# New York Appellate Court Holds Insurer's Failure to Defend Does Not Constitute a "Reasonable Excuse" Required to Overturn Judgment

By: Tony Miscioscia and Timothy A. Carroll
*Insurance Coverage and Bad Faith Alert*
12.4.18

A recent opinion by the New York Supreme Court, Appellate Division (Second Department) highlights the potential risks for an insurer leaving an insured unrepresented while the insurer pursues other parties or insurers who may be primarily responsible for defending the insured. In refusing to overturn a default judgment entered against an insured while its insurer knew that a complaint had been filed but refused to defend, the New York court's decision raises questions about how claims adjusters are to effectively manage new claims to prevent a default judgment being entered against the insured, while at the same time ensuring that the appropriate party or insurance company handles the insured's defense.

In *Kaung Hea Lee v. 354 Management Inc.*, 2018 N.Y. App. Div. LEXIS 7749 (N.Y. App. Div. Nov. 14, 2018) (*354 Management*) the underlying plaintiffs obtained a default judgment against the defendant insured due to its failure to answer the plaintiffs' complaint. The plaintiffs then moved to determine the extent of damages to which they were entitled by virtue of the default judgment. The defendant opposed that motion, relying on an affidavit from a senior liability claims adjuster employed by the defendant's insurer. "In the affidavit, the claim adjuster stated that she did not assign an attorney to answer the complaint because the codefendant . . . was contractually obligated to defend and indemnify the defendant [insured], and she had been attempting to have either [the codefendant] or its insurer provide an attorney" for the defendant. However, it was determined that the claims adjuster knew about the plaintiffs' complaint two weeks **after** the plaintiffs served it on the defendant and months **before** the plaintiffs moved for default judgment. Despite this knowledge, the defendant's insurer did not provide a defense or, apparently, obtain an extension of time to respond to the complaint, which led to the default judgment.

Apparently persuaded by the adjuster's affidavit, the trial court vacated the plaintiffs' default judgment (finding the defendant's default was excusable), and the plaintiffs appealed. On appeal, the Appellate Division reversed, observing that "the defendant's insurance carrier knowingly permitted the default to occur while it negotiated with another party as to who had the duty to defend." Doing so, the Appellate Division held, "did not constitute a reasonable excuse for failing to answer the complaint." In reaching its holding, the Appellate Division observed that, under New York law, "[t]o vacate an order on the ground of excusable default . . . a defendant is required to demonstrate both a reasonable excuse for its default and the existence of a potentially meritorious defense to the action." The defendant's insurance company's efforts to negotiate with another insurance company – about which company was to assign defense counsel – was not a sufficient excuse, and thus did not satisfy the standard for vacating a default judgment.

The ruling in *354 Management* poses a warning to claims adjusters in a scenario routinely encountered: what to do when you believe another party or insurer is liable for all or part of the insured's defense? The *354 Management* case holds that negotiating the insured's defense arrangement with the other insurer is not a "reasonable excuse" for failing to respond to a complaint. This is not to say that in every scenario an insurer must immediately assign defense counsel while negotiating with another insurer to take over the insured's defense, since the claims against the insured may not be covered. If risk transfer, contractual defense, and/or additional insured rights may exist, it may be sufficient to obtain an extension of time to respond until such time as the insurer can determine whether someone else will provide the insured a defense. But if obtaining an extension is not possible, allowing a default against the insured may invite adverse consequences for both the insured and the insurer.

If you have any questions about this case or its potential relevance to any claims that you are handling, please contact Tony Miscioscia (miscioscia t@whtieandwilliams.com; 215-864-6356) or another member of the Insurance and Bad Faith group.

This correspondence should not be construed as legal advice or legal opinion on any specific facts or circumstances. The contents are intended for general informational purposes only and you are urged to consult a lawyer concerning your own situation and legal questions.