

Insurance Alert: The First Circuit Holds That a Massachusetts Insured May Sue Its Insurer for Bad Faith after Winning a Separate Action for Declaratory Judgment As to Its Rights under an Insurance Policy

12/12/2008

In a significant decision concerning the preclusive effect of a declaratory judgment regarding insurance coverage, the First Circuit Court of Appeals recently found in *Andrew Robinson International, Inc. v. Hartford Fire Insurance Co.* that a final judgment in a declaratory judgment action does not bar a subsequent suit for damages.¹

The plaintiffs in the original action shared an office that was badly damaged when the occupant of a neighboring unit negligently discharged lead-laden dust into the plaintiffs' unit.² The plaintiffs thus filed a first-party claim against its insurer, Hartford Fire Insurance Co.; and, relying on its pollution exclusion, Hartford denied the claim.³ The plaintiffs then filed a complaint for declaratory judgment in the state court seeking a declaration of their rights under the insurance policy.⁴ A Massachusetts Superior Court ruled that the dust discharge did not constitute pollution, and, therefore, did not trigger the policy exclusion.⁵

Eight months later, after Hartford paid their claim, the plaintiffs again sued Hartford in state court, this time alleging that Hartford had violated the Massachusetts unfair and deceptive trade practices act, M.G.L. c. 93A ("Chapter 93A"), by refusing to pay their claim in bad faith, and seeking treble damages and attorneys' fees.⁶ Hartford removed the new case to federal court and moved to dismiss on the ground that the Chapter 93A suit was foreclosed by the preclusive effect of the declaratory judgment action (*i.e.*, *res judicata*).⁷ The U.S. District Court for the District of Massachusetts agreed with Hartford and dismissed the suit; and the plaintiffs appealed to the First Circuit.

Claim preclusion generally applies to bar a subsequent action when there is an identity of parties and causes of action in both actions, and the original action concluded with a final judgment on the merits.⁸ On appeal, the plaintiffs-appellants first contended that their two actions against Hartford did not present the requisite identity of causes of action. The First Circuit disagreed, however, finding that both suits arose from the same underlying transaction.⁹ Nevertheless, the plaintiffs then argued that Section 33 of the Restatement (Second) of Judgments provided a "special rule" which applied to permit a subsequent action for damages when the original action was for declaratory relief.¹⁰

The Restatement (Second) of Judgments § 33 provides that

[a] valid and final judgment in an action brought to declare rights or other legal relations of the parties is conclusive in a subsequent action between them as to the matters declared, and, in accordance with the rules of issue preclusion, as to any issues actually litigated by them and determined in the action.

Under this prescription, however, the Restatement comments explain that "[a] plaintiff who wins a declaratory judgment may go on to seek further relief, even in an action on the same claim which prompted the action for a declaratory judgment."¹¹ "This further relief may include damages which had accrued at the time the declaratory relief was sought; it is irrelevant that the further relief could have been requested initially."¹²

Because claim preclusion is a matter of state law, and the Supreme Judicial Court (SJC)—Massachusetts's highest court—has not spoken on this issue or adopted the special rule set forth in comments, the First Circuit made an "informed prophecy" as to whether the state court would follow it. "To this point," the First Circuit found, "all roads lead to Rome."¹³ Massachusetts courts generally apply claim preclusion in a conventional way, and have cited approvingly to Section 33 of the Second Restatement.¹⁴ The vast majority of states that have addressed this problem "unapologetically apply a special rule of claim preclusion, consistent with that section 33 of the Second Restatement."¹⁵ And the First Circuit's consultation of scholarly literature and weighing of policy rationales provided no reason to hold otherwise.¹⁶ Therefore, the First Circuit found that it could predict with some assurance that the SJC, if faced with the question, would likely follow the rule set out in the Restatement and its comments: a final judgment in an action brought to declare rights does not preclude a subsequent action between the same parties, arising out of the same transaction, and involving issues that could have been brought in the former action.¹⁷

Until and unless the SJC takes up this issue, the law is settled in the First Circuit. Insureds (and other plaintiffs alike) may strategically split claims between a declaratory judgment action and a subsequent action for damages under Chapter 93A.¹⁸ If they do, insurers and other defendants should consider asking the court to refuse to entertain the declaratory judgment action absent joinder of the damages claims.¹⁹ If joined, damages claims can be stayed.²⁰ But, as the First Circuit noted, whether to entertain a declaratory judgment is within the discretion of the trial court.²¹ The insurer should also consider whether it can bring, as a counterclaim, its own declaratory judgment claim seeking a declaration that it did not violate Chapter 93A. Finally, insurers should take the First Circuit's decision into account when considering whether to remove a state action to federal court, and should be sure to address a subsequent suit for damages in connection with the settlement of any declaratory judgment action.

Endnotes

¹ See *Andrew Robinson Int'l, Inc. v. Hartford Fire Ins. Co.*, No. 08-1255 (1st Cir. Nov. 10, 2008) ("*Andrew Robinson*").

² See *id.* at 2.

³ See *id.* at 3.

⁴ See *id.*

⁵ See *id.* (citing *Andrew Robinson Int'l, Inc. v. Hartford Fire Ins. Co.*, No. 03-1353, 2006 WL 1537382, at *13 (Mass. Super. Ct. Feb. 6, 2006)).

⁶ See *Andrew Robinson* at 3-4.

⁷ See *id.* at 4 (citing *Andrew Robinson Int'l Inc. v. Hartford Fire Insurance Co.*, 533 F. Supp. 2d 218, 222 (D. Mass. 2008)).

⁸ See *id.* at 7 (citations omitted).

⁹ See *id.* at 8.

¹⁰ See *id.* at 9 (citing Restatement (Second) of Judgments § 33 cmt. c).

¹¹ Restatement (Second) of Judgments § 33 cmt. c.

¹² *Id.*

¹³ See *Andrew Robinson* at 22.

¹⁴ See *id.* at 12-16.

¹⁵ *Id.* at 16-18 (citations omitted).

¹⁶ See *id.* at 19-21.

¹⁷ See *id.* at 23.

¹⁸ See *id.* at 22.

¹⁹ See *id.* at 22 (citing Restatement (Second) of Judgments § 33 cmt. c.).

²⁰ See *id.*

²¹ See *id.* (citing *El Dia, Inc. v. Hernandez Colon*, 963 F.2d 488, 493 (1st Cir. 1992)).

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