UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

AXA VERSICHERUNG AG, on its own behalf and as successor in interest to ALBINGIA VERISCHERUNGS AG,	05 Civ. 10180 (JSR)
Plaintiff,	MEMORANDUM ORDER
-v-	
NEW HAMPSHIRE INSURANCE COMPANY; AMERICAN HOME ASSURANCE COMPANY and NATIONAL UNION FIRE INSURANCE COMPANY OF PITTSBURGH, PENNSYLVANIA,	
Defendants.	

JED S. RAKOFF, U.S.D.J.

On January 30, 2008, following an eleven-day trial, a jury returned a verdict in this matter finding defendants New Hampshire Insurance Company, American Home Assurance Company, and National Union Fire Insurance Company of Pittsburgh, Pennsylvania (collectively, "AIG") liable to plaintiff AXA Versicherung AG ("AXA"), as the successor-in-interest of Albingia Verischerungs AG, on AXA's claim that AIG fraudulently induced it to enter two reinsurance contracts. The jury also awarded AXA punitive damages in the amount of $5,750,000. On February 6, 2008, the Court entered a final judgment in the case in the total amount of $34,373,170.

AIG has moved for judgment as a matter of law or, in the alternative, for a new trial pursuant to Federal Rule of Civil Procedure 50(b), and to amend the judgment under Rule 59(e), on the grounds that: (1) the Court improperly instructed the jury as to the appropriate standard for imposing punitive damages, and AXA did not offer sufficient proof to meet the correct standard; (2) there was

insufficient evidence to support an award of punitive damages even under the standard stated by the Court; and (3) that the there was no legally sufficient evidentiary basis for the jury's finding that the statute of limitations did not bar AXA's suit.

As to the first point, AIG renews its argument that the Court, in instructing the jury on punitive damages, failed to instruct the jury that it was required to find that AIG's conduct poses "a substantial risk of harm to the general public." Memorandum of Law in Support of Defendants' Motion for Judgment as a Matter of Law or a New Trial, at 1 ("Def. Mem.") (citing AIG's Proposed Jury Instructions). Essentially, AIG argues that AXA's fraud claim "ar[ose] from" a contractual relationship between AXA and AIG and that, consequently, punitive damages are available only when the conditions set forth in Rocanova v. Equitable Life Assur. Soc. of U.S., 83 N.Y.2d 603 (1994), are met. See New York University v. Continental Ins. Co., 87 N.Y.2d 308, 315 (1995) ("NYU") (specifying that under Rocanova, a plaintiff may obtain punitive damages only where defendant's tortious conduct was "directed at the public generally"). The parties are agreed that AXA presented no proof that AIG's fraud was directed at the public generally.

AIG first raised this argument in its motion for summary judgment and preserved (though did not actively argue) it at trial; the Court rejected it at both junctures. In the instant motion, however, AIG seeks to bolster its claim by including additional case citations it had not previously brought to the Court's attention.

These cases, all from lower New York courts, appear to interpret the heightened Rocanova standard to apply, in at least some circumstances, to punitive damages associated with claims for fraudulent inducement. See, e.g., Wright v. Selle,811 N.Y.S.2d 525, 527-28 (4th Dep't 2006); Steinhardt Group Inc. v. Citicorp, 708 N.Y.S.2d 91, 92-93 (1st Dep't 2000); Franco v. English, 620 N.Y.S.2d 156, 158, 161 (3d Dep't 1994). While the cases (which AIG could easily have cited earlier) are not without relevance, the Court remains unpersuaded that the law of New York requires Rocanova's application in the instant case, for several reasons.

First, it is well-established doctrine in New York that fraudulent inducement is an exception to the general rule that "a cause of action seeking damages for fraud cannot be sustained when the only fraud charged relates to a breach of contract, or where the fraud claim is duplicative of, or inextricably related to, a breach of contract claim." 60A N.Y. Jur. 2d Fraud and Deceit § 7 (specifying that ordinarily "a cause of action seeking damages for fraud cannot be sustained when the only fraud charged relates to a breach of contract," but that "a fraud claim may be based on allegations that the defendant fraudulently induced the plaintiff to enter into a contract" so long as the misrepresentations consist of more than "mere promissory statements" about intent to perform under the contract). The rationale for the exception for fraudulent inducement is that the fraud claim is distinct from the contract it precedes; indeed, in many cases if the plaintiff had known the truth,

the plaintiff would never have agreed to the contract at all. While some passing dicta in the NYU case loosely refers to the tort of fraudulent inducement as "aris[ing] from" or "hav[ing] its genesis in" a breach of contract, NYU, 87 N.Y.2d at 316, such language must only refer to the consequences of the fraud, for otherwise it would be inconsistent with the bedrock principles described above, and it cannot be imagined that the Court of Appeals intended by a few snippets of dicta to overrule doctrines otherwise so well established in New York law. The actual holding in NYU was simply that no cause of action for fraudulent inducement had been stated. Id. at 318.

Second, even if the dicta in NYU, and the gloss on that language in subsequent lower court cases, suggest that some fraudulent inducement claims may sound more in contract than in tort or be so intertwined with breach of contract claims that they are impossible to distinguish, this clearly is not such a case. The Second Circuit suggested this distinction in Carvel Corp. v. Noonan, 350 F.3d 6 (2d Cir. 2003), where it stated that "New York courts have applied the 'public harm' standard only to cases in which the defendant's allegedly tortious conduct was directly related to the contract between the plaintiff and defendant," that is, typically, "where the plaintiff claims that the defendant fraudulently misrepresented something about the contract between the two." Id. at 25 (citing NYU and Rocanova as well as New York Appellate Division cases) (emphasis added). Here, AXA alleged no breach of contract

whatsoever.[1] Rather, the evidence AXA adduced at trial pertained to misrepresentations by AIG and its agents that entirely preceded the formation of one or both Primary Facilities. AXA argued, and the jury apparently accepted, that these misrepresentations led AXA to enter contracts into which they otherwise would not have entered at all. As these claims neither arise out of an existing contractual relationship nor recast breach of contract claims, the Rocanova "public harm" requirement does not, in any event, apply to the particular fraud claim in this case. See, e.g,, Topps Co., Inc. v. Cadbury Stani S.A.I.C., 380 F. Supp. 2d 250 (S.D.N.Y. 2005) (holding that "[w]hen all of the essential contours of a claim precede the subsequent contractual relationship, such a claim cannot reasonably be said to arise from that relationship," but finding that in the case before the Court the fraudulent inducement claim arose "from [a] long-standing contractual relationship" and so Rocanova applied).

As to AIG's second point, it is clear that substantial evidence supported the jury's finding, under the appropriate standard, that AIG's conduct was "exceptionally outrageous, criminal-like," and performed "wantonly." Jury Instruction No. 11; Trial Transcript ("Tr.") 2084-85. AXA presented evidence that, among other things: AIG conceived of the Primary Facility as a means of writing unprofitable risks in a soft insurance market, Trial Exhibits ("Exs.") 20, 77, 267; AIG and its agents deliberately misled AXA

[1] Indeed, the very reason that AXA's claim was tried in this Court rather than before an arbitration panel was that it did not involve a breach of contract. See Trial Transcript ("Tr.") at 1472-75.

about the nature of the Facility and secured AXA's participation only because AXA was misled into believing that the Facility was facultative-obligatory, Exs. 8, 12, 15; Tr. 135 (testimony of Thomas Holzapfel); Tr. at 1121-23 (testimony of Scott Darragh); AIG and its agents then contrived to implement the Facility as purely facultative without alerting AXA that it had the right to refuse any risks AIG sought to cede to the Facility, Exs. 80, 81, 93, 96, 101; and AIG and its agents were aware that AXA continued to believe that the Facility was facultative-obligatory and did nothing to disclose the Facility's true nature, Exs. 228, 231, 240. Consequently, the Court, which must consider the evidence in the light most favorable to AXA and give AXA the benefit of all reasonable inferences that the jury might have drawn its favor, cannot conclude that "there is such a complete absence of evidence supporting the [punitive damages award] that the jury's findings could only have been the result of sheer surmise and conjecture." Concerned Area Residents for the Env't v. Southview Farm, 34 F.3d 114, 117 (2d Cir. 1994) (internal quotation marks and alterations omitted). The jury clearly determined that AIG's conduct was "sufficiently willful and egregious to indicate a need for something more than compensatory relief." Whitney v. Citibank, N.A., 782 F.2d 1106, 1118 (2d Cir. 1986).

AIG's final point is to challenge the jury's conclusion that the statute of limitations did not bar AXA's claims. Specifically, the jury was instructed that AXA's claims were barred "unless AXA can show, as to a given Facility, that AXA did not discover until after December 2, 2003 (that is, within two years of when this lawsuit was

commenced), and could not with reasonable diligence have discovered until after December 2, 2003, the facts from which a reasonable reinsurer in AXA's position would have inferred that it was fraudulently induced to enter into that Facility." Juror Instruction No. 9; Tr. 2083.[2] AIG points to three sets of documents that AXA received prior to December 2, 2003, each of which AIG claims a reasonable jury would have had to find triggered a duty of inquiry on AXA's part.

First, it asserts that in 1998, when AXA received and signed the contract wordings containing language indicating that the Facility was purely facultative, AXA possessed sufficient information to trigger a duty to inquire about the discrepancy. The jury, however, heard a variety of evidence about the context in which those wordings were received and signed that reasonably would have led it to conclude that no duty of inquiry was triggered. For example, AXA

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[2] AIG raises a strained challenge to the wording of the charge, which it claims erred in two respects: first, in suggesting that in order for the statute of limitations to run AXA had to be "aware of the specific facts constituting its claim," and second, in suggesting that AXA had to have "enough information to discover all the facts underlying its claim for fraud." Def. Mem. at 27-28. In actuality, the charge contained neither the word "specific" nor the word "all." Rather, the charge suggested – entirely properly - that AXA had either to possess, or to have been able with reasonable diligence to possess, "facts from which a reasonable reinsurer in AXA's position would have inferred that it was fraudulently induced to enter" the Facility in question. See, e.g., Erbe v. Lincoln Rochester Trust Co., 3 N.Y.2d 321, 326 (1957) ("[T]he plaintiffs will be held to have discovered the fraud when it is established that they were possessed of knowledge of facts from which it could be reasonably inferred, that is, inferred from facts which indicate the alleged fraud."). In any event, it is clear from AIG's submissions that the gravamen of their challenge on the statute of limitations issue is evidentiary.

presented evidence that: AIG's brokers placed the Facility as facultative-obligatory, and AIG's agents knew that AXA underwrote only that type of reinsurance, see Exs. 8, 12, 15; see Tr. 92, 135 (Holzapfel); Tr. 543-45 (testimony of Silvia Rauser-Dittman); Tr. at 1121-23 (Darragh); AIG and its brokers, even after the wordings were signed, represented to AXA that the treaty was facultative-obligatory and that the declarations were formalities associated with risks that had already attached, see Tr. 1120-21 (Darragh); Exs. 152, 236, 240; the critical phrase in the 1998 wording appeared in an entirely illogical section, see Tr. 635-38 (Rauser-Dittman); and, unlike every other change - both large and small - to the parties' agreement, this change was not presented to AXA through the established endorsement procedure, see Tr. 633-36 (Rauser-Dittman), Ex. 153, 217. Moreover, the jury also heard evidence about conversations among AIG officials and its brokers from which the jury could have concluded that it was precisely AIG's intent to conceal the true nature of the facility from AXA. See Exs. 21, 67, 101, 199, 210, 211, 258; Tr. 1220-06 (Darragh).

Second, AIG argues that a bordereau AXA received in September 2000, which disclosed thirty-six losses occurring prior to the placement of the 1998 Facility but not previously disclosed, see Ex. GR, should have alerted AXA to AIG's prior concealment of losses, thus triggering a duty of inquiry. As AXA notes, however, that bordereau indicated the date of loss, but not the date that AIG learned of the loss, see Ex. GR at GR-0005; Tr. 867 (testimony of Manja Diver); hence, the jury would reasonably have concluded that

AXA had no way to know of the concealment. AIG argues that the missing information - AIG's knowledge of the loss - goes only to AIG's scienter, and that a mere discrepancy, even without knowledge of intent, triggers a duty to investigate. See Chase Manhattan Bank, N.A. v. T&N PLC, 905 F. Supp. 107, 118 (S.D.N.Y. 1995). This argument is unavailing, however, because on the face of the bordereau there was no discrepancy, as AIG was only required to disclose, in the past, those losses already known to it. It was reasonable for a jury to conclude that AXA, upon receiving the bordereau and understanding insurers' duty to disclose all losses in a timely fashion, would more likely have concluded that the losses only became known to AIG later, rather than concluding that AIG had deliberately concealed them.

Third, AIG points to the 1998 contract wordings and to various declarations sent to AXA that AIG argues put AXA on notice of the alleged "grossing up" of AXA's liability in the Primary Facility. The jury heard evidence, however, that AXA interpreted these documents consistently with its initial expectations about its share of the loss, see Tr. 640-41 (Rauser-Dittman), and the jury was entitled to credit this understanding as reasonable.

In light of the above, the jury had a more than sufficient evidentiary basis upon which to conclude that a "reasonable reinsurer in AXA's position" would not have been put on notice that it had been defrauded until documents in another litigation came to its attention, causing what one witness described as a "thunderbolt."

Tr. at 947 (testimony of Georg Leers); Ex. 292.[3]

In conclusion, the Court is not persuaded to change its earlier ruling on the standard for punitive damages in this case, finds that the jury had a sufficient evidentiary basis on which to award such damages, and finds that the jury had a sufficient evidentiary basis on which to conclude that AXA's claims were not barred by the statute of limitations. Accordingly, AIG's post-trial motion is denied in its entirety.

SO ORDERED.

Dated: New York, NY
April 22, 2008

JED S. RAKOFF, U.S.D.J.

[3] Indeed, the three pieces of evidence the jury requested during deliberations (including the Leers testimony) pertained to the issue of when AXA did or should have discovered the fraud. See Tr. 2092.