Carye v. Granite State Ins. Co., No. 281-5-08 Wncv (Toor, J., Oct. 7, 2008)

STATE OF VERMONT
WASHINGTON COUNTY

RAYMOND CARYE and BARBARA CARYE, Plaintiffs v. GRANITE STATE INSURANCE CO., and AMERICAN INTERNATIONAL GROUP, INC., Defendants	SUPERIOR COURT Docket No. 281-5-08 Wncv

RULING ON GRANITE'S MOTION TO DISMISS

Plaintiffs Raymond Carye and Barbara Carye are owners of the Monument Plaza Shopping Center in Bennington. They initiated this case to establish their defense and indemnity rights under a commercial general liability (CGL) policy issued by Defendant Granite State Insurance Co. (Granite) to the Caryes' lessee, Monument Launderette, Inc.("Launderette"), a self-service laundry facility. In a separate case, the Caryes are facing liability for environmental contamination caused, according to the Vermont Agency of Natural Resources and the Environmental Protection Agency, at least in part by the laundry.

The complaint in this case also includes claims for breach of contract, breach of the covenant of good faith and fair dealing, and violation of the Consumer Fraud Act, all essentially based on Granite's pre-litigation resistance to the Caryes' coverage claim. Granite has filed a Rule 12(b)(6) motion to dismiss, arguing that the policy does not insure the Caryes and thus

there can be no coverage. Granite also argues that because the other claims are based on the availability of coverage, or the existence of a contract between the parties, they also necessarily fail.[1]

I. The "Incidental Contract" Claim

The only parties to the lease of shopping center space to Launderette are Plaintiffs, as lessors, and Launderette itself, as lessee. In the lease, Launderette agreed to indemnify and defend Plaintiffs against, among other things, all claims for damage to property claimed to have been caused by Launderette. Lease, ¶ 16.[2] Launderette also agreed to name Plaintiffs as insureds on a liability policy covering, among other things, relevant property damage claims. Lease, ¶ 17. Launderette took out a liability policy with Granite, but Plaintiffs were not listed as named or additional insureds.[3] Plaintiffs nevertheless claim that the policy extends coverage to so-called incidental contracts, that the lease is an incidental contract, and that Plaintiffs are thus entitled to claim rights of defense and indemnity directly against Granite.

The policy extends coverage as follows:

> The company will pay on behalf of the **insured** all sums which the **insured** shall become legally obligated to pay as damages because of
>
> A. **bodily injury** or
>
> B. **property damage**
>
> to which this insurance applies, caused by an **occurrence**, and the company shall have the right and duty to defend any suit against the **insured** seeking damages on account of such **bodily injury** or **property damage** . . . .

Policy at 37. The policy effectively defines "insured," under the general liability part, as it relates to this case, as Monument Launderette, Inc., and its officers, directors, and stockholders;

[1] Granite also suggests that AIG, which has not yet answered or appeared in this case, should be dismissed. The court does not address this issue as it has not been raised by AIG itself.

[2] The lease is in the record as an attachment to the complaint.

[3] The policy is in the record as an attachment to the complaint.

indemnitees are not included. *See* Policy § II(c) at 38 (describing persons insured); *see also* Policy at 32 (defining "insured" as persons described in relevant "Persons Insured" provision); Policy at 42 (additional persons insured).

Contractually assumed liabilities of the insured are expressly excluded from coverage. *See* Policy § I(a) at 37. "Incidental contracts" are excepted from this exclusion, however. *See* id. That is, coverage may extend to a liability assumed by the insured in an incidental contract. An "incidental contract" includes, among other things, a lease of the premises of the named insured. Policy at 31, 40 (defining "incidental contract").

Assuming that Plaintiffs' liability for environmental contamination is subject to the indemnification provision of the lease, that Launderette's indemnification liability would be covered under the incidental contract provision, and that no other exclusions would preclude coverage, the paramount question is whether the policy permits Plaintiffs to proceed directly against Granite, prior to establishing Launderette's liability.

The plain language of the policy reveals no direct action provision; nor does the incidental contract provision appear to contemplate a direct action by an indemnitee. Whether coverage extends to contractually assumed liabilities or not, the policy nevertheless only requires the insurer to pay sums that the insured becomes obligated to pay. Policy at 37. Nowhere does the policy obligate the insurer to pay a sum that an indemnitee of the insured becomes obligated to pay. Similarly, the policy limits the duty of defense to suits against the insured. Nowhere does the policy obligate the insurer to defend an indemnitee of the insured. Nothing textual in the incidental contract provision or definitions implies a direct action, or would explain why a third party claimant in this context would have a direct action while a third party claimant in relation to any other sort of covered liability would not. The policy is not ambiguous in this

regard.

Generally, liability policies are construed against the existence of a right of direct action that does not clearly appear.

> Although a direct action provision is construed liberally in favor of the claimant, in determining whether a contract contains a direct action provision, the contract is construed strictly against the existence of such a provision. Thus absent a statute to the contrary, a liability insurance policy should not be construed as being for the benefit of a third person and intended to accord him or her a right of action against the insurer, unless it clearly appears that this was what the parties intended. The intent that the policy benefits the third party must clearly appear, with any doubt construed against such intent.

7A Couch on Ins. 3d § 104:20; accord Korda v. Chicago Ins. Co., 2006 VT 81, ¶ 25, 180 Vt. 173 ("In general, direct actions against the insurer by persons other than the insured are prohibited because of the absence of privity of contract.").

Among the very few reported cases in which courts have considered whether an incidental contracts provision (also referred to in the case law as an "insured contracts" provision) itself *implies* a right to a direct action by an indemnitee of the insured are two, relied upon by Plaintiffs, in which the right was found.[4] Marlin v. Wetzel County Bd. of Educ., 569 S.E.2d 462 (W.Va. 2002); Krieger v. Wilson Corp., 131 P.3d 661, 674 (N.M. Ct. App. 2005). Krieger is not helpful here because the court in that case merely adopted the conclusion of Marlin without meaningful analysis. Krieger, 131 P.3d at 674.

Marlin also is not helpful. The Marlin court relied on an earlier West Virginia case for the proposition that a third party indemnified in an insured contract by an insured under a CGL policy "stands in the same shoes as the insured for coverage purposes." Marlin, 569 S.E.2d at 468 (quoting Syllabus Point 7, rather than the text of the opinion itself, of Consolidation Coal Co. v. Boston Old Colony Ins. Co., 508 S.E.2d 102 (W.Va. 1998)). With that proposition in

[4] The court found no significant cases on point other than the few cited by the parties.

hand, the court turned its attention to whether the contract at issue was an "insured contract," evidently assuming that if it was, then a right of direct action necessarily followed. See Marlin, 569 S.E.2d at 468 ("The question we must resolve, therefore, is whether the construction contract between Bill Rich Construction and the Board is an 'insured contract' under the Commercial Union general liability policy."). Because the court determined that there was an insured contract, it also concluded, ipso facto, that the right of direct action existed. Id. at 469.[5]

The weakness in the Marlin court's analysis is that the Consolidation Coal court never addressed the direct-action question at all. In Consolidation Coal, the third party indemnitee filed claims against the indemnitor-insureds and their insurer. Consolidation Coal, 508 S.E.2d at 104–05. The West Virginia Supreme Court's description of the trial court proceedings discloses no issue raised or decided with regard to whether the direct action against the insurer should have been permitted. Id. Nothing in the text of the Supreme Court decision indicates that the issue was raised or decided on appeal either. The standing-in-the-shoes proposition for which Marlin cited Consolidation Coal arose in the latter's analysis of the coverage amount that could be applied to insured contract liability, not whether there could be a direct action. Consolidation Coal, 508 S.E.2d at 109–10.

It may be that the insurer in Consolidation Coal simply failed to raise the direct-action issue in that case. It could as easily be that the policy at issue in that case expressly permitted the direct action. In either event, the direct-action issue was not decided in Consolidation Coal, which thus provides faint support for Marlin on this point. Krieger and Marlin are not persuasive on the point for which Plaintiffs have cited them.

In stark contrast to that of Krieger and Marlin, the reasoning in cases in which courts

[5] Moreover, in Marlin, the insurance company's agent, without authorization from the insurer, had issued a certificate of insurance listing the indemnitee as an additional insured. Id. Thus, the insurer was estopped from denying coverage. Id. at 472–73.

have concluded that there is no right of direct action in similar circumstances is well developed and compelling. *See, e.g.*, Alex Robertson Company v. Imperial Casualty & Indemnity Co., 10 Cal.Rptr.2d 165 (Cal. Dist. Ct. App. 1992). The insight of Alex Robertson arises directly out of the language of the insurance contract itself: "A contractual liability coverage endorsement does not make the person an insured whose liability is assumed by the party insured under the policy. Rather, as the endorsement clearly states, it extends the insurance afforded under the policy to include coverage for liability assumed by contract by the person insured." Id. at 168 (relying heavily on Jefferson v. Sinclair Refining Co., 179 N.E.2d 706 (N.Y. 1961)). As the Alex Robertson court concluded, Plaintiffs essentially have sued the wrong party; their indemnity agreement is with Launderette, not Granite. *See* Alex Robertson, 10 Cal.Rptr.2d at 170–71 ("Under the policy, [Insurer] agreed to pay 'on behalf of [Insured] all sums which [Insured] shall become legally obligated to pay . . . by reason of liability arising out of any negligent act [by Insured]' . . . . [Insured] has not yet become legally obligated to pay anything. Until such event, any claim by [third-party Indemnitee] against [Insurer] under the policy is premature.").

Granite is entitled to dismissal of Plaintiffs' claim for coverage based on the "incidental contracts" language of the policy.

II. The Third-Party Beneficiary Claim

The allegations of the complaint asserting the basis for the third-party beneficiary claim are as follows: "Under the lease, the Launderette was required to obtain liability insurance naming the Plaintiffs as additional insureds. Thus, the clear intent of the lease was to make the Plaintiffs the third-party beneficiaries of the AIG insurance policy issued to Launderette." Complaint ¶¶ 7–8. "[Granite] knew that the Launderette leased certain premises at the Plaza to

operate its business. [Granite] and the Launderette contemplated and intended that the insurance contract would confer a direct benefit to the Plaintiffs as owners of the Plaza." Id. ¶ 8.

The first allegation is insufficient. The parties to the lease cannot bind the insurer. "In order to be a third-party beneficiary entitled to recover on an insurance contract, it is not enough that it be intended by one of the parties to the [insurance] contract and the third person that the latter should be a beneficiary." Stainless, Inc. v. Employers Fire Ins. Co., 418 N.Y.S. 2d 76, 80 (N.Y. App. Div. 1979) (quoting 18 Couch on Ins. 2d § 74:330), *aff'd* 49 N.Y.2d 924 (N.Y. 1980).

The second allegation—that Granite and Launderette both intended Plaintiffs to be third-party beneficiaries—is a harder question. There is authority for the proposition that not only must both parties to the insurance policy so intend, but they "must indicate that intention in the contract." Id. *See also* 17 Couch on Ins. 3d § 241:25 ("In order for a third party to maintain an action against an insurer, an intent to make the obligation inure to the benefit of such person must clearly apply in the contract of insurance, and, if any doubt exists, the contract should be construed against such intent."); Counihan v. Allstate Insurance Co., 142 F.R.D. 387, 388 (E.D.N.Y. 1992) ("movant must show from within the four corners of the insurance contract, that both parties intended that she receive the benefits"). Because the policy here is not ambiguous, there is arguably no need to go beyond its terms. Schafer Oil Co. v. Universal Underwriters Ins. Co., 820 F. Supp. 321, 323–24 (E.D. Mich. 1993) ("It is well settled that an objective standard is to be used which discerns the parties' intentions from the contract itself . . . . When the language of an agreement is unambiguous, the meaning of the language is a question of law and the intent of the parties must be discerned from the words used in the instrument"). There is nothing in the policy supporting a claim that Granite intended Plaintiffs to be third-party beneficiaries of the

policy. The mere fact that there is reference to "incidental contracts" does not create a direct cause of action. *See, e.g.*, Kassis v. Ohio Casualty Ins. Co., 856 N.Y.S.2d 797, 799 (N.Y.App. Div. 2008).

However, under Vermont law, the "circumstances surrounding the making of the agreement" can demonstrate ambiguity in an otherwise clear contract. Kipp v. Chips Estate, 169 Vt. 102, 107 (1999) ("We allow limited extrinsic evidence of 'circumstances surrounding the making of the agreement' in determining whether the writing is ambiguous."); Isbrandtsen v. North Branch Corp., 150 Vt. 575, 579 (1988) ("Ambiguity will be found where a writing in and of itself supports a different interpretation from that which appears when it is read in light of the surrounding circumstances, and both interpretations are reasonable."). Plaintiffs here do not allege in the complaint or argue in their papers that there is any specific extrinsic evidence—such as promises made by Granite or other expressions of intent by the insurer—that makes the policy here ambiguous.[6] They do, however, allege that Granite and the Launderette "contemplated and intended that the insurance contract would confer a direct benefit to the Plaintiffs[.]" Complaint, ¶ 8. Even Granite acknowledges that "if they could show that Granite State had so intended," Plaintiffs could establish third-party beneficiary status. Motion to Dismiss at 8.

Because Plaintiffs so allege, and because this is a motion to dismiss rather than a motion for summary judgment, the court must take the Plaintiffs' allegations as true. Colby v. Umbrella, Inc., 2008 VT 20, ¶ 13, __ Vt. __; Wentworth v. Crawford & Co., 174 Vt. 118, 121 (2002). Under this standard, their pleading on this issue withstands dismissal.

[6] Instead, they suggest that Granite has the burden of proof on this, a proposition with which the court disagrees. Plaintiffs' Opposition at 19 ("By asserting that the insurer did not intend to make Plaintiffs third-party beneficiaries, the Defendant has raised a factual defense not present in any of the allegations of the Complaint."). In fact, Plaintiffs raised the issue in the complaint themselves, as noted above. The burden of proving the issue is on Plaintiffs. McMurphy v. State, 171 Vt. 9, 16 (2000) ("In order to sue on the contract between [two other parties], *plaintiffs must establish* that their daughter was a third-party beneficiary to the contract rather than an incidental beneficiary") (emphasis added).

III. The Claims for Bad Faith and Consumer Fraud

The bad faith claim turns on whether there was any contractual duty owed by Granite to Plaintiffs. This issue depends upon the ultimate resolution of the third-party beneficiary claim, and thus must wait.

The Consumer Fraud claim, however, can be disposed of now. Even assuming that a third-party beneficiary could meet the definition of a "consumer" under 9 V.S.A. § 2451a, the only claim asserted is that Granite denied coverage. As our Supreme Court has said, "[u]nder that logic, any denial of coverage becomes consumer fraud. . . . [A] mere breach of contract cannot be sufficient to show consumer fraud." Greene v. Stevens Gas Service, 2004 VT 67, ¶15, 177 Vt. 90. The Consumer Fraud claim is therefore dismissed.

Order

Granite's motion to dismiss is granted in part and denied in part. Any claims for coverage based upon the "insured contracts" terms of the policy are dismissed.[7] The Consumer Fraud claim (Count IV) is also dismissed. However, the claims for declaratory relief, breach of contract, and breach of the covenant of good faith may proceed at this time based upon the allegation that Plaintiffs were third-party beneficiaries.

Dated at Montpelier, Vermont this 6th day of October 2008.

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Helen M. Toor
Superior Court Judge

[7] As the complaint does not separately set forth a cause of action on this theory, the court cannot dismiss a discrete count. In essence, the court is dismissing the portion of Counts I, II, and III that rely upon this theory.