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**DISCRETIONARY REVIEW GRANTED BY SUPREME COURT:
SEPTEMBER 10, 2008
(FILE NO. 2008-SC-000037-D & 2008-SC-000044-D)**

Commonwealth of Kentucky

Court of Appeals

NO. 2006-CA-001737-MR

DANIEL GARCIA, M.D.; RITA GARCIA — APPELLANTS

v.

APPEAL FROM JEFFERSON CIRCUIT COURT
HONORABLE GEOFFREY P. MORRIS, JUDGE
ACTION NO. 02-CI-009027

ASSOCIATED INSURANCE SERVICE, INC.;
AON RISK SERVICES INC. OF OHIO — APPELLEES

OPINION
REVERSING AND REMANDING

** ** ** ** **

BEFORE: ACREE, THOMPSON AND WINE, JUDGES.

WINE, JUDGE: On April 18, 1998, Rita Garcia and her husband, Daniel Garcia, M.D., suffered substantial injuries in a mishap aboard the Star of Louisville, a pleasure craft then operating on the Ohio River by the City of Louisville. On April 14, 1999, the Garcias brought a personal injury action against the Star's owner, the Star of Louisville,

Inc. (the Star). The Star was defended by its liability carrier, HIH Casualty and General Insurance, Ltd. (HIH). In April 2001, while the litigation was pending, HIH declared bankruptcy, thereupon withdrawing its defense of the Star and, in effect, repudiating coverage. Suddenly faced with the prospect of a large, uninsured liability, the Star negotiated a settlement with the Garcias in exchange for the Garcias' promise to "forbear" seeking enforcement against the Star.

Pursuant to the settlement agreement, the Star conceded liability for the 1998 accident, agreed to arbitrate the amount of the Garcias' damages, and further agreed to assign to the Garcias any and all claims the Star might have against its insurance agent and broker for insuring the Star with an unreliable carrier. In June 2002, an arbitration order, incorporating the parties' agreement and independently fixing the Garcias' combined damages at $742,193.10, concluded the litigation against the Star.

In November 2002, pursuant to the assignment of the Star's claims, the Garcias brought the present action against the Star's insurance agent, Associated Insurance Service, Inc. (Associated), an insurance agency operating in Louisville. Associated then filed a third-party complaint against AON Risk Services Inc. of Ohio (AON), an insurance brokerage service with offices in Cleveland, Ohio. In December 2003, the Garcias amended their complaint to include claims against AON. The Garcias allege that Associated and AON breached insurance procurement contracts with the Star by negligently placing its coverage with HIH, and that this breach damaged the Star by exposing it to, and rendering it incapable of satisfying, the Garcias' claims for damages.

In a June 21, 2006, summary judgment, the Jefferson Circuit Court dismissed the Garcias' claims against Associated and AON on the ground that those

claims sound in tort rather than contract and thus were not assignable. Agreeing with the Garcias that the trial court misconstrued Kentucky law and that the Star's assignment of its claims against Associated and AON was valid, we must reverse and remand for additional proceedings.

As the parties correctly note, under CR 56.03 summary judgment is appropriate only if "there is no genuine issue as to any material fact and . . . the moving party is entitled to a judgment as a matter of law." This Court reviews *de novo* the trial court's application of this rule. *Steelvest, Inc. v. Scansteel Service Center, Inc.,* 807 S.W.2d 476 (Ky. 1991). In this case, although there is no dispute with regard to the pertinent facts, we are convinced that the trial court erred by disallowing as a matter of law the assignment of the Star's claims against its insurance agent and broker. Although the trial court's ruling focused on the assignment of the Star's claims, Associated and AON attack other aspects of the Garcias' settlement with the Star as well. In light of these additional contentions, it is useful to begin by noting that the type of settlement at issue here, in a closely related context, has already received widespread judicial approval.

Where an insurer denies coverage of a claim against its insured, refuses to defend, or unreasonably refuses to settle, the insured, to protect itself against the threatened out-of-pocket loss, will frequently have a strong incentive to settle with the plaintiff. Such settlements often take the form of a stipulated judgment against the insured, the insured's assignment to the plaintiff of its claims against the insurer, and the plaintiff's agreement not to seek execution of the judgment against the insured. Although each of the elements of these agreements has been challenged, these agreements have been widely upheld. *See* Note, "Judicial Approaches to Stipulated Judgments,

Assignments of Rights, and Covenants not to Execute in Insurance Litigation," 47 Drake L. Rev. 853 (1999). In Kentucky, although the law in this area is sparse, our highest Court has approved an insured's assignment of his claims against his insurer. *Terrell v. The Western Casualty & Surety Company,* 427 S.W.2d 825 (Ky. 1968); *Grundy v. Manchester Insurance & Indemnity Company,* 425 S.W.2d 735 (Ky. 1968).

However, where an insured's exposure is not attributable to the insurer, or where, as in this case, the insurer is insolvent, an obvious variation on the above agreement is for the insured to assign his claims against some other entity, such as an insurance agent allegedly responsible for the failure of coverage. In the context of such settlements, assignments of claims against allegedly negligent insurance agents have also been upheld. *Stateline Steel Erectors, Inc. v. Shields,* 837 A.2d 285, 288 (N.H. 2003).

With this background in mind, we now turn to the Star's settlement with the Garcias. Associated and AON challenge this settlement not only as an invalid assignment, but contend as well that the Garcias' agreement not to execute against the Star undermined the purported assignment. They further contend that the judgment—the arbitrator's ruling against the Star—may not be employed against them as a binding measure of the Star's purported damages. We will address these differences in turn, beginning with the contention that the assignment was invalid.

As the trial court correctly noted, the general rule in Kentucky is that tort claims for personal injuries may not be assigned. *State Farm Mutual Automobile Insurance Company v. Roark,* 517 S.W.2d 737 (Ky. 1974). The trial court believed that this rule extended to all tort-based claims. Further convinced that the Star's malpractice-like claims against its agent and broker sounded in tort, it concluded that those claims

were not assignable. However, in *Grundy v. Manchester Insurance & Indemnity Company, supra,* however, our state's highest Court indicated that tort claims could be assigned "for torts which are founded upon contracts and grow out of the contractual relations between the parties." *Id.* at 736 (citation and internal quotation marks omitted). The Court upheld, therefore, an insured's assignment of his bad-faith-settlement claim against his insurer on the ground that the duty of good faith the insurer allegedly breached arose from the insurance contract. Likewise, the duty of care Associated and AON allegedly breached arose from their contracts with the Star and the alleged breaches gave rise to purely economic injury. Thus, under *Grundy,* the Star's claims are assignable.

The trial court also believed that the assignment of the Star's claims violated public policy. It noted that in *Coffey v. Jefferson County Board of Education,* 756 S.W.2d 155 (Ky.App. 1988), this Court aligned itself with the vast majority of other jurisdictions and invalidated an assignment of a claim for legal malpractice to the adverse party. The *Coffey* Court wrote that

> [the] view that a chose in action for legal malpractice is not assignable is predicated on the uniquely personal nature of legal services and the contract out of which a highly personal and confidential attorney-client relationship arises, and public policy consideration based thereon.

Id. at 157. Relying on *Premium Cigars International, Ltd. v. Farmer-Butler-Leavitt Insurance Agency,* 96 P.3d 555 (Ariz.App. 2004), in which the Arizona Court of Appeals reached the same conclusion, the trial court ruled that an insured's business relationship with his or her insurance agent/broker was sufficiently similar to the relationship between attorney and client to require the same bar against the assignment of insurance agent malpractice claims. However, we are persuaded by the courts reaching the opposite

conclusion that the insured-agent relationship is neither so highly personal nor so fraught with public policy implications as to preclude assignment of the insured's malpractice claims, at least where, as here, the assignment is to the insured's adversary in the underlying litigation. *Forgione v. Dennis Pirtle Agency, Inc.,* 701 So. 2d 557 (Fla. 1997); *Daugherty v. Blaase,* 548 N.E.2d 130 (Ill.App. 1989); *Troost v. Estate of DeBoer,* 202 Cal. Rptr. 47 (Cal. 1984); *Esposito v. CPM Ins. Services, Inc.,* 922 A.2d 343 (Conn. Super. 2006).

As the above courts have noted, the attorney-client relationship is uniquely personal and involves the highest fiduciary duties of confidentiality and loyalty. In contrast, the insured-insurance agent relationship imposes on the agent a duty to use reasonable skill and diligence in obtaining coverage. The relationship does not hinge on privileged communications and does not prevent the agent's substitution by a different agent. Rather, it exists in conjunction with the agent's duty of good faith and perhaps loyalty toward represented insurers. In sum, notwithstanding the fact that the agent is providing a "personal" service, the insured-agent relationship is a simple, commercial transaction not genuinely comparable to the highly personal relationship between attorney and client and therefore not subject to the same bar against the assignment of malpractice claims.

Nor does the assignment of an insured's claims against his insurance agent raise the public policy concerns courts have noted in the attorney-client context. The assignment of a legal malpractice claim to an adversary in the litigation involves the assignee in an unseemly reversal of roles. The assignee, the adversary in the underlying litigation, who argued in that litigation that she was entitled to judgment on the merits,

must switch positions in the assigned case and there argue that she would have lost in the underlying litigation were it not for opposing counsel's negligence. This seeming reversal of roles would be confusing to juries and damaging to the credibility of the legal system. The assignment of an insured's claim against his or her agent/broker, on the other hand, does not require the adversary/assignee to reverse roles or to disavow in any way her former position. In the underlying litigation, the assignee argues that she was entitled to damages from the insured, and in the assigned case she argues, consistently, that she would have collected those damages from the insured, at least to the extent of insurance coverage, were it not for the negligence of the insured's agent. Therefore, public policy is not offended.

Finally, in *Premium Cigars International, Ltd. v. Farmer-Butler-Leavitt Insurance Agency, supra,* the Arizona Court of Appeals expressed concern at the prospect of a market in such claims if it permitted the assignment of an insured's malpractice claim against its insurance agent. Not only is this concern speculative, but it does not support the limited result Associated and AON seek. It may well be that insurance-agent malpractice claims should not be as freely assignable as claims for credit card debt or mortgages, but that does not imply that they should never be assignable. In the context presently before us, where the assignment was executed as a part of a settlement with the insured's adversary in the underlying tort litigation, we agree with the Courts cited above that public policy does not preclude the assignment of an insured's malpractice claim against his or her insurance agent.

Even if the assignment of the Star's claims was valid, Associated and AON contend that we should still affirm the trial court's judgment either because the Garcias'

agreement to forbear from execution against the Star rendered the assignment illusory, or because the arbitration ruling against the Star did not provide the sort of conclusion to the underlying litigation that can in fairness be asserted against them. There is some support for these contentions in the law of other jurisdictions.

In *Oregon Mutual Insurance Company v. Gibson,* 746 P.2d 245 (Or.App. 1987), for example, a case factually similar to this one, the Oregon Court of Appeals affirmed a summary judgment for the insurance agents on the ground that the agreement between the insured tortfeasor and the tort claimant, which insulated the insured from liability, left the insured without a viable claim to assign against its insurance agents. *See also Freeman v. Schmidt Real Estate & Insurance, Inc.,* 755 F.2d 135 (8th Cir. 1985). Again, however, the majority position is otherwise.

Most courts have held that a settlement, where a tort victim agrees not to execute against the insured tortfeasor in exchange for an assignment of the insured's claims against his insurer or insurance agent, is not illusory. *Stateline Steel Erectors, Inc. v. Shields,* 837 A.2d 285 (N.H. 2003); *Campione v. Wilson,* 661 N.E.2d 658 (Mass. 1996); *Gray v. Grain Dealers Mutual Insurance Company,* 871 F.2d 1128 (D.C. Cir. 1989). As the Supreme Court of New Hampshire observed in *Stateline Steel Erectors, Inc. v. Shields,* there is a substantial risk that a negligent agent will escape liability. Although no Kentucky appellate court has addressed this precise issue, our highest Court has upheld the assignment of an insured's claims against his insurer. And in *O'Bannon v. Aetna Casualty & Surety Company,* 678 S.W.2d 390 (Ky. 1984), our Supreme Court refused to invalidate the sort of agreement at issue here, whereby an insured assigned claims against his insurer in exchange for a release from personal liability,

notwithstanding the asserted risk of collusion between the settling parties. Because of our highest Court's repeated validation of an insured's assignment of claims against his insurer, we believe that the majority position upholding assignments of claims against insurers and insurance agents, even when coupled with agreements insulating the assignor from execution, is not only more persuasive but is more consistent with Kentucky law.

Although most courts have thus upheld settlements such as that between the Star and the Garcias to the extent that they provide for the assignment of the insured's claims while insulating the insured from execution, virtually every court addressing the question has recognized that the judgments emerging from these settlements are problematic. *See RLI Insurance Company v. CNA Casualty of California,* 45 Cal. Rptr. 3d 667 (Cal.App. 2006); *Stateline Steel Erectors, Inc. v. Shields, supra; State Farm Fire and Casualty Company v. Gandy,* 925 S.W.2d 696 (Tex. 1996); *Campione v. Wilson, supra.*

The problem is often referred to as a risk of collusion between the settling parties. There was nothing improper in the Star's seeking to protect its suddenly uninsured assets from a potentially ruinous judgment, or in the Garcias seeking to translate their claim against the Star into real rather than nominal but uncollectible relief. The real problem is simply that, by insulating the Star from execution, the settlement left the parties not truly adverse. Strangers to the agreement, therefore, such as Associated and AON, have no assurance that the Garcias' claims, particularly the amounts of their damages, have been scrutinized and tested. With all due respect for the arbitration in this case, an arbitrator's opinion simply cannot substitute for the thorough adversarial vetting upon which our system was founded.

In light of this problem and to reduce the risk of collusive settlements, the Supreme Courts of New Hampshire and Massachusetts have held, with respect to settlements such as the one between the Star and the Garcias, that tort victim-assignees of claims against insurance agents bear the burden of proof on the assigned claims and that the insurance agents, "who were not parties to the settlement agreement, cannot be bound by its terms." *Stateline Steel Erectors, Inc. v. Shields,* 837 A.2d at 289; *Campione v. Wilson, supra.* To recover against the insurance agent/broker, furthermore, the assignee must prove the elements of its assigned malpractice claim, including the fact of the insured-assignor's injury. "[T]he settlement agreement . . . is [not] conclusive on [that] point." *Stateline Steel Erectors, Inc. v. Shields,* 837 A.2d at 289. ("We do not consider the settlement agreement as probative on any of these points, particularly damages.") *Campione v. Wilson,* 661 N.E.2d at 663. We agree with these holdings, and are again convinced that they are consistent with our Supreme Court's observation in *O'Bannon v. Aetna Casualty & Surety Company, supra,* that an insurer subjected to a collusive settlement agreement "would obviously have a remedy against any obligation to pay such a judgment either when sued on its coverage or by collateral attack on the judgment." *Id.* at 393.

In conclusion, the Star's malpractice claims against its insurance agent and insurance broker were assignable to the Garcias notwithstanding the tort-like elements of the claims, the personal-services nature of the Star's relationships with its agent and broker, and the Garcias' agreement not to seek execution against the Star. The trial court erred, therefore, by dismissing the Garcias' assertion of those claims on the ground that they were not assignable. On remand, the Garcias will bear the burden of proving the

damages from the assigned malpractice claims, including the fact that the Star was injured by the alleged malpractice. Neither the Garcias' agreement not to seek execution against the Star nor the arbitrator's ruling against the Star will be probative with respect to that injury. Accordingly, we reverse the June 21, 2006, summary judgment of the Jefferson Circuit Court and remand for reinstatement of the Garcias' amended complaint.

ALL CONCUR.

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