UNITED STATES DISTRICT COURT
DISTRICT OF RHODE ISLAND

SEATON INSURANCE COMPANY (f/k/a UNIGARD MUTUAL INSURANCE COMPANY) and STONEWALL INSURANCE COMPANY,	:	CIVIL NO.: 1:09-cv-516S
Plaintiffs,	:	
v.	:	
CLEARWATER INSURANCE COMPANY (f/k/a SKANDIA AMERICA REINSURANCE CORPORATION),	:	
Defendant.	:	FEBRUARY 18, 2010

MEMORANDUM OF LAW IN SUPPORT OF
DEFENDANT'S OBJECTION TO REPORT AND RECOMMENDATION

Pursuant to District of Rhode Island Local Civil Rule 72(d)(2), Defendant Clearwater Insurance Company ("Clearwater") respectfully submits this memorandum of law in support of its objection to the February 4, 2010, Report and Recommendation of Magistrate Judge Almond, recommending that Clearwater's Motion to Dismiss or Stay this proceeding be denied. In recommending that Clearwater's Motion be denied, Magistrate Judge Almond erroneously applied the "stringent" abstention standard of Colorado River Water Conservation Dist. v. United States, 424 U.S. 800 (1976), rather than the "more forgiving, discretionary standard" articulated in Wilton v. Seven Falls Co., 515 U.S. 277 (1995). (R. Doc. 18, at 4.) As a result of his application of an overly burdensome standard, Magistrate Judge Almond incorrectly concluded that Clearwater's showing was not "*sufficiently* compelling" to warrant abstention. (Id. (emphasis added).)

I. FACTUAL BACKGROUND

The Report and Recommendation accurately describes the facts that are material to Clearwater's Motion. The dispute in this case involves two insurers and their reinsurer, and concerns the parties' respective obligations under reinsurance contracts from the 1970s. This dispute is the subject of overlapping lawsuits pending in Connecticut state court and in this Court. In May 2009, Clearwater filed a lawsuit in Connecticut Superior Court seeking a declaratory judgment regarding claims that Plaintiffs Seaton Insurance Company and Stonewall Insurance Company ("Plaintiffs") had submitted for losses paid under liability insurance policies for asbestos-related claims. Five months later – after introducing delay after delay into the Connecticut action – Plaintiffs filed this case seeking both declaratory relief and damages under the very same reinsurance contracts and raising for the first time minor related disputes under additional reinsurance contracts.

On December 14, 2009, Clearwater filed its Motion to Dismiss or Stay this case, demonstrating that this Court should abstain because the parties' coverage dispute was already being litigated in a court of competent jurisdiction in Clearwater's first-filed Connecticut lawsuit. Clearwater demonstrated that Plaintiffs' later-filed complaint in this court was a text-book example of forum shopping. It further showed that Plaintiffs had decided not to remove the Connecticut case to federal court within the time limits prescribed by 28 U.S.C. § 1446 and that Plaintiffs' attempt to obtain a federal forum months later through this lawsuit amounted to an impermissible attempt to make an end-run around the federal removal statute.

Less than a week earlier, Plaintiffs filed a motion to dismiss or stay the Connecticut case due to the pendency of this case. Plaintiffs' Connecticut motion was heard first, and on January 20, 2010, the Connecticut court granted that motion in a one-sentence order. As is its right under

Connecticut law, Clearwater timely moved for articulation of the Connecticut court's rationale for its decision; that motion remains pending.

Meanwhile, Magistrate Judge Almond heard oral argument on Clearwater's Motion to Dismiss or Stay on February 3, 2010. The next day, Magistrate Judge Almond issued his Report and Recommendation, recommending that Clearwater's Motion be denied. (See R. Doc. 18.) Magistrate Judge Almond recognized that Wilton had prescribed a "more forgiving discretionary standard" to govern abstention in cases involving declaratory relief while Colorado River had applied a "more stringent . . . abstention test" in cases seeking monetary damages. (See id. at 4.) Acknowledging that Plaintiff's "breach of contract and declaratory judgment claims are inherently intertwined," Magistrate Judge Almond concluded that "this is not a Wilton case and the more stringent Colorado River abstention test should be applied." (Id.) Although he found that Clearwater's "forum-shopping arguments are appealing and supported by the record," Magistrate Judge Almond concluded that Clearwater had not made a "*sufficiently* compelling showing that would support dismissal" under the rigorous Colorado River analysis. (Id. at 3, 4 (emphasis added).)

II. LEGAL STANDARD

Pursuant to Federal Rule of Civil Procedure 72(b)(3), this Court must "determine *de novo* any part of the magistrate judge's disposition that has been properly objected to. The district judge may accept, reject or modify the recommended disposition; receive further evidence; or return the matter to the magistrate judge with instructions." A proper objection "must identify specific factual findings or recommendations to which objections are being made." Frusher ex rel. Frusher v. Astrue, Civ. No. 08-271-ML, 2009 U.S. Dist. LEXIS 113062, at *3 (Dec. 4, 2009) (Lisi, Ch. J.).

III. LEGAL ARGUMENT

Although Magistrate Judge Almond recognized the appeal of Clearwater's "forum shopping" and other arguments, he improperly and unnecessarily limited his own discretion by applying the rigorous Colorado River abstention standard. Given his conclusion that "the breach of contract and declaratory judgment claims are inherently intertwined," Magistrate Judge Almond should have applied the Wilton test. This would have afforded him greater discretion to prevent the Plaintiffs from forum shopping and to vindicate the policies underlying the federal removal statute.

A. The Wilton Abstention Standard Applies When Claims For Declaratory Relief Are "Inherently Intertwined" With Claims For Other Relief

Magistrate Judge Almond's conclusion that the stringent Colorado River standard applies both to the counts seeking declaratory relief and to the counts seeking damages is contradicted by First Circuit precedent. In Rossi v. Gemma, 489 F.3d 26 (1st Cir. 2007), the plaintiffs sought declaratory relief, injunctive relief and damages under 42 U.S.C. § 1983 as well as declaratory relief, injunctive relief and damages under a state law claim for slander of title. The district court dismissed the § 1983 claims under the Rooker-Feldman doctrine, and it dismissed the state law claims pursuant to Colorado River. The First Circuit affirmed the dismissal of all claims, but emphasized that the district court was mistaken to have relied on Colorado River in dismissing the claims for declaratory relief. It explained:

> Importantly, even though the district court concluded that there were 'exceptional circumstances' sufficient to justify abstention under Colorado River, **the Supreme Court has made clear that when declaratory relief is sought under state law, the rigorous Colorado River test need not be met, and a much more lenient standard is applicable**.

Id. at 38-39 (emphasis added) (citing Wilton). Given that the plaintiffs' claims for declaratory relief raised "an issue that has been presented in the [first-filed] state court proceedings," the

First Circuit held that "[i]t was within the district court's discretion to dismiss the claim for declaratory relief" under Wilton. Id. at 39. It then proceeded to analyze the state law damages claims separately, holding that no abstention analysis was necessary because the district court had properly declined to exercise supplemental jurisdiction. Id.

Rossi makes clear that the Wilton standard remains applicable in cases involving claims for declaratory relief, even if claims for monetary damages are also asserted. Magistrate Judge Almond therefore erred in applying the Colorado River standard.

In fact, other courts have also applied the Wilton standard in cases involving claims for both declaratory and monetary relief. In ITT Indus. v. Pacific Employers Ins. Co., 427 F. Supp. 2d 552 (E.D. Pa. 2006), for example, the plaintiff sued its insurer, seeking both declaratory relief and damages for breach of contract. The district court granted the insurer's motion to stay the proceedings in favor of a declaratory judgment action regarding the same coverage dispute pending in New York state court. It rejected the plaintiff's invitation to apply Colorado River, holding that "[t]o apply the Colorado River standard to actions containing both declaratory judgment and coercive claims without an analysis of the facts at hand would be to ignore the Supreme Court's specific recognition that declaratory judgment actions necessitate a different treatment than other types of cases." Id. at 557. Instead, the court "cut[] through the rhetorical fog of the pleadings" and concluded "that the essence of the dispute concern[ed] the scope of the insurance coverage . . . ." Id. Recognizing that it would "have to interpret the relevant insurance policies, and make a judgment on their scope and reach before ruling on the breach of contract or bad faith claims," the court held that "[a]t its heart, this dispute is a declaratory judgment action." Id. Consequently, it applied the Wilton standard to all of the plaintiffs claims.

More recently, another district court reached the same conclusion in Leonard v. State Farm Mut. Auto. Ins. Co., Civ. No. 08-1451, 2009 U.S. Dist. LEXIS 87241 (W.D. Pa. Sept. 2, 2009), aff'd as modified, 2009 U.S. Dist. LEXIS 87282 (W.D. Pa. Sept. 23, 2009). In that insurance coverage dispute, the plaintiffs sought declaratory and injunctive relief as well as damages for breach of contract against their automobile insurer. Id. at *1-2. The insurer moved to dismiss or stay, arguing that identical coverage issues were being litigated in a state court declaratory judgment action the insurer had filed. Id. at *3. The district court granted the motion, holding that the more lenient Wilton standard applied to all claims in the case. Citing ITT, it explained that "[t]he outcome of Plaintiffs' coercive claims is largely, if not totally, dependent on the scope of the State Farm policies. This action is, at heart, a declaratory judgment action, and the discretionary standard of Wilton applies." Id. at *17 (internal quotation marks and alterations omitted).

Other district courts have similarly concluded that the Wilton standard governs the abstention analysis in insurance coverage disputes where both declaratory and coercive claims are raised. See, e.g., General Nutrition Corp. v. Charter Oak Fire Ins. Co., Civ. No. 07-0262, 2007 U.S. Dist. LEXIS 75775, at *5 (W.D. Pa. Oct. 10, 2007) ("GNC's breach of contract and third-party beneficiary claims undoubtedly hinge on an interpretation of the Policy. . . . As such, any monetary relief for such claims depends on the outcome of the claim for declaratory relief. Because this is a declaratory judgment action at heart, we apply the Wilton standard."); Lexington Ins. Co. v. Rolison, 434 F. Supp. 2d 1228 (S.D. Ala. 2006) (applying Wilton in dismissing all claims where declaratory relief was asserted in the original complaint and a co-defendant asserted breach of contract as a counterclaim); Coletc Indus. v. Continental Ins. Co., Civ. No. 04-5718, 2005 U.S. Dist. LEXIS 8837, at *10 (E.D. Pa. May 11, 2005) (staying all

claims under Wilton because "[a]lthough [plaintiffs] also sue for breach of contract and bad faith, the outcome of those claims depends on how we interpret the policies when we resolve the declaratory judgment claim"); Scully Co. v. OneBeacon Ins. Co., Civ. No. 03-6032, 2004 U.S. Dist. LEXIS 9953 (E.D. Pa. May 24, 2004) (staying insured's claims for declaratory and coercive relief under Wilton); see also Lake Effect Inv. Corp. v. Blusso, No. 1:06cv1527, 2007 U.S. Dist. LEXIS 30602 (N.D. Ohio Apr. 24, 2007) (applying Wilton because "[t]o hold otherwise would give litigants the power to supercede the discretionary power given to the Courts by Congress in such cases by merely adding a monetary request for relief to any request for declaratory judgment"). As one district court persuasively explained:

> To eradicate that distinction [between Wilton and Coloardo River] simply because a coercive claim has been tacked onto what is, at its core, a declaratory judgment action would be to jettison . . . considerations of practicality and wise judicial administration, to exalt form over substance, to marginalize Wilton, and to undermine the statutory scheme established by Congress. If peripheral monetary claims could deprive district courts of the discretion granted them by the Declaratory Judgment Act to hear or not hear what are fundamentally declaratory judgment actions, then such claims would render federal courts virtually powerless (save for the rare case in which Colorado River abstention is warranted) to avert wasteful, duplicative litigation on exclusively state law issues in federal court running alongside parallel state litigation on the same issues, with concomitant disruption of the time honored values of federalism, comity and efficiency.

Rolison, 434 F. Supp. 2d at 1237.

The same considerations apply in this case. As Magistrate Judge Almond recognized, Plaintiffs' claims for declaratory and coercive relief are "inherently intertwined." (R. Doc. 18, at 4.) The common thread that binds these claims is that they are all dependent upon the scope of coverage provided in the reinsurance contracts at issue. This Court will need to interpret the policies before it can award any damages to Plaintiffs. As a result, this action is, at heart, a declaratory judgment action, and the discretionary standard of Wilton applies. See Leonard, 2009 U.S. Dist. LEXIS 87241, at *17.

B. Clearwater's Motion Should Be Granted Under The Applicable Wilton Standard.

Magistrate Judge Almond's application of Colorado River rather than Wilton is a legal error that led directly to his recommendation that Clearwater's motion be denied. The difference between these two abstention standards is far from academic. Colorado River emphasized that a district court has a "virtually unflagging obligation" to exercise jurisdiction and may only abstain from doing so in "exceptional circumstances." 424 U.S. at 813, 817. Colorado River abstention is "the exception, not the rule." Id. at 813. In contrast, Wilton recognizes that federal courts have "substantial discretion" to abstain in declaratory judgment cases. 515 U.S. at 286. Indeed, Wilton explicitly rejected the exceptional circumstances test in favor of a standard that is "more forgiving" and affords greater discretion to the district court. See Std. Fire Ins. Co. v. Gordon, 376 F. Supp. 2d 218, 223 (D.R.I. 2005).

As set forth in Clearwater's motion, this action is a classic example of forum shopping. Plaintiffs filed this case after needlessly delaying the progress of the Connecticut action for several months. In fact, Magistrate Judge Almond clearly acknowledged that the Plaintiffs were forum shopping, or attempting to circumvent the time limits for removal of an action from state to federal court. Under his view, however, those facts, while compelling, were not "*sufficiently* compelling" to justify abstention under Colorado River. (R. Doc. 18, at 3, 4 (emphasis added).) Analyzed under the Wilton standard, however, the arguments Clearwater has raised are more than sufficient to warrant the granting of its Motion.

IV. CONCLUSION

For the foregoing reasons, as well as those set forth in its motion to dismiss or stay this action, Clearwater respectfully objects to the Report and Recommendation that its motion be denied. Under the appropriate legal test set forth in Wilton, rather than the more exacting and

narrow standard of Colorado River that Magistrate Judge Almond erroneously applied, Clearwater's motion should be granted.

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CERTIFICATION

I hereby certify that on February 18, 2010, a copy of the foregoing was filed electronically and served by mail on anyone unable to accept electronic filing. Notice of this filing will be sent by email to all parties noted below by operation of the Court's electronic filing system or by mail to anyone unable to accept electronic filing as indicated on the Notice of Electronic Filing. Parties may access this filing for viewing and/or downloading through the Court's CM/ECF System.

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