

Emphasizing Key Distinction Between Defense And Indemnity Obligations, Second Circuit Clarifies Jurisdictional Standard For Declaratory Judgment Actions (Insurance Law Alert)

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Holding

The Second Circuit ruled that a New York district court properly concluded that it lacked jurisdiction to rule on a declaratory judgment action regarding an insurer's duty to indemnify for lack of a justiciable case or controversy, but remanded the case so that the district court could determine whether it had jurisdiction to address whether the insurer owed a duty to defend. *Admiral Ins. Co. v. Niagara Transformer Corp.*, 2023 U.S. App. LEXIS 297 (2d Cir. Jan. 6, 2023).

Background

Niagara purchased PCB chemicals from Monsanto for use in its manufacture of transformers. The purchase agreement provided that Niagara would defend and indemnify Monsanto against any claims arising out of the PCBs. When Monsanto was named as a defendant in suits across the country, it demanded defense and indemnity from Niagara. Although Niagara denied liability, Monsanto did not commence formal litigation against Niagara. Thereafter, Niagara notified Admiral, its insurer, of Monsanto's demands, seeking defense and indemnity in connection with any claims made by Monsanto. Admiral denied coverage and filed a declaratory judgment action, seeking a ruling that it had no duty to defend or indemnify. The district court granted Niagara's motion to dismiss on justiciability grounds, ruling that there was no "case or controversy" under the Declaratory Judgment Act because there was no "practical likelihood" that Niagara would incur liability. In so ruling, the district court emphasized that Monsanto had not sued Niagara or explicitly threatened to sue and that questions existed as to the enforceability of the indemnification agreement.

Decision

The Second Circuit affirmed the district court's ruling that it lacked jurisdiction to issue a declaratory judgment as to Admiral's duty to indemnify Niagara. The court explained that because the duty to indemnify is triggered by a determination of liability; the absence of any real or threatened litigation against Niagara, in conjunction with the uncertainty as to the validity and scope of the indemnification agreement,

meant there was no “practical likelihood” of a case or controversy as to Niagara’s duty to indemnify Monsanto.

However, the court remanded the matter with respect to a declaration as to Admiral’s duty to defend. The court explained that “the district court’s jurisdiction to declare Admiral’s duty to defend Niagara properly turns on the question of whether there exists a ‘practical likelihood’ that Monsanto *will file suit*.” (emphasis in original). Further, the court noted that a third-party action against an insured is a sufficient, but not necessary, condition for jurisdiction over a Declaratory Judgment Act suit based on the duty to defend.

Importantly, the court emphasized that even if the district court concludes that it has jurisdiction to declare Admiral’s duty to defend Niagara, it may nevertheless decline to exercise such jurisdiction.

Implications

This decision not only highlights the important distinction between an insurer’s defense and indemnity obligations in the context of the justiciability analysis, but also clarifies the “considerable confusion” among district courts as to the scope of discretion in declining to exercise jurisdiction in such cases, even where jurisdiction is deemed to exist. In particular, the court reiterated the “broad discretion” of district courts to decline jurisdiction based on six enumerated considerations, at the same time noting that discretion in this context is not “unfettered.”

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