SUPREME COURT OF KENTUCKY
CASE NOS. 2008-SC-000037-DG and 2008-SC-000044-DG

ASSOCIATED INSURANCE SERVICE, INC. — APPELLANTS
AND
AON RISK SERVICES, INC. OF OHIO

v.

APPEAL FROM COURT OF APPEALS
CASE NO. 2006 CA-001737-MR AND
JEFFERSON CIRCUIT COURT
CASE NO. 02-CI-009027

DANIEL GARCIA, M.D. — APPELLEES
AND
RITA GARCIA

REPLY BRIEF OF APPELLANT, AON RISK SERVICES, INC. OF OHIO

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CERTIFICATE OF SERVICE

It is hereby certified that true and correct copies of this Reply Brief of Appellant, Aon Risk Services, Inc. of Ohio, were served, by first class mail, postage prepaid, this 22nd day of January, 2009, upon the following: Lee E. Sitlinger, Sitlinger, McGlincy, Theiler & Karem, 370 Starks Building, 455 S. Fourth St., Louisville, Kentucky 40202; Larry B. Franklin, Franklin Law Group, 505 W. Ormsby, Louisville, Kentucky 40203; Frank P. Doheny, Jr. and Michael C. Merrick, 1400 PNC Plaza, 500 W. Jefferson St., Louisville, Kentucky 40202; Hon. Geoffrey P. Morris, Jefferson Circuit Court, Division 11, 700 W. Jefferson, Louisville, Kentucky 40202; and the Clerk of the Kentucky Court of Appeals, 360 Democrat Dr., Frankfort, Kentucky 40601.

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STATEMENT OF POINTS AND AUTHORITIES

Appellant, Aon Risk Services, Inc. of Ohio ("ARS Ohio"), submits this Reply to the Brief for Appellees, Daniel and Rita Garcia (the "Garcias"), in Response to ARS Ohio's Appellant Brief ("Brief").

INTRODUCTION

The Garcias' Brief for Appellees ("Response") is an exercise in contradiction, on the one hand arguing that ARS Ohio, as the insurance broker in the transaction, was neither a "necessary", "appropriate" or even "permissible" party to the arbitration proceeding between the insured Star and the personal injury plaintiff Garcias, and that "**[t]he arbitration in no way addressed any claims of the Star against its agent or broker** (Associated or AON)", yet on the other claiming that the arbitration award against the Star for the Garcias' personal injury damages (including loss of consortium) should actually be imposed against ARS Ohio as the insurance broker. Compare Response pp. 5 (emphasis in original) and 22-23, with pp. 5-6.[1] Setting aside for a moment whether an arbitration award is even binding upon a non-party to the arbitration, which it is not, there is a clear distinction between the personal injury damages the Garcias may be entitled to recover as a result of the Star's conceded negligence, as opposed to the damage claim the Star may have against its agent or broker for alleged negligent procurement of insurance.

Even more troubling, however, is the Garcias' refusal to address or even attempt to refute the majority of the points raised in ARS Ohio's Brief. More importantly, the Garcias fail to address the core issue presented to this Court on discretionary review – the validity and enforceability of a purported assignment by an insured of a stipulated "claim" as the basis for a professional negligence claim against a third party insurance

[1] To the extent that the Garcias attempt to press this issue to this Court it is not preserved, as the Garcias did not file a cross-motion for discretionary review of that aspect of the Court of Appeals' Opinion.

broker, and the public policy concerns of collusion and unfairness inherent in and that disfavor this type of arrangement. Simply put, the Garcias' Response wholly fails to analyze the propriety of holding an insurance agent, let alone an insurance broker, liable for a stipulated judgment that the agent and broker were not even party to based upon the unanticipated failure of an insurance carrier years after the applicable policy was in effect. Refusing to directly confront the true issues before this Court is telling as to the merits of the Garcias' position.

This appeal involves a legal and public policy determination for the Commonwealth's highest court to decide, rather than simply an affirmance or denial of the trial or appellate court decisions. This Court is the final arbiter of the law in Kentucky, and has the authority to declare whether these types of contrived assignments – especially against a far removed insurance broker – are disfavored and void as a matter of law and pursuant to public policy. Accordingly, ARS Ohio respectfully requests that this Court reverse the Court of Appeals, and dismiss the Garcias' claims against ARS Ohio with prejudice.

ARGUMENT

A. The Star Had No Valid Cause Of Action To Assign To The Garcias.

Independent of the issues raised in the next two sections below, the Star simply cannot legally assign a valid cause of action to the Garcias because, as adopted by Coffey, and as set forth in Doser, "no legal liability was ever imposed" against the Star since the Garcias agreed to forebear any collection or execution against it [Trial Record ("T.R.") at 459, 472 ¶¶ 5 and 7 and Appendix ("App.") 7 at 2]. Coffey v. Jefferson County Bd. of Educ., 756 S.W.2d 155, 157 (Ky. App. 1988); Doser v. Middlesex Mut. Ins. Co., 101 Cal. App. 3d 883, 891 (1980). The Garcias claim this argument is

"circuitous", Response p. 29, but there is nothing circuitous about requiring a party to actually have a ripe and valid cause of action to assign before assigning it.

The fact that the Star had no cognizable claim to assign is further reiterated by the provisions of the applicable insurance policy with HIH, yet the Garcias completely ignored this key point in their Response. The HIH policy specifically limits the covered amount the insurance carrier will reimburse to "such sums as the assured, as owner of the FLEET PER SCHEDULE **shall have become legally liable to pay and shall have paid** on account of: Loss of life, or injury to, or illness of, any person . . ." [T.R. at 387, Ex. 1 and App. 4 at 25] (emphasis added). The Star never became "legally liable to pay", nor did it actually pay, *anything* to the Garcias. The "claim" the Star assigned to the Garcias simply had no value or legally cognizable existence.

Finally, the Garcias simply failed to present any evidence in the record to overcome the trial court's entry of summary judgment in favor of ARS Ohio. This case was pending in the trial court since 2002, affording the parties ample opportunity to conduct discovery.[2] Indeed, and although ignored by the Garcias, it is undisputed that ARS Ohio lacked privity of contract with the Star as a result of the "agent of record" status conferred by the Star upon its agent, Associated. See Brief pp. 2-3. Accordingly, the Star lacked privity and standing to assign a claim against ARS Ohio. The Star, not ARS Ohio, even made the decision to purchase insurance from HIH, largely as a cost savings measure. Id. at 4.

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[2] In yet another example of contradiction, and in a half-hearted attempt to respond to ARS Ohio's point that these types of assignments are undesirable because they produce and prolong litigation, the Garcias contend that assignments like the one they entered into with the Star are laudable because they actually "minimize and expedite the resolution of such cases." Response p. 32. Using this case as an example, it is clear that the contrived assignment reached by the Garcias and the Star has in no way expedited the resolution of the Garcias' case. In fact, the Garcias could have resolved their claims against the Star almost a decade ago in their personal injury lawsuit, but instead elected to pursue the invalid assignment at issue here, which has led to a second lawsuit that has dragged on for almost seven years.

Instead, the Garcias repeatedly assert in their Response that "[d]iscovery in this case has clearly demonstrated that both Associated and AON were negligent in placing the Star's insurance coverage with HIH Insurance" (Response pp. 6 and 29) but, tellingly, fail to provide *any* cite to the record in support of that bold, conclusory and erroneous statement. The reason is because such evidence does not exist. Rather, the record in this case reflects that at the time the 1997 policy at issue was written (the policy covering the Garcias' April, 1998 injury), neither ARS Ohio, nor the insurance industry for that matter, had any knowledge that HIH was having any financial difficulties. The question is not what the broker knows in hindsight, four years after the applicable policy was written, but what the broker actually knew at the time the policy was written. The applicable testimony in the record, which was elicited from the agent of record in the transaction, establishes that ARS Ohio was *not* negligent because HIH was not only a large, solvent and financially stable insurance company, but highly rated by a reputable firm, at the time the applicable policy was written. [T.R. at 786-788, and Wetterer Depo., App. 3 at 7-8 and 172-173.][3] Only afterwards, based upon hindsight unavailable to ARS Ohio in 1997, has it been disclosed that HIH management was intentionally and criminally misrepresenting the true financial condition of HIH in order to hide it from the insurance industry and the public, resulting in HIH being placed in receivership four years later in 2001. [T.R. at 786-788, Bell Depo. at 160, 165, 168-169, 177-178, Wetterer Depo. at 6-7 and App. 5 and 6].[4]

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[3] See Cherokee Ins. Co. v. E.W. Blanch Co., 66 F.3d 117, 122, 124 (6th Cir. 1995) (granting the insurance broker summary judgment on a negligence claim for allegedly failing to examine the financial strength of reinsurers that the broker recommended, and in doing so recognizing the propriety of an insurance broker relying upon a similar rating company).

[4] Once again the Garcias boldly contend, with absolutely no legal, factual or record support, that their "expert witnesses will testify that both AON and Associated were negligent in the procurement of liability insurance for the Star", and that ARS Ohio owed some continuing obligation to the Star to monitor the financial condition of HIH. Response pp. 6-7 and 28-29. If the Garcias actually had such critical and

If the Garcias' requested relief is granted, this Court would be countenancing what would likely become a flood of malpractice suits against insurance brokers (or other professional advisors) based solely upon a retrospective standard of care. These types of contrived assignments simply should not be allowed. Given the evidence in the record, the Star had no valid cause of action to assign, and the trial court was correct in entering summary judgment in favor of ARS Ohio.

B. Existing Kentucky Law Prohibits Agreements That Create The Risk of Collusion And Illusory Damage Awards In The Insurance Context.

Despite the Garcias' strained efforts to distinguish that authority, the Court of Appeals has previously declared – in a published decision – that these types of agreements are void and unenforceable because they involve the assignment of non-cognizable claims, violate public policy and create an unacceptable risk of collusion to impose liability on a third party. Coffey, 756 S.W.2d at 156-57 (relying primarily on Doser, 101 Cal. App. 3d 883). See also Strahin v. Sullivan, 647 S.E.2d 765, 773 (W. Va. 2007).[5]

Significantly, by principally relying on the California Court of Appeals decision in Doser – a case invalidating the assignment of an *insurance* related claim – the Coffey decision clearly suggests that its holding against collusive assignment agreements applies beyond the legal malpractice paradigm. Yet, the Court of Appeals and the Garcias completely overlooked this important contextual issue.[6] The Court of Appeals

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crucial evidence against ARS Ohio, especially in the face of a dispositive motion, they obviously should have presented it to the trial court. Indeed, the Garcias had more than ample time to present any such evidence, as the case was filed as far back as 2002. The bottom line is that no such evidence exists. In any event, the trial court made its decision based upon legal rather than factual issues and purported expert opinions. Finally, the contention that ARS Ohio had a continuing obligation to monitor the financial condition is a baseless "red herring" because the Garcias were injured during the Star's *first* policy period with HIH, rather than the two subsequent policy periods.

[5] These cases are addressed and analyzed in detail on pp. 13-17 of the Brief.

[6] While the Court of Appeals cited Coffey in support of its Opinion, it failed to consider Coffey in the

compounded this error by placing reliance on cases purportedly upholding the "sort of agreement at issue here," even in the face of asserted "collusion between the settling parties." [App. 1 at 9].[7]

Indeed, none of the cases cited by the Garcias or relied upon by the Court of Appeals actually supports the assignment in this case. Instead, the cases they cite[8] merely reflect the proposition that assignment agreements against insurance companies – as opposed to insurance *brokers* – are typically upheld "[w]here an insurer denies coverage of a claim against its insured, refuses to defend, or unreasonably refuses to settle [as in Terrell, Grundy and State Farm]." [App. 1 at 3-4]. What the Garcias fail to recognize in their Response at pp. 9 and 30-32 is that these Kentucky cases would not even allow assignments against insurers (much less a broker) predicated on collusion, and an unenforceable damage calculation. See Ayers v. C&D Gen. Contractors, 269 F. Supp. 2d 911, 915 (W.D. Ky. 2003) (predicting Kentucky law regarding an assignment against an insurance carrier after a consent judgment and covenant not to execute, and noting that a court must look "carefully" at these types of assignments for "collusion" and a "reasonable calculation of damages").[9]

The Garcias strangely contend that Doser and Strahin, which involve assignments

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context of collusive assignments involving insurance claims and instead looked to authority outside of Kentucky, an error which ARS Ohio cited in its Brief at pp. 23-27. [App. 1 at 8-11].

[7] The Garcias attempt to avoid this issue by noting that the Honorable Ken Corey, in performing his duties as an arbitrator, would never engage in any form of collusion. See Response pp. 25 and 30. Of course, ARS Ohio in no way suggests that Judge Corey engaged in any form of collusion. Nor does ARS Ohio contend that actual collusion needed to occur in order to invalidate this assignment. Rather, the mere risk of collusion is a public policy justification enough for invalidating these types of assignments. The bottom line is that the type of pre-arbitration assignment agreement reached between the Star and the Garcias presents an unnecessary risk of collusion that should not be sanctioned.

[8] Terrell v. The Western Cas. & Sur. Co., 427 S.W.2d 825 (Ky. 1968); Grundy v. Manchester Ins. & Indem. Co., 425 S.W.2d 735 (Ky. 1968); State Farm Mut. Auto. Ins. Co. v. Marcum, 420 S.W.2d 113 (Ky. 1967).

[9] The analysis adopted in Ayers and championed by the Garcias involves an assignment against an insurer, not an assignment against the insurance agent or broker, and in no way considers or analyzes the inherent policy differences between assignments against insurers versus agents or brokers.

against insurance companies rather than agents or brokers, are inapplicable because "the insurance company [unlike the agent or broker] is directly involved in both the defense and indemnification of the tort claims against its insured or affirmatively elects not to defend its insured." Response p. 29 and Note 17. However, the fact that Doser and Strahin precluded an assignment against an insurer actually underscores the impropriety of allowing such an assignment against an insurance broker who, unlike the insurer, performed a limited, ministerial function in the Star's search for a new carrier.

Neither the Court of Appeals nor the Garcias specifically considered or analyzed the distinct role of an insurance *broker* like ARS Ohio, or the limited function performed by ARS Ohio in this matter. The Court of Appeals and the Garcias make a leap of logic and lump together assignment of claims against insurance companies, insurance agents and insurance brokers. A more thorough analysis reveals why an insurance broker, such as ARS Ohio, should not be subjected to the Garcias' assigned claim under the circumstances of this case.

The public policy concerns against assignments expressed in Coffey, Doser and Strahin apply with particular force to an insurance broker like ARS Ohio under these circumstances. The Star's stipulated arrangement was particularly prejudicial to ARS Ohio, which had no privity of contract with the Star or the Garcias, and is not the guarantor of the financial stability of an insurance company years into the future. See Brief pp. 2-4 and 19-20. While such a stipulation of liability may be enforceable in appropriate circumstances against the insured's insurance company – which was paid premiums to insure the risk in question – such an arrangement is unfair to a third party insurance broker that had a distinct and limited involvement in the policy transaction. ARS Ohio should not be subjected to liability for a risk it never assumed. Indeed, these

points were raised and adopted in the very case cited by the Garcias as a basis for *not* allowing these types of collusive and stipulated assignments against insurance *agents*:

> In contrast, an insurance agent generally has no contractual duty to defend and indemnify the client. Our prior holdings that an insurer may be bound in certain circumstances by a judgment entered against the insured arose out of, and are limited to, the insurer-insured relationship. Absent such a relationship, we do not perceive, and Gittlen has not suggested, any basis for concluding that insurance agents would be bound by stipulated judgments to which they were not parties.

Webb v. Gittlen, 174 P.3d 275, 280-81 (Ariz. 2008), which is attached at Tab 5 to the Garcias' Response.

In this non-insurer context, any possible usefulness to these types of assignments is far outweighed by the concern with the risk of potential collusion and unfairness.

C. The Arbitration Award Simply Has No Bearing on ARS Ohio, And The Agreement Cannot Be Re-written To Change That.

The Garcias contend that the arbitration and resulting personal injury damage Award should be imposed against ARS Ohio as the insurance broker, yet at the same time suggest that ARS Ohio was not a necessary, appropriate or even a permissible party to the arbitration. See Response pp. 5-6 and 22-23. This argument, while not preserved for review,[10] fails in any event, as there is a clear distinction between the personal injury damages the Garcias may be entitled to recover for the Star's conceded negligence as opposed to the damage claim the Star may have against its agent or broker for alleged negligent procurement of insurance.

The bottom line is that the Star never actually incurred *any* alleged damages because it was relieved of responsibility for damages well before the Garcias and the Star created a damage award, and the Award in this case did not even address the Star's alleged claims against ARS Ohio. Just as in Doser, and despite the Garcias' arguments to

[10] Again, this argument is unpreserved as the Garcias' failed to file a cross-motion for discretionary review.

the contrary, ARS Ohio was not even a party to the Arbitration Agreement and did not participate in any way in, nor was it notified of, the arbitration.[11] Doser, 101 Cal. App. 3d at 893. Because the Star was relieved of exposure to damages prior to the arbitration, it was not motivated to challenge, or even participate in, the arbitration. Strahin, 647 S.E.2d at 773. Indeed, and despite the Garcias' hollow suggestions to the contrary, neither the Award, nor the record, identifies any evidence offered, or arguments made, by the Star during the arbitration, underscoring the illusory nature of the transaction at hand.[12] The Award was meaningless because, by agreement, it could not be collected from the Star.[13]

Even if there was no actual intended collusion between the Star and the Garcias, public policy dictates that a claim which the assignor/insured is not legally liable to pay creates a clear and unacceptable risk of collusion in setting a damage amount in which the assignor has no interest or motivation to defend. The Court of Appeals and the Garcias overlook the impropriety of re-writing the agreement between the parties given

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[11] The Garcias continue to contend, with absolutely no citation to the record or evidence, in violation of CR 76.12(4)(c)(v), that ARS Ohio was provided notice of, invited to and had an opportunity to attend the arbitration. See Response pp. 5, 23, 26 and 35. Setting aside for a moment that the Garcias also contend, in direct contradiction, that ARS Ohio was not even a "permissible" or "appropriate" party to the arbitration, there is absolutely no support for the Garcias' contentions. See Response p. 23. ARS Ohio confirmed in its trial court briefing on at least three occasions that it was never notified of, invited to or provided an opportunity to attend the arbitration, and has also confirmed this inaccuracy at both appellate court levels. See Brief pp. 8 and 17. The Garcias have provided no evidence to the contrary.

[12] The Garcias also continue to contend, that the arbitration proceeding was somehow "adversarial", suggesting that the Star actually presented evidence to contest the Garcias' claims. See Response pp. 5 and 23. Yet, the lack of evidence of any defense presented by the Star at the arbitration has also been raised by ARS Ohio on at least three occasions at the trial court level, as well as at both appellate court levels. See Brief p. 18. In violation of CR 76.12(4)(c)(v), there simply has been no factual, legal or record evidence whatsoever presented by the Garcias at any time suggesting that the Star did anything other than acquiesce at the arbitration.

[13] While wholly ignored by the Garcias in their Response, pursuant to paragraph 11 of the Arbitration Agreement, the Star was required to provide at least thirty (30) days notice of the arbitration to ARS Ohio. The Star's failure to notify ARS Ohio, violating numerical paragraph 11 of the Arbitration Agreement, independently voids the entire Arbitration Agreement (and assignment) as set forth in numerical paragraph 12, which expressly provides: "Violation of any portion of this agreement, absent good cause shown, voids this entire agreement." [T.R. at 473 and App. 7 at 3].

this recognized risk of collusion, and propose a "re-do" of the damages' recalculation. See App. 1 at 10-11 and Response pp. 27-28. However, as set forth in ARS Ohio's Brief, the damages methodology was an integral component of the overall assignment agreement, and cannot simply be written out of that agreement by judicial fiat. See Brief pp. 27-28. That is especially so given that the Garcias and the Star agreed that the Garcias retained their right to seek reimbursement from the Star in the event there was ever any issue concerning the validity of the assignment. [T.R. at 472-473 par. 10 and App. 7 at 2-3]. It also bears repeating that there is nothing to prevent the Garcias from pursuing the Star for its admitted liability, as no evidence has established that the Star, which continues to do business, is judgment proof or unable to satisfy any judgment in favor of the Garcias. [T.R. at 757-776 and App. 8]. The arbitration Award simply has no bearing on ARS Ohio, and there is no permissible basis for the Court of Appeals to rewrite the parties' agreement.

CONCLUSION

For the foregoing reasons, ARS Ohio requests that this Court reverse the Court of Appeals, and affirm the summary judgment entered by the Jefferson Circuit Court which dismissed all of the Garcias' claims against ARS Ohio with prejudice.

Respectfully submitted,

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