of insolvency or bankruptcy." Cuppy did not involve the issue presented in this case. There, the plaintiffs filed a tort action after the one-year statute of limitations expired. They sued the defendant and his insurer alleging they were estopped to plead the limitations defense because the insurer represented that it would resolve their claim. In affirming the dismissal of plaintiffs' action, the Court cited the rule that "with the possible exception of insolvency or bankruptcy," an injured person cannot sue the insurance company in his original action against the insured. 378 S.W.2d at 632 citing Ewen, 298 S.W. 182 (Ky. 1927); Chambers v. Ideal Pure Milk Co., 245 S.W.2d 589 (Ky. 1952); Happy v. Erwin, 330 S.W.2d 412 (Ky. 1959). The Court's reference to a possible bankruptcy/insolvency exception is plainly dicta, as there was no bankrupt or insolvent defendant and the decision did not turn on the purported exception.

Additionally, even a cursory reading of the cases cited by the Court in Cuppy reveals there is no exception of insolvency or bankruptcy to the rule that a plaintiff may not sue the defendant's insurer. Chambers and Happy did not involve bankrupt or insolvent insureds, and the courts in those cases did not suggest an exception existed. And as established above, Ewen confirmed that the rule prohibiting direct actions against an insurer applies to cases involving insolvent or bankrupt insureds.

Harris v. Jackson, 192 S.W.3d 297, 302 (Ky. 2006) also fails to establish a bankruptcy/insolvency exception. That case did not involve the assertion of a tort action against a bankrupt or insolvent defendant or a direct action against a tortfeasor's insurer. Rather, the defendant sought to dismiss the tort action, which arose out of an automobile

accident, after the plaintiff failed to timely revive the action against the estate of defendant following the defendant's death. The defendant's attorney knew of his death but failed to advise the plaintiff, and the defendant's insurer continued to defend the action after its insured's death.

In denying the defendant's motion to dismiss and allowing the tort claim to proceed against the deceased defendant, the Court held that although the insurer was not a party under the long-standing precedent that an "injured person could not sue the negligent party's insurance company, except in cases of insolvency or bankruptcy," the insurer was a real party in interest and provided adequate virtual representation of the defendant. Harris, 192 S.W.3d at 302-04 citing Cuppy, 378 S.W.2d at 632. The Court's reference to the purported exception is clearly dicta.

Reliance by the Court of Appeals in footnote 4 of its Order on Ford v. Ratliff, 183 S.W.2d 199 (Ky.App. 2006) is also misplaced. In that case, the plaintiff settled a personal injury lawsuit with the defendants but reserved the right to pursue its lawsuit to the extent of any coverage provided by the defendants' liability insurer. The plaintiff thereafter amended its complaint to sue the insurer directly, which the trial court dismissed. The Court of Appeals affirmed, citing the rule that "an injured person cannot sue the insurance company in his original action against the insured." Id. at 203 citing Cuppy, 378 S.W.2d at 632. The Court of Appeals then said in a footnote in dicta that Cuppy excepted from this rule cases of insolvency and bankruptcy.

Neither Cuppy, Ratliff, nor any of the other cases that suggested an exception exists involved bankrupt or insolvent insureds. The Courts simply repeated erroneous dicta casually offered by prior courts without having reviewed the initial case from which

the exception purportedly originated, Ewen. Ewen *did* involve a bankrupt insured, but nevertheless applied the rule prohibiting actions against insurers before judgment is obtained against defendants, even if they are bankrupt or insolvent.

Even if this Court were to create a bankruptcy/insolvency exception, it would not and should not apply in this case. The irony of McCown's reliance on this purported exception is that his claim would had been payable in full (to the extent meritorious) notwithstanding the bankruptcy case, but for McCown's failure to timely assert its post-petition claim in the bankruptcy proceedings. AISLIC is an excess carrier which provides coverage of $1 million over and above Parkview's self-insured retention of $1 million per occurrence. Parkview's $1 million self-insured retention would have been available to pay McCown's claim (if meritorious(had McCown timely asserted it in the bankruptcy proceedings. Thus, the mere filing of Parkview's bankruptcy did not bar McCown from recovering against Parkview, and McCown therefore should not be permitted to invoke this declaratory judgment action,

The decision in Padgett v. Long, 453 S.W.2d 272 (Ky. 1970) confirmed that the insolvency of the insured does not allow a plaintiff to sue the insurer before obtaining judgment in the tort action. In that case, the defendants filed a bankruptcy petition after being sued for injuries the plaintiff sustained in a construction accident. After the bankruptcy court discharged their potential liability, the plaintiff's claim was dismissed. The plaintiff moved to set aside the dismissal and attempted to amend the complaint to add the defendants' insurer as a defendant. The trial court upheld its dismissal and did not enter an order on the motion to amend the complaint.

On appeal, Kentucky's then highest court looked to the language of the policy, which is similar in all pertinent respects to AISLIC's policy and provided that "[n]o action shall lie against the company . . . until the amount of the insured's obligation to pay shall have been finally determined either by judgment against the insured after actual trial or by written agreement of the insured, the claimant and the company." Id. at 274. The Court held that rather than dismissing the plaintiff's claim against the defendants because of their bankruptcy, the trial court should have allowed the plaintiff to establish the claim without permitting enforcement against the defendants. The judgment, "if obtained, would be collectible only by claiming against the insurance company." Id. at 276.

The Court concluded that "[n]o error was committed in not granting the request to make the insurance company a party to this action." Id. citing Ewen, Moores and Cuppy. It held that it was unnecessary "at least before establishing and liquidating the claim, to bring in the insurance company as a party defendant." Id.

As established above, Kentucky law clearly prohibits an injured person from suing the tortfeasor's insurer prior to obtaining a judgment against the insured. Given this long-standing rule, Kentucky courts would apply the prohibition against direct actions where the plaintiff seeks to litigate coverage issues under the applicable policy. McCown's counsel acknowledged as much and espoused a non-existent exception to this rule in cases of insolvency or bankruptcy in a fruitless attempt to maintain its declaratory judgment action against AISLIC. Regardless, a bankruptcy/insolvency exception would not apply, because Parkview's $1 million self-insured retention would have been

available to satisfy McCown's claim had McCown timely filed a post-petition claim with the bankruptcy court.

Accordingly, the Court should reverse the Court of Appeals order denying AISLIC's writ, and prevent the trial court from acting without jurisdiction in maintaining such action.

II. Even if the Court Acted Within Its Authority, but Erroneously, AISLIC is Entitled to a Writ of Prohibition and/or Mandamus Because It Has No Adequate Remedy by Appeal and It Would Suffer Great and Irreparable Injury if the Writ is Denied.

As set forth above, the trial court acted beyond its jurisdiction when it failed to dismiss McCown's declaratory judgment action against AISLIC, which is reason alone to reverse the Court of Appeals Order and grant a writ of prohibition and/or mandamus. Notwithstanding the sufficiency of this first basis on which to grant a writ, assuming *arguendo* that the trial court was within its jurisdiction but erroneously denied AISLIC's motion to dismiss, a writ is also warranted under the second class of cases. In these cases, the petitioner must establish that it has (1) no adequate remedy by appeal, and (2) it will suffer great and irreparable injury if the writ is denied. Newell, 158 S.W.3d at 754.

A. AISLIC Has No Adequate Remedy by Appeal if the Trial Court Maintains the Declaratory Judgment Action.

The first requirement of "no adequate remedy by appeal" means that "any injury to [petitioner] could not thereafter be rectified in subsequent proceedings in the case." Id. In the present case, the harm to AISLIC if the Court does not grant a writ is having to incur vast expense to defend a declaratory judgment action that Kentucky case law clearly holds is improper. This harm cannot be rectified in subsequent proceedings, because AISLIC cannot recover the litigation expense regardless of the outcome of the declaratory judgment action. Moreover, if McCown fails to obtain a judgment against

The rule prohibiting direct actions against insurers essentially makes insurers

Parkview, a prior declaration that the AISLIC policy covers McCown's claim is worthless to McCown. In such instance, AISLIC would have needlessly incurred expense to defend McCown's declaration of rights action where coverage under the policy was never implicated.

This harm is analogous to a writ of prohibition to prevent a trial court from compelling disclosure of privileged documents. In St. Luke Hospitals, Inc. v. Kopowski, 160 S.W.3d 771 (Ky. 2005), the Court held that there is no adequate remedy on appeal "because privileged information cannot be recalled once it has been disclosed." Id. at 775. Here, once AISLIC has incurred significant legal expense in defending the declaratory judgment action, it cannot be recouped. Thus, there is no adequate remedy on appeal if the Court does not grant a writ of prohibition and/or mandamus.

While some Kentucky courts have held that the expense of litigation is insufficient to show inadequate remedy by appeal and great and irreparable injury (see, e.g., Brown v. Knuckles, 413 S.W.2d 899 (Ky. 1967)), AISLIC is in a different position than the vast majority of other defendants who seek interlocutory relief from the denial of a motion to dismiss. Unlike some defendants, who may not be liable as a matter of law but must still answer and defend the lawsuit against it, Kentucky law is clear that AISLIC is *not* subject to being sued in a direct action by an injured party prior to judgment against the insured. Without the right to seek a writ prohibiting the trial court to entertain McCown's direct action, the rule against such an action is effectively subverted.

The rule prohibiting direct actions against insurers essentially makes insurers immune from such actions. The United States Supreme Court has held that the denial of a defense of absolute immunity "is an order appealable before final judgment, for the

essence of absolute immunity is its possessor's entitlement not to have to answer for his conduct in a civil damages action." Mitchell v. Forsyth, 472 U.S. 511, 525, 105 S.Ct. 2806, 86 L.Ed.2d 411 (1985) (emphasis added).

Likewise, the essence of the rule in Kentucky prohibiting direct actions against insurers is the insurers' entitlement not to have to litigate whether coverage is afforded under a policy unless and until a judgment is rendered against the insured. Accordingly, AISLIC would not have an adequate remedy at law if the trial court entertains McCown's declaratory judgment because the damage of having to defend such action will have already been inflicted by the time AISLIC would file an appeal.

B. Maintenance of the Declaratory Judgment Action Violates Kentucky Law Against Direct Actions.

The second requirement of great and irreparable injury means "something of a ruinous nature." Bender v. Easton, 343 S.W.2d 799, 800 (Ky. 1961). Such a showing is not an absolute prerequisite, however:

> The requirement may be put aside in "*certain special cases* . . . [where] a substantial miscarriage of justice will result if the lower court is proceeding erroneously, *and* correction of the error is necessary and appropriate in the interest of orderly judicial administration.

Grange Mut. Ins. Co. v. Trude, 151 S.W.3d 803, 808 (Ky. 2004) citing Bender, 343 S.W.2d at 801 (emphasis in original). These special cases "tend to be limited to situations where the action for which the writ is sought would violate the law, e.g. by breaching a tightly guarded privilege or by contradicting the requirements of a civil rule." Id. (emphasis added). In those cases, "a court may peek behind the curtain, i.e., beyond

the petitioner's failure to meet the great and irreparable harm test, at the merits of the petitioner's claim of error by the lower court." Id.[4]

Here, allowing the declaratory judgment action to proceed would violate clear Kentucky law that expressly prohibits such actions where the plaintiff has not yet obtained a judgment against the insured in the underlying tort action. Establishing a right in a stranger to the insurance contract to contest coverage before judgment against the insured would also cause shock waves in the insurance industry. Every time an insurer defends under a reservation of rights, it could be haled into court by an injured party seeking to invalidate the reserved coverage defenses. This has never previously been permitted and could inundate the courts with declaratory judgment actions, which will be moot to the extent that the injured person fails to obtain a judgment against the insured. Such would be a waste of judicial resources.

Simply put, correction of the trial court's error in proceeding with McCown's declaratory judgment action is "necessary and appropriate in the interest of orderly judicial administration" and will avoid a substantial miscarriage of justice. Trude, 151 S.W.3d at 808. Thus, AISLIC is entitled to the writ of prohibition/mandamus.

CONCLUSION

For all the foregoing reasons, AISLIC respectfully requests the Court to enter the attached Order reversing the Court of Appeals Order, and granting a writ of prohibition and/or mandamus to preclude the trial court from hearing the declaratory judgment action and require the trial court to dismiss such action against AISLIC.

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[4] The same relaxed *de novo* review standard in granting a writ of the first class where the trial court is acting without jurisdiction applies to those writs of the second class "where the alleged error [of the trial court] invokes the 'certain special cases' exception or where the error involves a question of law." Trude, 151 S.W.3d at 810.

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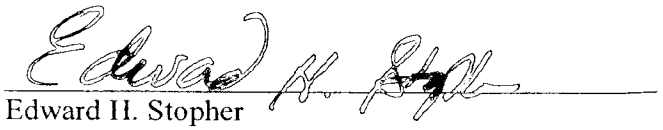

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