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APPROVAL OF THE APPELLATE DIVISION

SUPERIOR COURT OF NEW JERSEY
APPELLATE DIVISION
DOCKET NO. A-3530-12T3

ROBERT D. FERGUSON, KANSA
INTERNATIONAL CORPORATION,
LTD., BANKRUPTCY ESTATE,
MILO FAMILY LIMITED PARTNERSHIP,
IMIPOLEX, LLC, and OMPHALOS, LLC,

Plaintiffs-Appellants,

v.

TRAVELERS INDEMNITY COMPANY,
and EXECUTIVE RISK SPECIALTY
INSURANCE COMPANY,

Defendants-Respondents.

Argued May 5, 2014 – Decided August 4, 2014

Before Judges Yannotti, St. John and Manahan.

On appeal from Superior Court of New Jersey, Law Division, Mercer County, Docket No. L-2911-11.

Robert E. Bartkus and Francis J. Menton, Jr. (Willkie Farr & Gallagher LLP) of the New York bar, admitted pro hac vice, argued the cause for appellants (Dillon, Bitar & Luther, L.L.C. and Mr. Menton, attorneys; Mr. Bartkus and Mr. Menton, on the briefs).

Brian M. Sher argued the cause for respondent Travelers Indemnity Company (Kaufman Borgeest & Ryan, LLP; attorneys;

Mr. Sher and Joan M. Gilbride, of the New York bar, admitted pro hac vice, on the brief).

Michael O. Kassak argued the cause for respondent Executive Risk Specialty Insurance Company (White and Williams, LLP, attorneys; Mr. Kassak, of counsel and on the brief; Edward M. Koch and Edward F. Beitz, on the brief).

PER CURIAM

Plaintiffs appeal from the Law Division's order entered February 21, 2013, which granted, with prejudice, the motions of defendants Travelers Indemnity Company (Travelers) and Executive Risk Specialty Insurance Company (ERSIC) to dismiss the complaint for lack of standing. For the reasons that follow, we reverse and remand to the Law Division.

I.

Plaintiffs Robert D. Ferguson, Kansa International Corporation, Ltd., Bankruptcy Estate, Milo Family Limited Partnership, Imipolex LLC and Omphalos LLC (collectively, plaintiffs) are former shareholders of Lion Holding, Inc. (Lion), an insurance holding company. Lion's principal operating companies were Clarendon America Insurance Company and Clarendon National Insurance Company, which, for simplicity, we will refer to collectively as "Clarendon."

In 1993, Clarendon retained Raydon Underwriting Management Company Limited (Raydon), based in Bermuda, as an outside

program manager and managing general agent. In that capacity, Raydon conducted an evaluation of a reinsurance program known as LMX[1] and encouraged Clarendon to begin writing LMX reinsurance in 1994. According to the allegations in plaintiffs' complaint, Raydon failed to either recognize or disclose substantial flaws in the LMX program, which generated significant risk to Clarendon. By the end of 1995, Clarendon ceased participating in LMX.

In 1999, plaintiffs sold Lion and its subsidiaries, including Clarendon, to Hannover Ruckversicherungs-Aktiengesellshaft (Hannover), a large reinsurer. In order to ameliorate Hannover's reluctance to consummate the purchase, plaintiffs reduced the sale price by $25 million and indemnified Clarendon-Hannover up to $50 million against losses in connection with the troubled LMX program. In exchange for that indemnification, plaintiffs became contractually subrogated to Clarendon. They were assigned Clarendon's rights and claims against third parties, including claims against Raydon, the company whose conduct allegedly caused Clarendon to participate in the LMX program.

[1] As stated in the complaint, the LMX program "reinsured risks assumed under direct insurance policies that provided personal accident and death benefits to individuals."

Following the sale, several "excess reinsurers" involved in the LMX program with Clarendon "sought to avoid" their agreements based partly on "submissions for reinsurance prepared by Raydon." Clarendon thereafter entered into "working group" settlements with other LMX participants, apparently causing the company "to lose the basic reinsurance protection upon which it had conditioned its entry into the program." Plaintiffs and Hannover disputed the amount Hannover was entitled to under their indemnity agreement, and almost $24 million from the sale proceeds was withheld in escrow from plaintiffs.

In late 2005, plaintiffs brought an action against Raydon in Bermuda, uncontested by the defunct Raydon, and on September 28, 2011, obtained a judgment for damages in the amount of $92.137 million. Raydon did not contest or otherwise participate in those proceedings. That judgment, however, remains unsatisfied because Raydon has no known operations or assets.

In order to serve as Clarendon's MGA, Raydon was required to obtain "errors and omissions" liability insurance protection (the Gulf Policy),[2] which was secured in or about July 1997

[2] According to the allegations in the complaint, a company called Stirling Cooke Brown Holdings, Ltd. (SCB) is the named insured under the Policy, which apparently covers losses of any SCB (continued)

through Gulf Insurance Company, to which Travelers is now the successor company after a January 2005 merger. As stated in the complaint, the Gulf Policy covered Raydon for losses up to $15 million incurred via claims arising from rendering or failing to render professional services.[3] ERSIC, meanwhile, issued an "Excess Indemnity Policy" (the Excess Policy) to Raydon's parent company, thereby providing $10 million in additional coverage for the same type of losses to the extent they exceeded $25 million.[4]

Neither Travelers nor ERSIC took any action after plaintiffs filed their lawsuit against Raydon in the Supreme Court of Bermuda in December 2005. However, two days before a September 28, 2011 court hearing on plaintiffs' damage application following the default judgment against Raydon, Travelers informed plaintiffs "that it was refusing to cover [p]laintiffs' losses under [the Gulf Policy]." Allegedly,

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(continued)
subsidiary. Raydon was at all relevant times a subsidiary of SCB.

[3] According to the allegations in the complaint, the Policy definition of a covered loss includes "Wrongful Acts," broadly delineated as "any actual or alleged error, misstatement, misleading statement, act, omission, neglect, or breach of duty" on the part of Raydon.

[4] According to the complaint, an intermediate layer of insurance coverage existed via an excess policy obtained through the Reliance Insurance Company, not a party to this action.

Travelers maintained that it regarded the Gulf Policy as void for breach of warranty and that Travelers, alternatively, "'hereby avoids/rescinds the policy.'" To date, Travelers has refused to pay for any losses, which plaintiffs contend are covered and compensable under the Gulf Policy. Likewise, ERSIC disputes plaintiffs' claim that the Bermuda judgment is a covered loss under its Excess Policy.

On September 28, 2011 — the same day that the Bermuda Court set plaintiffs' damages at $92 million — Travelers commenced a civil action against Raydon in the Bermuda courts, seeking a declaration that the Gulf Policy was obtained by fraud and thus void, and that Travelers therefore possessed no obligation to indemnify Raydon.

On November 23, 2011, plaintiffs commenced this action, asserting a claim of breach of the insurance contract against Travelers and seeking declaratory relief against ERSIC. The first count alleged that Travelers, having "assumed all insuring commitments" of its predecessor-in-interest Gulf Insurance Company, "wrongfully repudiated and breached its obligation to perform under [the Gulf Policy]" by failing to pay plaintiffs the amounts due as judgment creditors of Raydon.

In the second count, plaintiffs alleged that ERSIC wrongfully refused to compensate plaintiffs for its covered

portion of the Raydon judgment, and therefore sought a declaration that ERSIC is obligated to pay that portion pursuant to the Excess Policy.

On February 10, 2012, defendants separately moved to dismiss the complaint in lieu of answering, asserting forum non conveniens and plaintiffs' lack of standing. In essence, defendants argued that the suit should be dismissed not only because New Jersey was an inappropriate forum considering the ongoing litigation in Bermuda, but also for failure to state a cause of action since plaintiffs were not in privity with Travelers as parties to the Gulf Policy and thus lacked standing.

On July 12, 2012, the motion judge heard oral argument on the motions,[5] after which the judge requested supplemental briefing on a specific portion of the insurance policy. On February 21, 2013, the court rendered a decision via telephonic conference granting defendants' motion and dismissing the complaint with prejudice.

The court did not address forum non conveniens, acknowledging at the outset before rendering its decision that

[5] Between the filing of defendants' motion to dismiss and oral argument, the parties made several applications to the court regarding purported discovery violations. In the order now under appeal, the judge resolved those motions as mooted by the dismissal of the complaint.

its decision was based solely on the standing issue. Addressing first whether plaintiffs had standing to bring suit as third-party beneficiaries of the Gulf Policy, the court concluded that the "no-action clause"[6] in the policy contract was sufficient evidence that the original contracting parties did not intend "to assume a direct obligation to Clarendon." Accordingly, the court determined that plaintiffs did not have standing under that theory.[7]

With respect to the other asserted ground, the court likewise ruled that plaintiffs failed to demonstrate standing as

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[6] Under a clause entitled "Action Against Insurer," the Gulf Policy provided in pertinent part:

> No action shall lie against the Insurer unless, as a condition precedent thereto, there shall have been full compliance by the Insureds with all of the terms of this Policy; nor shall any such action lie until the amount of the Insured's obligation to pay shall have been finally determined either by judgment against an insured after actual trial or by written agreement of the Insured, the claimant and the Insurer. No person or organization shall have any right under this Policy to join the Insurer as a party to any action against the Insureds to determine the Insurer's liability, nor shall the Insurer be impleaded by the Insureds or their legal representatives.

[7] We have briefly summarized the court's analysis on this issue because, as explained below, we are reversing the decision and order on a separate ground. Therefore, we need not address plaintiffs' challenge to this aspect of the Law Division's decision.

judgment creditors of Raydon. The court summarized the case law raised by both sides in support of their contentions, and ultimately accepted defendants' argument that plaintiffs were not permitted to directly sue the insurers because no statutory or contractual basis existed:

> The cases relied upon by the plaintiffs I find are limited to the direct action statute. And I also note [that in Merchants Mutual Insurance Co. v. Monmouth Truck Equipment, Inc., No. 06-CV-05395 (D.N.J. Jan. 4, 2008)(slip op.), the district court] summarized that as a general rule the common law prohibits actions by a third party against an insurer absent some statutory or contractual provision permitting direct action.
>
> The New Jersey direct action statute requires a potential claimant to first obtain a judgment against the insured and receive it back unsatisfied before a direct action can be commenced against the potentially responsible party's insurer[.]
>
> So, I find that because the plaintiffs cannot demonstrate any New Jersey case law indicating a right of judgment creditors in the case of an errors and omissions policy, not a tort action, to bring suit directly against the insured, that the plaintiffs do not have standing . . . as judgment creditors to bring this cause of action.

Having thus determined that plaintiffs failed to demonstrate standing as either third-party beneficiaries or judgment creditors, the court granted defendants' motions and dismissed the complaint. A written order memorializing that

decision was entered on the same date, which indicated that the dismissal had been granted with prejudice.

Plaintiffs timely filed a notice of appeal from that decision and order. On appeal, plaintiffs contend that the Law Division erred in concluding that plaintiffs lacked standing to bring suit against defendants either as judgment creditors or third-party beneficiaries. Plaintiffs also challenge the dismissal of their complaint with prejudice.

II.

We review the grant of a motion to dismiss a complaint for failure to state a cause of action de novo, applying the same standard under Rule 4:6-2(e) that governed the motion court.[8] See Frederick v. Smith, 416 N.J. Super. 594, 597 (App. Div. 2010), certif. denied, 205 N.J. 317 (2011). A trial court should grant the dismissal "in only the rarest of instances." Printing Mart-Morristown v. Sharp Elecs. Corp., 116 N.J. 739, 772 (1989). Such review "is limited to examining the legal sufficiency of the facts alleged on the face of the complaint," and, in determining whether dismissal under Rule 4:6-2(e) is

[8] While the parties couched the issues in terms of "standing," we believe the more accurate formulation would have been whether New Jersey law recognizes a valid cause of action by plaintiffs, the assignees of Clarendon and judgment creditors of Raydon, against defendant-insurers Travelers and ERSIC to collect an unsatisfied judgment against the insured Raydon under the Gulf and Excess policies.

warranted, the court should not concern itself with the plaintiffs' ability to prove its allegations. Id. at 746. If "the fundament of a cause of action may be gleaned even from an obscure statement of claim," then the complaint should survive this preliminary stage. Craig v. Suburban Cablevision, Inc., 140 N.J. 623, 626 (1995)(citation omitted).

As a general rule, an injured third party may not maintain a "direct action" against the tortfeasor's insurer until damages have first been fixed by a final judgment or settlement. See Cruz-Mendez v. Isu/Insurance Servs., 156 N.J. 556, 566-67 (1999)(citing Tuckey v. Harleysville Ins. Co., 235 N.J. Super. 221, 226 (App. Div. 1989)); cf. 15 Holmes' Appleman On Insurance § 112.10, at 338 (2d ed. 2000)("The modern rule is 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."). Many insurance policies backstop that general rule by including "no action" clauses, which prohibit joinder of the insurer "in an underlying lawsuit in which a third party seeks damages from an insured." Kenny & Lattal, N.J. Insurance Law § 2-25:2, at 66 (2d ed. 2000); see also Condenser Serv. & Eng'g Co. v. Am. Mut. Liab. Ins. Co., 45 N.J. Super. 31, 41 (App. Div.), certif. denied, 24 N.J. 547

(1957); Bacon v. Am. Ins. Co., 131 N.J. Super. 450, 458-59 (Law Div. 1974), aff'd, 138 N.J. Super. 550 (App. Div. 1976).

It appears well settled in New Jersey, however, that an injured plaintiff, having obtained a judgment against an insured tortfeasor which remains unsatisfied due to insolvency, "stands in the shoes" of the insured with respect to the insurance policy and thus acquires standing to pursue an action against the insurer. Dransfield v. Citizens Cas. Co., 5 N.J. 190, 194 (1950)(a judgment creditor holds rights "purely derivative" from the insured, "which ripens into a right of action when he recovers a judgment against the [insured] whose insolvency is proved by the return of an execution unsatisfied"); see also In re Gardinier, 40 N.J. 261, 265 (1963); Manukas v. Am. Ins. Co., 98 N.J. Super. 522, 524 (App. Div. 1968)("Ordinarily, an injured person possesses no direct cause of action against the insurer of the tortfeasor prior to recovery of judgment against the latter."); Hanover Ins. Co. v. McKenney, 245 N.J. Super. 282, 287 (Law Div. 1990); Rapp v. Awany, 205 F. Supp. 2d 279, 284 (D.N.J. 2002).

In determining that plaintiffs lacked standing to pursue this lawsuit against defendant-insurers for the amount of the unsatisfied Bermuda judgment, the motion judge relied upon New

Jersey's so-called direct action statute,[9] N.J.S.A. 17:28-2.

That statute provides in pertinent part:

> No policy of insurance against loss or damage resulting from accident to or injury suffered by an employee or other person and for which the person insured is liable, or against loss or damage to property caused by animals or by any vehicle drawn, propelled or operated by any motive power, and for which loss or damage the person insured is liable, shall be issued or delivered in this state by any insurer authorized to do business in this state, unless there is contained within the policy a provision that the insolvency or bankruptcy of the person insured shall not release the insurance carrier from the payment of damages for injury sustained or loss occasioned during the life of the policy, and stating that in case execution against the insured is returned unsatisfied in an action brought by the injured person . . . because of the insolvency or bankruptcy, then an action may be maintained by the injured person . . . against the corporation under the terms of the policy for the amount of the judgment in the action not exceeding the amount of the policy.
>
> [Ibid.]

Defendants contend, as they did before the Law Division, that plaintiffs' "direct suit" here is barred by N.J.S.A. 17:28-

[9] Referring to N.J.S.A. 17:28-2 as a "direct action statute" is a misnomer because, unlike statutory enactments in other states, see, e.g., 15 Holmes' Appleman On Insurance, supra, § 112.10, at 338-57, it does not actually "authorize" direct actions. Rather, it prohibits insurers from contractually disclaiming, in the specifically enumerated policy types, an injured party's right to sue the insurer for an unsatisfied judgment.

2 because the statute only authorizes such a direct action for particular personal injury and property damage lawsuits.[10] We disagree.

In essence, N.J.S.A. 17:28-2 requires that any New Jersey insurer who deals in certain kinds of liability policies — namely, personal injury and property damage caused by vehicles — must include certain provisions "within the policy." Cf. Dransfield, supra, 5 N.J. at 192 (noting that the post-judgment action by plaintiff against insurer had been "instituted pursuant to a condition of the policy" mandated by N.J.S.A. 17:28-2's identical predecessor statute, and not under the statute itself). Chief among them for our purposes is the requirement that if execution of a damages judgment against the insured party "is returned unsatisfied in an action" by the judgment creditor due to the former's "insolvency or

[10] The term "direct action" has sometimes been utilized to describe two situations that are analytically distinct. The first is where a third party either skips an action against the insured outright and sues the insurer alone, or seeks to join the insurer in an action against the insured. See, e.g., Cruz-Mendez, supra, 156 N.J. at 566-67; Tuckey, supra, 236 N.J. Super. at 226. The other scenario is, as here, the case where the third party has sued and obtained judgment against the insured, and thereafter initiates a second lawsuit to collect an unpaid judgment against the insurer. See, e.g., Rapp, supra, 205 F. Supp. 2d at 281-85. We think the latter could more appropriately be labeled a "post-judgment action" or "derivative action." Cf. Dransfield, supra, 5 N.J. at 194 (noting that a judgment creditor under such circumstances holds rights that are "purely derivative" from the insured party).

bankruptcy," then a suit may be maintained against the insurer "under the terms of the policy for the amount of the judgment in the action not exceeding the amount of the policy." Ibid. Stated differently, N.J.S.A. 17:28-2 declares that when the enumerated policy types are implicated, the insurer is not free to contractually preclude a lawsuit by an injured third party for an unsatisfied damages judgment.

The statute "does not apply to all policies or cover all types of losses." Flexi-Van Leasing, Inc. v. Through Transp. Mut. Ins. Ass'n Ltd., 108 Fed. App'x 35, 39 (3d Cir. 2004). The language of N.J.S.A. 17:28-2 restricts its scope to a

> policy of insurance against loss or damage resulting from accident to or injury suffered by an employee or other person and for which the person insured is liable, or against loss or damage to property caused by animals or by any vehicle drawn, propelled or operated by any motive power, and for which loss or damage the person insured is liable.

We do not agree the statute conveys what defendants assert it does: that the Legislature, by enacting N.J.S.A. 17:28-2, meant to preclude all suits against insurers for unsatisfied judgments resulting from the insured's insolvency or bankruptcy except those involving personal-injury or vehicle-induced property-damage policies. Simply because the statute mandates that those specifically identified types of policies contain a

contractual provision establishing the right to a post-judgment action, it does not follow that no such right therefore exists in other, non-listed insurance policies.

The effect of the statute is that a post-judgment action against an insurer will be available to certain plaintiffs under the enumerated policies, assuming of course that all other conditions are satisfied (for example, the injury was covered under the applicable policy, the lawsuit is timely, etc.) because the policy is statutorily required to contain a clause so providing. Had the Legislature intended that derivative or post-judgment actions be available under only certain types of policies, it could have enacted such a law.

Here, the allegations in plaintiffs' complaint, accepted as true and given all favorable inferences, demonstrate that: (1) as the successor in interest to Clarendon, plaintiffs obtained a judgment against the insured-tortfeasor Raydon and were awarded $92.137 million following a damage-proofs hearing; (2) despite making "reasonable efforts" to collect, the judgment remains unsatisfied due to Raydon's insolvency; (3) plaintiffs' injury was the result of tortious acts by Raydon covered under the policy, which was in full force and effect at all applicable times; (4) the judgment was duly recorded in New Jersey under the Uniform Foreign Country Money-Judgments Recognition Act,

N.J.S.A. 2A:49A-16 to -24, and is therefore enforceable in this state; and (5) plaintiffs have a direct and enforceable right under the Gulf Policy to collect the policy proceeds from Travelers, as well as the follow form Excess Policy from ERSIC.

Thus, plaintiffs have alleged sufficient facts establishing a cognizable cause of action against Travelers and ERSIC to pursue proceeds from the relevant insurance policies, as third-party judgment creditors of Raydon. See Gardinier, supra, 40 N.J. at 265; Manukas, supra, 98 N.J. Super. at 524; see also Rapp, supra, 205 F. Supp. 2d at 285 (noting the "long line of cases that recognize the right of an injured third party [,having obtained judgment against the insured,] to sue the insurer").

Because we have determined that plaintiffs have alleged a valid cause of action to recover damages from defendants under the applicable insurance policies as judgment creditors of Raydon and that N.J.S.A. 17:28-2 does not act as a bar to plaintiffs' lawsuit, we need not examine whether the Law Division correctly decided that plaintiffs lacked standing as third-party beneficiaries to the policies at issue.

In conclusion, we reverse the order of the Law Division and remand the matter to the Law Division for further proceedings consistent with this opinion, including entry of an order

denying, in part, defendants' motions to dismiss. On remand, the Law Division must first address that aspect of defendants' motions to dismiss based on forum non conveniens, and, depending on that ruling, thereafter take up the parties' various discovery applications which were determined to be moot. We do not retain jurisdiction.