IN THE COURT OF APPEALS
STATE OF NEW MEXICO

NAUTILUS INSURANCE COMPANY,

Plaintiff / Appellee,

vs.

COA No. 33,820
D-504-CV-2012-00654

OHIO SECURITY INSURANCE COMPANY,

Defendant / Appellant.

PLAINTIFF-APPELLEE'S ANSWER BRIEF

Civil Appeal from the Fifth Judicial District Court
District Court No. 5-504-CV-2012-00654
The Honorable Charles C. Currier Presiding

Oral Argument Requested

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Certificate of Compliance

As required by Rule 12-213(G), NMRA (2015), I certify that this Brief uses a proportionally-spaced type style or typeface, such as Times New Roman, and that this Brief contains 7796 words as calculated by Microsoft Office 2013, the word processing system used to prepare this Brief.

SUMMARY OF PROCEEDINGS

I. Nature of the case

This is an appeal from a final judgment entered by the district court on April 16, 2014 in a subrogation action between two insurers, Nautilus Insurance Company ("Nautilus") and Ohio Security Insurance Company ("Ohio Security"). [RP 223] The district court ruled initially on cross-motions for summary judgment, and later in the final judgment, that (1) Ohio Security owed its insured, Norman/Dent Custom Homes, Inc. ("Norman/Dent"), a duty to defend in the underlying action, and (2) Ohio Security's breach of its duty to defend estopped it from asserting or relying on policy exclusions to limit or avoid its indemnity obligations. [RP 223-25]

II. Course of Proceedings and Disposition Below

Nautilus filed the present subrogation action against Ohio Security to recover amounts it paid on behalf of its insured in connection with a lawsuit brought by John and Jamie Lewinger. [RP 1-7] After discovery concluded, the parties entered into a Stipulation of Facts, and, thereafter, filed cross-motions for summary judgment based on the stipulated facts. [RP 68-109, 121-167]

Ohio Security argued in its motion that it owed no duty to defend or indemnify in the underlying action because certain exclusions applied to preclude coverage for all of the Lewingers' claims. [RP 69] Nautilus argued in its motion for partial summary judgment that Ohio Security owed a duty to defend because the Complaint

filed against the insured was too ambiguous to allow for a determination that the exclusions applied as a matter of law. [RP 121] Nautilus further argued that Defendant's breach of its duty to defend estopped it from relying on policy exclusions to avoid or limit its indemnity obligations. [RP 121]. The parties' cross motions were heard by the district court on November 4, 2013. [RP 196]

Counsel presented oral argument at the hearing before the presiding judge, the Honorable Charles C. Currier. [RP 196] The remarks made by counsel and by Judge Currier at the hearing are important because they further confirm which issues were, and which issues were not, in dispute in the proceedings below. They show that the issue of whether Ohio Security owed a duty to defend was clearly disputed. They also show, however, that Ohio Security did not contest, dispute or challenge Nautilus' assertion that Ohio Security's breach of its duty to defend estopped it from relying on or asserting policy exclusions to limit or avoid its indemnity obligations.

At the hearing, counsel for Nautilus emphasized, in accordance with its written briefing, that Ohio Security had not challenged Nautilus' arguments regarding the estoppel issue or its application in this case. [Tr. 15:47 – 17:37]. Opposing counsel responded by stating that, as far as the estoppel issue was concerned, "the law is what the law is, and I'm sure your honor knows that, and so we're not really focusing on that right now …". [Tr. 30:50 – 31:47]. This led Judge Currier to remark that, insofar as the estoppel issue was concerned, "again, there

doesn't appear to be dispute...". [Tr. 53:22 – 54:42]. Throughout the proceedings below, Ohio Casualty consistently maintained the position that the only reason it had no indemnity obligations was because it owed no duty to defend. [RP 118, 136-39; Tr. 15:47 – 17:37, Tr. 30:50 - 31:47].

At the conclusion of the hearing, Judge Currier ruled from the bench, granting Nautilus' motion and denying Defendant's motion. [Tr. 53:55 – 54:50] Later, on November 6, 2013, the district court entered its Order to that same effect. [RP 197-98] On April 16, 2014, after the parties had stipulated to certain additional facts and damages, the district court entered its Final Judgment. [RP 218-20, 223-25] Appellant timely filed a Notice of Appeal in the district court on May 13, 2014. [RP 227] No cross-appeal has been filed.

III. Summary of Facts

John and Jamie Lewinger entered into a New Home Construction Contract with Norman/Dent in or around December of 2005. [RP 2, 89, 102] Construction of the new home was finished in or around October of 2006. [RP 142] Within the first year of having moved into the home, the Lewingers noticed cracks on both the exterior and interior sections of the home. [RP 157] They reported the problems to Norman/Dent and cosmetic repairs were made to cover the cracks. [RP 157] The cracking continued inside and outside of the home, which led to an inspection by Norman/Dent in October of 2009. [RP 157]

After the inspection, a stucco subcontractor, selected by Norman/Dent, attempted to patch the cracks and to seal a large crack that had developed in the concrete patio slab. [RP 157] But the cracking continued to occur and the number and severity of the cracks accelerated. [RP 157] On August 11, 2010, the Lewingers notified Norman/Dent in writing that it was in breach of contract. [RP 160] On or about August 24, 2010, Nautilus received notice that the Lewingers were asserting a claim against Norman/Dent's insurance policy. [RP 141]

While investigating the claim, Nautilus discovered that Norman/Dent was also insured by Ohio Security for the periods of time pertinent to the claim. [RP 141- 42] Accordingly, Nautilus contacted Ohio Security and asked it to set up a claim. [RP 142] Shortly thereafter, on January 7, 2011, the Lewingers filed suit against Norman/Dent in the Second Judicial District Court. [RP 88]. On or about March 7, 2011, Nautilus asked Ohio Security to share in the cost of defending Norman/Dent against the action brought by the Lewingers. [RP 142]. Ohio Security refused Nautilus' request on April 20, 2011. [RP 142]

The Lewingers' Complaint was a typical construction defect complaint, but it did not allege that any one defect in particular was the cause of all of the alleged damage. [RP 88 – 100] Rather, the Lewingers broadly alleged that the construction was defective for a number of reasons, including faulty soil compaction, deficient or inadequate plans and specifications, structural problems and drainage issues. [RP

90 – 91, 98] Additionally, it was alleged in the Complaint that the Lewingers' investment in the home, lot and subsequent improvements to the property was in excess of $1,000,000.00, and that they had been damaged in an amount in excess of $1,000,000.00. [RP 89, 96] The Complaint did not specifically identify what subsequent improvements had been made, nor did it expressly allege whether or not any of the subsequent improvements had been damaged. [RP 88-100]

Shortly after Ohio Security refused to defend Norman/Dent, the district court referred the Lewingers' suit to binding arbitration. [RP 142]. Nautilus defended Norman/Dent under a full reservation of rights throughout the lawsuit and arbitration. [RP 218] The Lewingers ultimately received an arbitration award against Norman/Dent in the amount of $684,629.82. Nautilus paid the arbitration award in full. [RP 218] A Satisfaction was filed with the Second Judicial District Court on March 20, 2012. [RP 218] Additionally, Nautilus incurred, and, paid in full, defense costs, including attorney's fees and expert's fees, in the amount of $284,939.04 in connection with the Lewingers' action. [RP 218] The Final Judgment obtained by Nautilus in its subrogation action against Ohio Security awarded Nautilus total damages of $546,943.02. [RP 225].

ARGUMENT

I. THE DISTRICT COURT CORRECTLY CONCLUDED THAT OHIO SECURITY OWED A DUTY TO DEFEND BECAUSE AMBIGUITIES IN THE LEWINGERS' COMPLAINT WOULD NOT ALLOW FOR A DETERMINATION THAT THE POLICY EXCLUSIONS APPLIED AS A MATTER OF LAW.

Standard of Review

Summary judgment is appropriate where there are no genuine issues of material fact and the movant is entitled to judgment as a matter of law. Self v. United Parcel Serv., Inc., 1998-NMSC-046, ¶ 6, 126 N.M. 396, 970 P.2d 582. Where the facts are entirely undisputed, or when summary judgment is decided on stipulated facts, the legal questions are reviewed *de novo*. See id; Barncastle v. Am. Nat. Prop. and Cas. Co., 2000-NMCA-095, ¶ 5, 129 N.M. 672, 11 P.3d 1234. Furthermore, the issue of whether a complaint is ambiguous is a question of law subject to a *de novo* standard of review. See Envtl. Control Inc. v. City of Santa Fe, 2002-NMCA-003, ¶ 14, 131 N.M. 450, 38 P.3d 891 ("Whether ambiguity exists is a question of law; therefore, this Court reviews the district court's decision *de novo.*").

Preservation

Appellee agrees that Appellant raised and preserved the issue of whether or not a duty to defend was owed. [RP 68-79, 111-119].

The question presented to the insurer in each case involving the duty to defend is whether the injured party's complaint states facts which bring the case within the coverage of the policy, not whether he can prove an action against the insured for damages. Am. Emp'rs' Ins. Co. v. Cont'l Cas. Co., 1973-NMSC-073, ¶¶ 4-5, 85 N.M. 346, 512 P.2d 674. "The duty of an insurer to defend arises from the allegations on the face of the complaint or from the known but unpleaded factual basis of the claim that brings it arguably within the scope of coverage." Am. Gen. Fire & Cas. Co. v. Progressive Cas. Co., 1990-NMSC-094, ¶ 11, 110 N.M. 741, 799 P.2d 1113.

In New Mexico, insurers must fulfill their promise to defend even though an injured party's complaint fails to state facts with sufficient clarity so that it may be determined from its face whether or not the action is within the coverage of the policy, provided the alleged facts tend to show an occurrence within the coverage. Am. Emp'rs' Ins. Co., 1973-NMSC-073 at ¶¶ 4-5. Where the pertinent allegations of a complaint are ambiguous or incomplete, they are construed in favor of the duty to defend. Foundation Reserve Ins. Co. v. Mullenix, 1982-NMSC-038, ¶ 8, 97 N.M. 618, 642 P.2d 604. To successfully show that no defense was owed, the insurer disclaiming coverage must prove as a matter of law that all claims asserted in a complaint fall within the scope of the exclusion(s) relied upon. See Lopez v. N.M. Pub. Schs. Ins. Auth., 1994-NMSC-017, ¶ 11, 117 N.M. 207, 870 P.2d 745.

A. The District Court Properly Concluded That Ohio Security Failed to Show That the "Your Work" or "Impaired Property" Exclusions Precluded the Duty to Defend Because the Complaint Was Ambiguous Regarding Damage to Subsequent Improvements.

Appellant relies upon the policy's "Your Work" exclusion to support its argument that it owed Norman/Dent no duty to defend. *Brief-in-Chief, pp. 15 -21.* This exclusion states that no coverage is afforded for "property damage" to "your work" arising out of it or any part of it and included in the "products completed operations hazard." [RP 144, 148]. The term "your work" is defined by the policy, in pertinent part, to mean "work or operations performed by you or on your behalf." [RP 150]. Thus, by its very terms, the "Your Work" exclusion does not apply when there is damage to other property - that is, property not considered to be work performed by or on behalf of the insured. Computer Corner, Inc. v. Fireman's Fund Ins. Co., 2002-NMCA-054, ¶¶ 15-16, 132 N.M. 264, 46 P.3d 1264.

Nautilus argued in the proceedings below, and the district court agreed, that the Lewinger Complaint was ambiguous regarding whether or not "other property" had been damaged. [RP 130, 197-98]. The ambiguity arises from the Complaint's reference to "subsequent improvements." Specifically, the Lewingers alleged that their investment in the home, lot and subsequent improvements to the property was in excess of $1,000,000.00, and that they had been damaged in an amount in excess of $1,000,000.00. [RP 89, 96]

In drafting their Complaint, the Lewingers did not specify what subsequent improvements to their property had been made. [RP 88–100] But they did generally allege damage to many different areas of their property. [RP 88-100] As one example, they alleged that there was damage to the "shop area." [RP 159] However, in reading the Complaint, there is no way of knowing whether or not the "shop area" was one of the subsequent improvements. As a result, Ohio Security was required to do exactly what Nautilus did - construe the ambiguity in favor of the existence of a duty to defend. See Am. Emp'rs' Ins. Co., 1973-NMSC-073 at ¶¶ 4-5. However, Ohio Security chose to take a different route. It opted, instead, to assume facts that were not stated in the Complaint just so that it could apply its exclusionary provision. This is contrary to established New Mexico insurance law. See id.

Ohio Security's arguments on appeal concerning the "Your Work" exclusion are unavailing because they urge application of the wrong rule. Ohio Security argues that the applicable rule is that courts are not permitted to assume facts that are not stated in the complaint. *Brief-in-Chief*, pp. 17-20, (*citing* State Farm Fire & Cas. Co. v. Mhoon, 31 F.3d 979 (10th Cir. 1994)). But this rule only applies when the issue is whether or not the complaint state facts suggesting the case falls within the policy's coverage. See id. at 985; Western Commerce Bank v. Reliance Ins. Co., 1987-NMSC-009, ¶ 5, 105 N.M. 346, 732 P.2d 873. Where facts *are* alleged that tend to show the case falls within coverage, the rule does not apply. See id.

The rule Ohio Security urges this Court to apply has no application here because it is undisputed that the Lewinger Complaint stated facts falling within the policy's coverage. Ohio Security stipulated, as fact, in the proceedings below that the Complaint alleged both an "occurrence" and "property damage." [RP 143]. Thus, unlike the cases on which Ohio Security relies, the insuring clause of its policy *was* fully satisfied and the action necessarily fell within the policy's coverage. Consequently, the burden shifted to Ohio Security to demonstrate that its exclusions applied to preclude coverage. See Battishill v. Farmers Alliance Ins. Co., 2006-NMSC-004, ¶ 6, 139 N.M. 24, 127 P.3d 1111 (after burden of showing coverage is met, the burden shifts to the insurer to prove that the loss was not covered due to an exception, exclusion or other limitation).

New Mexico law is clear than an insurer attempting to meet this burden is not permitted to assume facts that are not found within the four corners of the complaint. See Mullenix, 1982-NMSC-038, ¶¶ 8-9. In Mullenix, the Court noted the complaint tended to show an occurrence within the coverage of the policy. Id. at ¶ 8. The Court then shifted its focus to the issue of whether or not the complaint alleged facts that would allow for application of the exclusionary provision. Id. The Court concluded that the exclusion at issue, a towing exclusion, could not be applied as a matter of law because the language of the complaint was ambiguous in that it did not allege that the vehicle was being towed. Id.

Ohio Security, like the insurer in Mullenix, assumed the existence of facts that were not alleged in the complaint to reach the conclusion that the "Your Work" exclusion applied. It assumed that the Lewingers' subsequent improvements to their property either had not been damaged and/or that they were Norman/Dent's own work. The Mullenix opinion plainly demonstrates that Ohio Security was not permitted to make either assumption because the complaint did not unambiguously supply the answer to the question. See id. Thus, as in Mullenix, the only conclusion that could be drawn was that Ohio Security owed a duty to defend. See id; Am. Emp'rs' Ins. Co., 1973-NMSC-073 at ¶¶ 4-5.

Ohio Security also makes passing reference to the "impaired property" exclusion to support its argument on the duty-to-defend issue. *Brief-in-Chief*, pp. 19-20. Significantly, this is an exclusion which has been held by this very Court to be "unintelligible from the standpoint of a hypothetical reasonable insured." Computer Corner, Inc., 2002-NMCA-054 at ¶ 20. In spite of this, Ohio Security did not cite the opinion, or attempt to distinguish it in any way, in its *Brief-in-Chief*. Moreover, Ohio Security fails to mention that the district court read the Computer Corner, Inc. opinion to mean that the "Your Work" and "Impaired Property" exclusions were ambiguous as a matter of law and unenforceable. [Tr. 31:55 – 36:33]

In any event, it is clear that the district court was right to reject Ohio Security's arguments on the "impaired property" exclusion because, again, the Complaint was too ambiguous to allow for a determination that the exclusion applied as a matter of law. The "impaired property" exclusion, like the "Your Work" exclusion, does not apply when there is damage to other property. See 9A *Lee R. Russ & Thomas F. Segalla*, Couch on Insurance, § 129:21 (3d ed. 2014). Because the Lewingers' Complaint was ambiguous regarding damage to subsequent improvements, Ohio Security could not show that the "impaired property" exclusion was applicable any more than it could the "Your Work" exclusion. Accordingly, the exclusion could not serve as a valid basis to disclaim the duty to defend.

B. The District Court Properly Concluded That Ohio Security Failed to Show That All Property Damage Alleged in the Complaint Was Related to Subsidence.

Ohio Security also relies on the policy's "Subsidence" exclusion to support its contention that it owed no duty to defend. This exclusion, in pertinent part, states that coverage does not apply to "property damage" arising out of "any loss, claim, suit or other proceeding arising out of, caused by, resulting from, contributed to, or aggravated by subsidence, settling, slipping, falling away, caving in, shifting, eroding, mud flow, rising, tilting, or any other movement of land or earth, whether such movement of land or earth occurs alone, in combination with, before, after or

concurrently with any other cause, contributing condition, or aggravating factor." [RP 144-45, 153]. Ohio Security's reliance on this exclusion is unavailing.

The Lewingers' Complaint can be reasonably read to allege that at least some of the construction defects were caused by subsidence or movement of land. This, however, does not show that no duty to defend existed because the operative question is whether Ohio Security carried its burden of showing that *all of the damage* was related to subsidence. See Lopez, 117 N.M. at 209. Not only was this burden not met by Ohio Security; it was an impossible burden to carry because the complaint was ambiguous regarding whether all of the damage incurred was related to subsidence.

To illustrate, the Lewingers' Complaint alleged a variety of construction defects: (1) inadequate preparation of soils at the construction site, (2) inadequate compaction testing, (3) significant structural defects, (4) deficient plans and specifications, (5) failure to construct the home in accordance with the plans and specifications, (6) failure to exercise ordinary care and competence with respect to the construction and (7) drainage issues. [RP 88 – 100, ¶¶ 16, 19, 20, 21, 36, 45, and 64]. The allegations relating to inadequate soil preparation and compaction testing may very well have implicated the Subsidence exclusion. But what about all of the other allegations?

Again, the Complaint left a number of important questions unanswered. How were the plans and specifications deficient? Did any such deficiency cause, or contribute to, subsidence or movement of land, as opposed some other type of movement or damage? Did the deficient plans and specifications cause the land to move in such a way as to damage the subsequent improvements to the property? Did Norman/Dent's alleged failure to follow the plans and specifications result in subsidence or movement of land? How does the allegation of "drainage issues" fit into the equation?

The fact that the Complaint left these questions unanswered is crucial because it shows that the Complaint was too ambiguous to allow for a conclusion, as a matter of law, that the Subsidence exclusion applied across-the-board. See Mullenix, 1982-NMSC-038 at ¶ 8. Contrary to what Appellant appears to argue, the Lewingers did not tie each and every alleged construction defect to the movement of soil. The Complaint did not allege, for example, that Norman/Dent's failure to follow the plans and specifications resulted in the movement of the foundation or cracking. Nor did it allege that the deficiency in the plans and specifications themselves resulted in subsidence. Without specific allegations of this nature, it was impossible to tell from the face of the Complaint whether or not all of the damage alleged was related to subsidence.

In reaching its decision to deny coverage, Appellant merely assumed that there was a connection between all of the alleged defects and subsidence. Not only was this improper; it was a rather large assumption to make. Generally speaking, the cracking of a concrete slab, which was alleged in the Complaint, can occur as the result of both subsidence and non-subsidence related construction defects. Concrete can crack when the maximum load is exceeded. Errors in the design, such as mistakes in estimating the expected loads, calculation errors and even the transfer of calculations into plans and specifications can result in a structure that is unable to carry the loads. As a further example, concrete can crack when the ready-mixed concrete supplier uses the wrong mix design or makes measurement errors. Other times, it can be defective or substandard material used in the mix or application by the contractor who chose to add more water than allowed.

These are but a few examples of defects that are not related to subsidence or earth movement, yet still result in cracking. Ohio Security could not have known from the face of the Complaint whether all of the cracking was caused by subsidence or whether some was caused by other defects such as those noted above. In fact, the Complaint makes clear that even the Lewingers did not know the precise cause(s) of the damage to their property because of an ongoing work product dispute over the engineering report. [RP 160-61, ¶¶ 31, 32, and 36] Regardless, the fact that the

Lewingers may have tied some of the defect allegations to the movement of soil does not somehow mean that all of the other deficiencies were tied to subsidence as well.

In short, it would have been reasonable for Ohio Casualty to read the Lewingers' Complaint and suspect that the policy's Subsidence exclusion may ultimately have some application at the indemnification stage of the case. But it was not at all reasonable for it to cast aside patent ambiguities in order to reach the desired, yet unsupported, conclusion that all of the damage was related to subsidence. See Mullenix, 1982-NMSC-038, ¶¶ 8-9. The district court agreed that Ohio Security acted unreasonably in this regard, and, therefore, ruled that the subsidence exclusion did not preclude the duty to defend. The ruling was correct and it should be upheld.

C. The District Court Properly Concluded That Ohio Security Failed to Show That the "Professional Liability" Exclusion Applied as a Matter of Law to Exclude Coverage For All of the Lewingers' Claims.

Ohio Security conceded in the proceedings below that the "professional liability" exclusion was potentially inapplicable to some of the Lewingers' claims. [RP 117, 188]. It is unclear whether or not Ohio Security is attempting to walk back this concession on appeal. See *Brief-in-Chief*, p. 14. Nevertheless, it is clear that the district court did not err in concluding that Ohio Security failed to show as a matter of law that the Lewingers' claims were excluded from coverage by the Professional Liability exclusion.

The analysis regarding whether or not the Professional Liability exclusion precluded the duty to defend closely mirrors that of the exclusions discussed above. As is true with respect to the other exclusions, the issue again turns on whether or not the Lewinger Complaint was ambiguous. If the allegations of the Complaint unambiguously alleged that all of the damage to the home was caused by the deficient compaction testing, then the exclusion would be wholly applicable. If, on the other hand, the allegations of the Complaint do not clearly answer the issue, the exclusion cannot support the contention that no duty to defend was owed. Am. Emp'rs' Ins. Co., 1973-NMSC-073 at ¶¶ 4-5.

The questions left unanswered by the Lewingers' Complaint that are pertinent to the Professional Liability exclusion are also similar to those it left unanswered in connection with the Subsidence exclusion. How were the plans and specifications deficient? Did such deficiency somehow cause the compaction testing to be improperly performed? Did improper compaction testing damage the subsequent improvements to the property? Did Norman/Dent's failure to follow the plans and specifications affect how the compaction testing was conducted? How does faulty compaction testing relate to the Complaint's allegation of "drainage issues"? Were all of the defects caused by faulty compaction testing or were some caused by other, unrelated acts or omissions?

Again, the fact that the Complaint left these questions unanswered is crucial because it shows that the Complaint was too ambiguous to allow for a conclusion, as a matter of law, that the Professional Liability exclusion applied across-the-board. See Mullenix, 1982-NMSC-038, ¶ 8. Accordingly, the district court was correct in ruling that Ohio Security could not rely on the exclusion to disclaim its duty to defend Norman/Dent. See id.

II. THIS COURT SHOULD AFFIRM THE DISTRICT COURT'S RULING THAT APPELLANT WAS ESTOPPED FROM ASSERTING POLICY EXCLUSIONS TO LIMIT OR AVOID ITS INDEMNITY OBLIGATIONS BECAUSE APPELLANT FAILED TO PRESERVE ANY ERROR BELOW.

Appellant advances two separate and distinct arguments regarding the district court's ruling that it was estopped from relying on or asserting coverage defenses to avoid or limit its indemnity obligations. *Brief-in-Chief*, pp. 21-30. The first argument is that estoppel should not apply because no duty to defend was owed. *Brief-in-Chief*, p. 21. The second argument is that the doctrines of waiver and estoppel do not apply in the context of a dispute between two insurers. *Brief-in-Chief*, p. 21. It is clear that the first of Appellant's arguments was properly preserved. [RP 68-79, 111-119] It is equally clear, however, that Appellant's second argument was not.

The issue of estoppel was raised in the district court by Nautilus in its Motion for Partial Summary Judgment. [RP 121]. Nautilus argued that, if the district court

were to rule in its favor on the duty-to-defend issue, Ohio Security should then be estopped from relying upon its policy exclusions to limit or avoid its duty to indemnify. [RP 136]. Nautilus submitted case law directly on point for the district court to consider, and it advanced numerous arguments in support of the rule's application. [RP 136-39]. Significantly, however, Ohio Security did not challenge Nautilus' arguments or authorities regarding the estoppel issue in the district court. [RP 118]. Instead, it maintained that it had no indemnity obligations merely because it owed no duty to defend. [RP 118]. This is not the same argument that is now being advanced as Ohio Security's second argument on appeal, and Nautilus submits that it was not preserved in the district court.

It is well established that arguments that were not preserved in the district court are not reviewed on appeal. Village of Angel Fire v. Board of County Comm's of Colfax County, 2010-NMCA-038, ¶ 15, 148 N.M. 804, 242 P.3d 371. The primary purposes for the preservation-of-error rule are (1) to specifically alert the district court to a claim of error so that any mistake can be corrected at that time, (2) to allow the opposing party a fair opportunity to respond to the claim of error and to show why the court should rule against that claim, and (3) to create a record sufficient to allow the appellate court to make an informed decision regarding the contested issue. State v. Lopez, 2008-NMCA-002, ¶ 8, 143 N.M. 274, 175 P.3d 942 (2007).

"[T]o preserve an issue for review on appeal, it must appear that *appellant* fairly invoked a ruling of the trial court on the same grounds argued in the appellate court." Selmeczki v. N.M. Dept. of Corrections, 2006-NMCA-024, ¶ 23, 139 N.M. 122, 129 P.3d 158, *quoting* Woolwine v. Furr's, Inc. 106 N.M. 492, 496, 745 P.2d 717, 721 (Ct.App.1987) (*emphasis in original*). Moreover, an appellant cannot rely on the argument of the opposing party to preserve error. Azar v. Prudential Ins. Co. of America, 2003-NMCA-062, ¶ 25, 133 N.M. 669, 68 P.3d 909.

In this case, Ohio Security did not ask the district court to rule that it was entitled to rely on its policy exclusions to avoid or limit its indemnity obligations in the event that a duty to defend was found. The only argument ever advanced by Ohio Security was that it should not be stripped of its policy exclusions *because it owed no duty to defend.* [RP 118] Presently, however, Ohio Security takes the position for the first time on appeal that the trial court's ruling on the estoppel issue was in error because the doctrines of waiver and estoppel do not apply in subrogation cases. *Brief-in-Chief*, p. 21.

The record plainly demonstrates that Ohio Security did not alert the district court to any claim of error on the estoppel issue. In fact, Nautilus pointed out to the district court in its summary judgment briefing that "Defendant does not contest any of the arguments advanced by Nautilus on the issue." [RP 188] Nautilus also emphasized, accordingly, that "should the Court disagree with Defendant and find

that it owed and breached the duty to defend, there is no stated opposition to a ruling that Defendant is estopped from relying on its policy exclusions to avoid or limit its indemnity obligations." [RP 188-89]

In spite of these representations, Ohio Security's position never changed, even at the time of the summary judgment hearing. At the hearing, counsel for Nautilus emphasized, in accordance with its written briefing, that Defendant had not challenged Nautilus' arguments regarding the estoppel issue or its application in this case. [Tr. 15:47 – 17:37] Opposing counsel responded by stating that, as far as the estoppel issue is concerned, "the law is what the law is, and I'm sure your honor knows that, and so we're not really focusing on that right now ...". [Tr. 30:50 – 31:47] This led the presiding judge to remark that, insofar as the estoppel issue was concerned, "again, there doesn't appear to be dispute...". [Tr. 53:22 – 54:42]

Not once did counsel for Ohio Security mention, either at the hearing or in the written briefing, that Ohio Security should not be subject to the doctrine of estoppel in the event a duty to defend was found. Consequently, the district court was not afforded any opportunity to correct the error of which Ohio Security now complains on appeal. See Village of Angel Fire, 2010-NMCA-038 at ¶ 15. It is undeniably unfair, unjust and against this Court's rules for Appellant to complain about the district court's ruling on this issue without ever having asked the district court to rule on it. See id; Selmeczki, 2006-NMCA-024 at ¶ 23.

Because the district court was never asked to rule in Ohio Security's favor on the estoppel issue on grounds that the doctrine does not apply in subrogation cases, it also stands to reason that Nautilus was never given the opportunity in the district court to respond to the argument. Appellant did not advance any argument, or submit any authority, in the district court to show that it should not be estopped from relying on its exclusions if a duty to defend existed. Nor did it present any argument or authority to show that the doctrine of estoppel does not apply in subrogation cases. Nautilus could not have responded in the court below to an argument that was never raised. Simply stated, the issue was uncontested in the district court. Accordingly, there is not a sufficient record to allow this Court to make an informed decision regarding a "contested issue." Village of Angel Fire, 2010-NMCA-038 at ¶ 15.

Nautilus further submits that Ohio Security cannot rely on Nautilus' efforts to raise the issue of estoppel in the district court to show that its claimed error was preserved. Azar, 2003-NMCA-062 at ¶ 25. The fact that Nautilus argued for application of the estoppel rule does nothing to aid Ohio Security in making its necessary showing that error was preserved. Id. It is the Appellant who must invoke the ruling of the trial court on an issue – not the Appellee. See id; Selmeczki, 2006-NMCA-024 at ¶ 23.

The New Mexico Rules of Appellate Procedure require an appellant to include in their Brief-in-Chief "a statement explaining how the issue was preserved in the

court below with citations to authorities, record proper, transcripts of proceedings or exhibits relied on." Rule 12-213(A)(4), NMRA (2015). In this appeal, aside from a solitary, conclusory statement, Appellant does not even attempt to describe how the issue was preserved in the district court. *Brief-in-Chief*, pp. 21-22. This is in spite of the fact that Nautilus argued at length in its Memorandum in Support of Proposed Summary Disposition that Ohio Security did not preserve any error regarding the district court's ruling on the estoppel issue. See *Appellee's Memorandum in Support of Proposed Summary Disposition*, pp. 5-9.

Moreover, Appellant did not present any authority, or cite to the transcript of proceedings or exhibits in accordance with Rule 12-213(A)(4). Rather, Appellant merely cites one page of the record proper in support of their contention that any error was preserved. *Brief-in-Chief*, p. 22. The page of the record proper which was cited, however, contains no reference to any argument that the doctrines of waiver and estoppel do not apply in subrogation cases. [RP 118]. Rather, it refers to the only argument concerning the estoppel issue that was ever made by Ohio Security in the district court: "Ohio Security is not Estopped From Relying on its Policy Exclusion Because it Correctly Denied a Defense to Norman/Dent." [RP 118].

This is clearly not the same argument which is now being advanced on appeal. It is not even close. Ohio Security should not be allowed raise new arguments, skirt the issue of preservation and hope that the appellate court does not notice. Nautilus

submits that this Court should take notice and affirm the district court's ruling on estoppel issue on grounds that the claimed error was not preserved. Village of Angel Fire, 2010-NMCA-038 at ¶ 15; Selmeczki, 2006-NMCA-024 at ¶ 23; Azar, 2003-NMCA-062 at ¶ 25.

III. THE DISTRICT COURT'S JUDGMENT ON THE ESTOPPEL ISSUE SHOULD BE UPHELD, EVEN IF APPELLANT'S UNPRESERVED ARGUMENTS ARE CONSIDERED, BECAUSE IT IS CONSISTENT WITH NEW MEXICO LAW.

A. The Doctrine of Estoppel is Applicable Because, Under New Mexico Law, Nautilus, as a Subrogated Insurer, is Granted the Same Rights as the Insured.

Ohio Security argues for the first time on appeal that the New Mexico Supreme Court's decision in Am. Gen. Fire & Cas. Co. demonstrates that the doctrine of estoppel is not available in a subrogation action between two insurers. *Brief-in-Chief*, p. 23-25. According to Appellant, estoppel is not available in this context because the doctrine is only warranted where there is prejudice to the insured. Appellant argues that there was no prejudice to Norman/Dent in this action because Nautilus provided a defense and indemnification, and, as a result, there is no reason for the doctrine of estoppel to apply.

Appellant's argument should be summarily rejected because it is premised on a misunderstanding of the Court's opinion in Am. Gen. Fire & Cas. Co. In that case, the Court held that the doctrine of estoppel was not available *to preclude* the subrogated insurer's ability to bring a subrogation action against a breaching insurer.

1990-NMSC-094 at ¶ 16. The Court reasoned that the doctrine, which in that context was based on the concept of prejudice to the insured, had no application to the subrogated insurer's right or ability to recover against the breaching insurer. See id.

The Court's holding does not, however, stand for the blanket proposition that the doctrine of estoppel is never available in a subrogation action involving two insurers. See id. If anything can be extrapolated from the opinion, it is that the doctrine of estoppel cannot be asserted by the breaching insurer to preclude the subrogated insurer's right of recovery against it. This makes perfect sense. The doctrine of estoppel was a defense held by the insured. The Court simply reasoned that a defense held by the insured was not available to the breaching insurer to prevent a subrogation recovery because the rationale for the estoppel rule under consideration had no application between the insurers. See id.

This stands in sharp contrast to the present case where the doctrine of estoppel is being relied upon *by the subrogated insurer to obtain a recovery against the breaching insurer.* Moreover, unlike the version of estoppel at issue in Am. Gen. Fire & Cas. Co., the doctrine of estoppel applied here is actually consistent with New Mexico subrogation law. Nautilus, as a subrogated insurer, "is considered to be standing in the shoes of its insured." Health Plus of New Mexico, Inc. v. Harrell, 1998-NMCA-064, ¶ 15, 125 N.M. 189, 958 P.2d 1239. And, "[b]y standing in the

shoes of the insured," Nautilus "has the same rights and is subject to the same defenses as the insured." Id.

Therefore, assuming Norman/Dent had the right to rely on the doctrine of estoppel to preclude Ohio Security from asserting coverage defenses to limit or avoid its indemnity obligations, Nautilus should also be granted that right. See id. In this regard, it is important to note that Appellant does not take issue with Norman/Dent's right or ability to apply the doctrine of estoppel. See *Brief-in-Chief*, p. 27 ("... Ohio Security may have been precluded from asserting coverage defenses to limit or avoid its indemnity obligations in a suit by the insured ..."). Thus, all that is required to defeat Appellant's newly-asserted argument is application of the basic subrogation principle that subrogated insurers are granted the same rights as their insureds. See Harrell, 1998-NMCA-064 at ¶ 15.

B. The District Court's Ruling on the Estoppel Issue is Consistent with New Mexico Insurance and Subrogation Law.

This Court, in its Notice of Proposed Summary Disposition, correctly concluded that the Supreme Court's opinion in Collier v. Union Indem. Co. supports the proposition that an insurer will not be allowed to rely on policy exclusions where the insurer failed to defend its insured. 1934-NMSC-030, 38 N.M. 271, 31 P.2d 697. Ohio Security does not take issue with the Court's conclusion. See *Brief-in-Chief*, p. 26. In fact, Ohio Security only takes issue with the proposition that the doctrine of estoppel can be applied in the context of a subrogation action involving two

insurers. See *Brief-in-Chief*, p. 26 ("*Collier* and other cases involving suits between and insured and its insurer are distinguishable from the instant case which involves an action by one insurer against another insurer for equitable subrogation.").

The fact that Collier was not an action between two insurers is immaterial because subrogated insurers are granted the same rights as their insureds. See Harrell, 1998-NMCA-064 at ¶ 15. What is material, however, is the Supreme Court's reasoning in Collier that the breaching insurer cannot claim the benefits of its contract after having refused its burdens. Collier, 1934-NMSC-030 at ¶ 38. There is no reason why this rationale should not extend to a subrogation action between two insurers.

In fact, the Collier Court's rationale has been applied consistently by courts in Illinois, and that same rationale has been extended to subrogation cases brought by one insurer against another. See Aetna Cas. & Surety Co. v. Coronet Ins. Co., 358 N.E. 2d 914 (Ill.App. 1976); Cas. Ins. Co. v. Northbrook Prop. & Cas. Ins. Co., 501 N.E. 2d 812 (Ill.App. 1986); Aetna Cas. & Surety Co. v. Prestige Cas. Co., 553 N.E.2d 39 (Ill.App. 1990). In each of these cases, it was held that the breaching insurer was estopped from raising policy defenses against the non-breaching insurer in a subrogation action. Coronet Ins. Co., 358 N.E. at 917; Northbrook Prop. & Cas. Ins. Co., 501 N.E. 2d at 816; Prestige Ca. Co., 553 N.E. 2d at 42.

The Illinois Court of Appeals' opinion in Coronet Ins. Co. is instructive. The insured in Coronet Ins. Co., John Hogie ("Hogie"), was involved in an automobile accident and he was sued by an injured passenger. 358 N.E. at 915. Coronet Insurance Company ("Coronet") refused to defend Hogie on the ground that he did not have the owner's permission to use the automobile. Id. at 916. Hogie's other insurer, Aetna, did defend the suit, however, and settled it on his behalf. Id. After the settlement, Aetna brought a subrogation action against Coronet. Id. The trial court held that Coronet breached its duty to defend, and that it was therefore estopped from asserting policy defenses. Id. at 917.

On appeal, Coronet argued that it was error for the trial court to rule that it was estopped from raising policy defenses. Coronet argued that, because Aetna had defended and settled the case, Hogie was not prejudiced by Coronet's failure to defend him. Id. The court responded to this argument at pages 917-18 of its opinion:

> Although the argument has superficial appeal, we reject the argument. Estoppel arises as a direct result of the insurer's breach of contract. (*Sims v. Illinois Nat. Cas. Co. of Springfield*, 43 Ill.App.2d 184, 193 N.E.2d 123, *Kinnan v. Charles B. Hurst Co.*, 317 Ill. 251, 148 N.E.12.) As the court stated in *Sims*:
>
> '(T)he insurer has no right to insist that the insured be bound by the provisions of the insurance contract inuring to its benefit, *i.e.* the 'Exclusions' provisions, when it has already breached the contract by violating the provisions inuring to the benefit of the insured, *i.e.* the defense provisions.' (43 Ill.App.2d at 197, 193 N.E.2d at 129).
>
> The contract becomes no less breached because of the fortuitous existence of another insurer who is willing to meet its own obligations.

> The thrust of Illinois law places a burden upon the primary insurer rather than the insured or any other party, to fulfill its duty to defend and to take any action necessary to preserve its exclusionary defenses. The law also provides simple procedures which are available to the primary insurer in which case it can assert its defenses. In the case at bar, to hold that Coronet is not estopped would, in effect, shift that burden to Aetna and would require us to find that, in these circumstances, Coronet's duty to defend is no broader than its duty to pay. Since Coronet's refusal to defend is no less unjustified because Aetna defended Hogie, Coronet is estopped from raising any exclusionary coverage defenses.

The Coronet Ins. Co. case demonstrates that the New Mexico Supreme Court's rationale in Collier logically extends to subrogation cases between two insurers. As in Collier, the holding in Coronet Ins. Co. was based on the rationale that the breaching insurer cannot claim the benefits of its contract after having refused its burdens. Collier, 1934-NMSC-030 at ¶ 38; Coronet Ins. Co., 358 N.E.2d at 917. Whether the case is one of the insured versus insurer, or insurer versus insurer, makes no difference because the rule precluding reliance on policy defenses is focused on the conduct of the breaching insurer – not on the insured or any other party. See id.

Furthermore, New Mexico law, like the law of Illinois, provides simple procedures that Ohio Security could have utilized in order to preserve and assert its policy defenses. Ohio Security could have intervened in the underlying action prior to its conclusion and sought a declaratory judgment on coverage. See e.g. Mullenix, 1982-NMSC-038, ¶¶ 11-12. However, because it chose, instead, to sit on the

sidelines and see how things turned out with Nautilus defending, it cannot be heard to complain when its policy defenses are unavailable. See Coronet Ins. Co., 358 N.E. 2d at 917 (noting that where there is a potential for coverage, the insurer can adjudicate its exclusionary provisions in a declaratory judgment action, and if it chooses not to do so, it is estopped); see also State Farm Fire & Cas. Co. v. Price, 1984-NMCA-036, ¶¶ 32-22, 101 N.M. 438, 684 P.2d 524 (stating that "[w]hen an insurance company fails to defend after a demand, it suffers serious consequences" and, more specifically, "[w]hen an insurance company unjustifiably fails to defend it becomes liability for a judgment entered against the insured and for any settlement entered into by the insured in good faith"), *overruled on other grounds by* Ellingwood v. N.N. Investors Life Ins. Co., 1991-NMSC-006, ¶ 17; 111 N.M. 301, 805 P.2d 70; Valley Improvement Ass'n., Inc. v. United States Fidelity & Guaranty Corp., 129 F.3d 1108 (10th Cir. 1997) (applying NM law and holding that an insurer may not rely upon policy defenses after having breached its duty to defend); State Farm Fire & Cas. Co. v. Ruiz, 36 F.Supp.2d 1308 (D. N.M. 1999) (memorandum opinion and order) (same).

The district court's ruling on the estoppel issue should be upheld in this case because it would further New Mexico's public policy of encouraging insurers to fulfill their defense obligations in cases where coverage is unclear. See Mullenix, 1982-NMSC-038, ¶¶ 11-12. Moreover, if the doctrine of estoppel is made

unavailable in cases where the insured is defended by only one of two obligated insurers, the breaching insurer would suffer no "serious consequences" whatsoever for its inaction. Meanwhile, the subrogated insurer, which actually fulfilled its obligations, is forced to spend even more money to litigate and recover what it is owed by the breaching insurer. As was true in Collier, Ohio Security should not be able to "set itself free by so simple a device." Collier, 1934-NMSC-030 at ¶ 38.

CONCLUSION

In the beginning, Nautilus, much like Ohio Casualty, had concerns regarding whether the claims asserted by the Lewingers against Norman/Dent were covered under its policy. The Nautilus Policy contained exclusions similar to those found in the Ohio Security Policy. However, unlike Ohio Security, Nautilus correctly recognized that the allegations of the Lewingers' Complaint were too ambiguous to determine whether coverage could be fully and properly disclaimed from the outset. Thus, Nautilus appropriately defended its insured under a full reservation of rights. Ohio Security, however, ignored the Complaint's ambiguities and unjustifiably disclaimed coverage. The district court was correct in ruling that Ohio Security owed a duty to defend, and this Court should uphold its decision.

This Court should also uphold the district court's judgment on the estoppel issue. First and foremost, it is clear that the arguments raised by Appellant on the issue are being raised for the first time on appeal, and that it failed to preserve any

error in the district court regarding estoppel. The district court's judgment should be affirmed on these grounds alone.

Nevertheless, even if Appellant's newly-asserted arguments are considered, it remains clear that New Mexico's insurance and subrogation law warrants affirmance of the district court's judgment. A reversal of the district court's judgment, on the other hand, would serve only to encourage unjustifiable denials of coverage. Accordingly, Nautilus prays that the Court affirm the district court's judgment in its entirety.

REQUEST FOR ORAL ARGUMENT

Pursuant to Rule 12-214, NMRA (2015), Nautilus requests oral argument on this appeal. Oral argument would be helpful to a resolution of this case because of the procedural posture of the case on appeal, as well as the important insurance issues raised herein.

Respectfully submitted,

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CERTIFICATE OF SERVICE

I HEREBY CERTIFY that a true and correct copy of the foregoing pleading was served via United State first class mail on the following this 9th day of April, 2015:

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