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Third Circuit: Insurers May Have Easier Time Keeping Coverage Litigation In Federal Court

In a recent ruling, the United States Court of Appeals for the Third Circuit may well have made it easier for insurers to litigate coverage in federal court regardless of whether there is an existing underlying proceeding pending in state court.

In *Kelly v. Maxum Specialty Insurance Group*, 2017 U.S. App. LEXIS 15824, the Third Circuit Court of Appeals reversed a ruling by U.S. District Judge Joel Slomsky, who had opted to abstain from exercising jurisdiction over the removal of a declaratory judgment action filed by a dram shop liability personal injury plaintiff against the tavern defendant's insurance agent and the agent's liability insurer. The plaintiff sought a ruling that the insurer, Maxum, had an obligation to defend and indemnify the insurance agent, Carman, in an underlying state suit against Carman relating to the agency's failure to advise the tavern's insurer of notice of the original dram shop suit, which led to a default judgment against the tavern.

Judge Slomsky remanded the insurance coverage suit, filed under the Federal Declaratory Judgment Act, on the grounds that the underlying state proceeding against the insurance agent, Carman, was a prior, parallel proceeding. Judge Slomsky ruled that the insurance coverage issues could be resolved in the state court action filed by the dram shop plaintiff against the agent, Carman, because Maxum could conceivably be added as a party to that suit.

Last week, however, a three-judge panel of the Third Circuit disagreed with Judge Slomsky's reasoning and ruled instead that that a federal action brought under the Declaratory Judgment Act is not parallel to a state case "merely because they have the potential to dispose of the same claims."

Circuit Judge Michael Chagares wrote on behalf of the panel that "[Defining] 'parallel state proceeding' so broadly balloons a court's discretion to decline a [Declaratory Judgment Act] action beyond the measured bounds we set forth in our prior decisions." The appeals panel further ruled that, while the presence of related state court proceedings was a factor to consider, the district judge failed to consider a number of other factors, including Maxum's argument that it was not even a party to the underlying civil errors and omissions case against its insured, Carman.

Judge Chagares wrote:

We hold that the mere potential or possibility that two proceedings will resolve related claims between the same parties is not sufficient to make those proceedings parallel; rather, there must be a substantial similarity in issues and parties between contemporaneously pending proceedings.

Using that standard, the Third Circuit found that the state negligence action against Carman and the federal declaratory judgment suit which included Maxum were clearly not parallel, as they involved different parties and distinct claims.

The Third Circuit remanded the federal declaratory judgment case to Judge Slomsky with the instruction that he proceed to confirm complete diversity of citizenship of the parties to the federal declaratory judgment action.

Editor's Note:

The opinion issued by the Third Circuit in Kelly should be given close attention by insurers wishing to maintain declaratory judgment litigation in generally more favorable federal forums. Those insurers often have to defend their federal coverage suits from remand motions in which state court plaintiffs make enticing arguments to federal trial judges presenting them with an opportunity to clear an active case off of their dockets through exercise of the abstention doctrine. The rule set forth in Kelly may allow insurers to effectively respond to such remand claims, by pointing out to the federal court that an underlying personal injury proceeding which does not involve a defendant's insurer and a federal declaratory judgment suit on coverage which does are hardly "parallel" proceedings.



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