No. 130242

In the

Supreme Court of Illinois

ZURICH AMERICAN INSURANCE COMPANY, as subrogee of Community College District No. 508 d/b/a/ City Colleges of Chicago and CMO, a Joint Venture,

Plaintiff-Appellee,

v.

INFRASTRUCTURE ENGINEERING, INC.,

Defendant-Appellant.

On Leave to Appeal from the Illinois Appellate Court,
First Judicial District, No. 1-23-0147.
There Heard on Appeal from the Circuit Court of Cook County, Illinois,
County Department, Law Division, No. 16 L 12712.
The Honorable **Patrick Sherlock**, Judge Presiding.

BRIEF OF PLAINTIFF-APPELLEE

PATRICK C. HESS, ARDC No.: 6207073
JENNA L. MAHONEY, ARDC No.: 6318066
NIELSEN, ZEHE & ANTAS, P.C.
55 West Monroe Street
Suite 1800
Chicago, Illinois 60603
(312) 322-9900
phess@nzalaw.com
jmahoney@nzalaw.com

Attorneys for Plaintiff-Appellee
Zurich American Insurance Company

COUNSEL PRESS · (866) 703-9373

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NATURE OF THE CASE

This subrogation action involves water damage to a Malcolm X College building during its construction in 2015. Plaintiff-Appellee Zurich American Insurance Company ("Plaintiff" or "Zurich") issued a "builder's risk" insurance policy for the construction project. Builder's risk insurance is a specialized type of property insurance policy that covers physical damage to a building during its construction.

As such, a construction project requires only one builder's risk policy, which is typically purchased by either the owner or general contractor. For the construction project at issue, the owner and general contractor agreed that the general contractor would obtain the builder's risk insurance policy, and the owner would reimburse the general contractor for the insurance premiums. Although not the situation in this case, it would not be uncommon for the owner to purchase the builder's risk policy.

In this case, the general contractor purchased the builder's risk insurance policy from Zurich. As the party who obtained coverage, the general contractor became the "named" insured under Zurich's policy. The owner was an "additional named" insured under the same policy. As the named insured, the general contractor was responsible, per the policy, for paying the premiums and, in the event of a loss, handling the insurance claim, including the receipt of claim payments.

For purposes of builder's risk insurance, physical damage to a building is referred to as a "loss." Thus, when the subject building sustained physical water damage during its construction in 2015, Zurich paid for that loss pursuant to the terms of its builder's risk policy. Zurich initiated this subrogation action to recover payments made due to the loss (i.e., claim payments).

Here, Zurich seeks to recover its claim payments for the subject loss from Defendant-Appellant Infrastructure Engineering, Inc. ("Defendant" or "IEI"). As subrogee of the project owner, Zurich alleges that IEI breached its contractual duties to the project owner by designing a defective system for managing stormwater resulting in the aforementioned water damage during the 2015 construction process.

At issue on this appeal is whether Zurich has standing to sue IEI. More specifically, at issue is whether Zurich has a claim for contractual subrogation against IEI based on the subrogation clause in Zurich's policy. In the circuit court, IEI moved for summary judgment arguing, *inter alia*, that Zurich was not subrogated to the project owner's contract rights against IEI because the project owner did not participate in handling the insurance claim or receive any claim payments from Zurich and, therefore, did not suffer a "loss." The circuit court entered orders granting IEI's motion for summary judgment and denying Zurich's motion to reconsider. Zurich appealed those orders.

On appeal, the First District reversed the circuit court's summary judgment order in IEI's favor. The First District held that Zurich had a contractual right of subrogation against IEI based on the subrogation clause in Zurich's policy, and the circuit court erred in ruling otherwise. Additionally, the First District held that the right to subrogate may arise from either contract terms or equitable factors, but where the right arises from contract terms, there is no need to apply the equitable factors. IEI did not submit a petition for rehearing to the First District. This Court accepted IEI's timely filed petition for leave to appeal.

ISSUE PRESENTED FOR REVIEW

1. Whether the First District correctly held that Zurich has a contractual right to pursue subrogation against IEI based on Zurich's insurance policy.
2. Whether the First District correctly held that Zurich's claim for contractual subrogation does not depend on Zurich's ability to establish the distinct elements of a claim for equitable subrogation.

JURISDICTIONAL STATEMENT

Respectfully, IEI's jurisdictional statement is incomplete. On October 5, 2022, the circuit court granted summary judgment on behalf of IEI. (C10713-10716 V7). Zurich timely filed its motion to reconsider on November 3, 2022. (C10717-10721 V7). After briefing by the parties, on December 19, 2022, the circuit court denied Zurich's motion to reconsider. (C10888-10889 V7). Zurich timely filed its notice of appeal on January 17, 2023. (C10890-10891 V7).

The First District reversed the circuit court's entry of summary judgment for IEI via an unpublished order released on September 19, 2023. On September 27, 2023, Zurich filed a motion to publish the First District's opinion, which was granted on October 4, 2023. The First District withdrew its Rule 23 unpublished order and issued a published opinion on October 24, 2023. No petition for rehearing was filed.

On November 27, 2023, IEI timely filed its petition for leave to appeal to this Court. On January 24, 2024, this Court allowed IEI's petition for leave to appeal. Based on the foregoing, this Court has jurisdiction over this appeal pursuant to Illinois Supreme Court Rule 315.

STATEMENT OF FACTS

1. Community College District No. 508 d/b/a City Colleges of Chicago ("City Colleges") owns and operates Malcom X College in Chicago. (C78 at ¶ 3).

2. City Colleges resolved to improve the Malcom X College campus with a new academic building. (C79 at ¶¶ 10-12).

3. On April 4, 2013, City Colleges contracted an architecture firm, Moody Nolan, Inc. ("Moody Nolan") to design the new building. (C79 at ¶ 13; C102-211).

4. Under their contract, Moody Nolan agreed to design the entire project, including the preparation of all necessary plans and specifications. (C110, C142-155).

5. However, their contract expressly allowed Moody Nolan to subcontract engineering consultants to perform some of the design work, subject to certain conditions. (C118-120).

6. City Colleges' contract with Moody Nolan did not include a provision that waived any claims against Moody Nolan or IEI for damages covered by property insurance for the building. (C102-211). Moody Nolan did not bargain for such a waiver of subrogation. (C102-211).

7. Moody Nolan subcontracted assorted engineering firms to perform some of the design work on the project. (C682-684 at ¶¶19, 24, 29).

8. Relevant to this appeal, Moody Nolan subcontracted IEI to design a system for capturing and temporarily storing rain (i.e., stormwater) before gradually releasing it into the Chicago sewer system. (C682 at ¶¶ 19-20; C10244-10245 V7 at pp. 32-34). Such systems are called stormwater management systems. (C10245 V7 at pp. 33-36).

9. Pursuant to the subcontract between Moody Nolan and IEI, IEI agreed to design the stormwater management system, including the preparation of all necessary plans and specifications. (C212-234; C10244-10245 V7 at pp. 32-34).

10. Moody Nolan's subcontract with IEI did not include a provision that waived any claims against IEI for damages covered by property insurance for the building. (C212-235). IEI did not bargain for such a waiver of subrogation. (C212-235).

11. On January 8, 2014, City Colleges contracted CMO, A Joint Venture ("CMO") to serve as the general contractor responsible for constructing the Malcolm X College building, including its stormwater management system. (C86 at ¶¶ 62-63; C10339-10571 V7).

12. Their construction contract provided that a builder's risk policy[1] should be obtained to protect City Colleges and CMO's interests in the building during its construction:

> The Contractor [CMO] shall purchase and maintain, in a company or companies authorized to do business in the jurisdiction in which the Project is located, property insurance written on a builder's risk "all-risk" or equivalent policy form in the amount of the initial Contract Sum, plus value of subsequent Contract Modifications and costs of materials supplied or installed by others, comprising total value for the entire Project on a replacement cost basis without optional deductibles. Such property insurance shall be maintained . . . until final payment has been made . . . or until no person or entity other than the Owner [City Colleges] has an insurable interest in the property required by this Section 11.3 to be covered, whichever is later. This insurance shall include the interests of the Owner [City Colleges], the Contractor [CMO], Subcontractors and Sub-subcontractors in the Project.

(C10388-10389 V7 at §§11.3.1, 11.3.1.1).

[1] A builder's risk policy is first-party property insurance that provides coverage for a building under construction before it becomes insurable as a completed structure. 5 New Appleman on Insurance Law Library Edition § 50.01 (2023). It pays for necessary repairs if the building is physically damaged during construction. *Id*.

13. City Colleges agreed to reimburse CMO for the builder's risk insurance policy premiums. (C10342 V7 § 5.1; C 10346 V7 at § 7.6.1).

14. CMO fulfilled its obligation to obtain the builder's risk policy for the benefit of City Colleges, CMO and others. (C526-569; C10629-10630 V7 at pp. 44-45).

15. CMO purchased a builder's risk policy from Zurich, identified under policy number IM 5420384-00 (the "policy" or "Zurich's policy"). (C526-569).

16. CMO was named an insured on the first page of Zurich's builder's risk policy. (C526).

17. Zurich's policy imposed certain administrative duties on CMO as the first named insured:

> The first Named Insured shown in A. above shall be deemed the sole and irrevocable agent of each and every Insured hereunder for the purpose of giving and receiving notices to/from [Zurich], giving instruction to or agreeing with [Zurich] as respects Policy alteration, for making or receiving payments of premium or adjustments to premium, and as respects the payment for claims.

(C530 at §3).

18. Zurich's policy defined "Additional Named Insured" to mean:

> All owners, all contractors and subcontractors of every tier, and tenants at the project location, except as named in A. above, as required by any contract, subcontract or oral agreement for the INSURED PROJECT*, and then only as their respective interests may appear are recognized as Additional Named Insureds hereunder. As respects architects, engineers, manufacturers and suppliers, their interest is limited to their site activities only.

(C530 at §3B; C10388-10389 V7 at §§11.3.1, 11.3.1.1).

19. Zurich's builder's risk policy provided coverage for "all risks of direct physical loss of or damage to" the Malcolm X College building during its construction. (C530 at §5; C534 at §§1A and 2; C545 at §8).

20. The builder's risk policy granted Zurich subrogation rights to the extent of its claim payments:

> If the Company [Zurich] pays a claim under this Policy, they will be subrogated, to the extent of such payment, to all the Insured's rights of recovery from other persons, organizations and entities.
>
> * * *
>
> It is a condition of this Policy that the Company shall be subrogated to all the Insured's unwaived rights of recovery, if any, against any third party Architect or Engineer, whether named as an Insured or not, for any loss or damage arising out of the performance of professional services in their capacity as such and caused by any error, omission, deficiency or act of the third party Architect or Engineer, by any person employed by them or by any others for whose acts they are legally liable.

(C548-549 at §12).

21. During construction, the subject building sustained physical damage when the basement flooded during a rainstorm. (C86-87 at ¶¶ 66-68, 72).

22. Much of the physical damage was to the building's electrical and mechanical systems and related equipment. (C86-87 at ¶¶ 66-68, 72).

23. In the wake of the flooding incident, CMO fulfilled its administerial obligations as the first named insured on the builder's risk policy. (C530 at §3).

24. CMO submitted to Zurich a claim for building damage resulting from that incident. (C530 at §3; C10624 V7 at p. 24; C10627 V7 at pp. 33-36; C10633 V7 at p. 58).

25. CMO subsequently communicated with Zurich and submitted documents in support of the claimed loss, including estimates and invoices for the necessary building repairs. (C10627 V7 at pp. 36; C10636 V7 at p. 72; C10662 V7 at p. 176).

26. Zurich determined that the physical damage to the building was a covered loss. (C10630-10631 V7 at pp. 48-49; C10641 V7 at p. 92).

27. After applying the $50,000.00 policy deductible, Zurich issued claim payments totaling $2,998,929.35 to cover the cost of necessary building repairs. (C530 at §3; C10664 V7 at 183:23-184:7).

28. CMO received those claim payments in accordance with its administrative duties as the first named insured on the policy. (C530 at §3; C533 at §11; C10664 V7 at p. 184).

PROCEDURAL HISTORY

I. Circuit Court Proceedings.

On December 29, 2016, Zurich initiated this contractual subrogation action as subrogee of its insureds, CMO and City Colleges, to recover its claim payments from IEI and others. (C76-569). With respect to Zurich's breach of contract claim against IEI, Zurich claims that IEI breached its subcontract with Moody Nolan by providing a defective design for the stormwater management system. (C91-93). Zurich alleges that City Colleges was a third-party beneficiary of that subcontract. (C80-81) Zurich further claims that the basement flooded as a result of IEI's breach, resulting in physical damage to the building and related equipment. (C91-93).

IEI twice moved for summary judgment on Zurich's contract action. IEI filed its first such motion on February 14, 2020, arguing that IEI did not have any contractual duty to City Colleges to protect the subject building from water damage while the storm water detention system was still under construction. (C1377-1385). IEI claimed that because CMO controlled the means and methods of construction, it would be improper to hold IEI liable for incomplete work. (C1384). The circuit court disagreed, holding that IEI assumed its contractual duty to City Colleges in April of 2013 when it entered into the subcontract

with Moody Nolan. (C6469-6477 V5). The circuit court denied IEI's motion and found that questions existed whether IEI breached its contractual duty to City Colleges when it provided its revised stormwater management system design. (C6477 V5).

On July 20, 2022, IEI again moved for summary judgment on Zurich's contract action, arguing, *inter alia*, that Zurich was not subrogated to City Colleges' contract rights against IEI because City Colleges did not participate in handling the insurance claim or receive any claim payments from Zurich, and, therefore, did not suffer a "loss." (C9085-9096 V6). The circuit court heard oral arguments on September 27, 2022 and subsequently directed the parties to provide supplemental briefs on the issue of whether an insurer that names more than one insured on its policy and makes claim payments to only one named insured may pursue recovery as subrogee of a different named insured. (C10697 V7; C10075 V7). As ordered, the parties submitted supplemental briefs on September 29, 2022. (C10698-10700 V7; C10703-10710 V7).

The circuit court issued an order granting IEI's motion for summary judgment on October 5, 2022, holding that Zurich did not have a right to pursue any recovery as subrogee of City Colleges. (C10713-10716 V7). The circuit court reasoned that Zurich could not proceed as City Colleges' subrogee unless Zurich could prove three elements: "(1) a third party must be primarily liable to the insured for the loss; (2) the insurer must be secondarily liable to the insured for the loss under an insurance policy; and (3) the insurer must have paid the insured under the policy, thereby extinguishing the debt of the third party." (C10715 V7). The circuit court found that Zurich failed to establish the second and third elements because City Colleges "simply sustained no loss and was not paid by the insurer; two requirements for there to be subrogation." (C10716 V7).

On November 3, 2022, Zurich filed a motion to reconsider. (C10717-10721 V7). Zurich noted that the circuit court failed to consider the subrogation provision in the builder's risk policy when determining Zurich's subrogation rights. (C10718-10719 V7 at ¶¶ 3, 5-6). After briefing by the parties, the circuit court denied Zurich's motion to reconsider on December 19, 2022. (C10888-10889 V7). The circuit court relied primarily on *Econ. Premiere Assurance Co. v. Country Mut. Ins. Co.*, 2021 IL App (1st) 19264-U, ¶ 65 and refused to evaluate Zurich's subrogation rights under the policy. (C10888-10889 V7).

II. First District Appellate Proceedings.

Zurich timely filed its notice of appeal on January 17, 2023. (C10890-10891 V7). The First District unanimously reversed the circuit court's summary judgment order via an unpublished order released on September 19, 2023. The First District withdrew its Rule 23 unpublished order and issued a published opinion on October 24, 2023. *Zurich Am. Ins. Co. v. Infrastructure Engineering, Inc.*, 2023 IL App (1st) 230147.

The First District held that Zurich had a contractual right of subrogation against IEI based on Zurich's policy, and that the circuit court erred in ruling otherwise. *Id.* at ¶¶ 39, 45. The First District noted that "the proper focus in this case is whether Zurich is entitled to subrogate based on the express terms of the builder's risk policy it issued." *Id.* at ¶ 34. The First District further reasoned that the subrogation term in the builder's risk policy defined Zurich's "right to subrogation and the scope of that right." *Id.* at ¶ 39. Based on the unambiguous language of the policy, the First District concluded that Zurich established its right to subrogate on behalf of City Colleges. *Id.* at ¶ 45.

Additionally, the First District held that where the right to subrogate arises from unambiguous contract terms, there is no need to consider whether such right arises from equitable factors because "the existence of the unambiguous subrogation contract provision bars the application of the common law doctrine." *Id.* at ¶¶ 32-33 (citing *Schultz v. Gotlund*, 138 Ill. 2d 171 (1990)).

STANDARD OF REVIEW

The circuit court's entry of summary judgment is subject to *de novo* review. *Outboard Marine Corp. v. Liberty Mut. Ins. Co.*, 154 Ill. 2d 90, 102 (1992). The construction of an insurance policy, which is a question of law, is also reviewed *de novo*. *American States Ins. Co. v. Koloms*, 177 Ill. 2d 473, 479-80 (1997).

ARGUMENT

I. The First District correctly ruled that Zurich has an enforceable claim for contractual subrogation against IEI based on Zurich's insurance policy.

A. Subrogation rests on the sound principle that ultimate responsibility should fall on the party responsible for the loss.

Subrogation rights originated in common law. *Dix Mut. Ins. Co. v. LaFramboise*, 149 Ill. 2d 314, 319 (1992).

> The right of subrogation is an equitable right and remedy which rests on the principle that substantial justice should be attained by placing ultimate responsibility for the loss upon the one against whom in good conscience it ought to fall.

Id. (citing 34 Ill. L. & Prac. Subrogation § 2 (1958)). When put into the insurance context, subrogation is "[t]he principle under which an insurer that has paid a loss under an insurance policy is entitled to all the rights and remedies belonging to the insured against a third party with respect to any loss covered by the policy." *Sheckler v. Auto-Owners Ins. Co*., 2022 IL 128012, ¶ 39 (quoting Black's Law Dictionary 1726 (11th ed. 2019)).

Subrogation rights may be created by common law, contract, or statute. *Trogub v. Robinson*, 366 Ill. App. 3d 838, 842 (1st Dist. 2006). Equitable subrogation is a creature of common law that is utilized to prevent unjust enrichment. *Dix*, 149 Ill. 2d at 319. "There is no general rule that can be laid down to determine whether a right of equitable subrogation exists, since the right depends upon the equities of each particular case." *Id*. Conventional subrogation, on the other hand, arises from an agreement between the parties. *AAMES Capital Corp. v. Interstate Bank*, 315 Ill. App. 3d 700, 706 (2d Dist. 2000). Fittingly, conventional subrogation is also referred to as contractual subrogation. *See Schultz*, 138 Ill. 2d at 173.

B. The subrogation clause in Zurich's policy should be enforced as written.

Zurich's policy provided Zurich the right to subrogate to the extent of its payment:

> If [Zurich] pays a claim under this Policy, they will be subrogated, to the extent of such payment, to all the Insured's rights of recovery from other persons, organizations and entities.
>
> * * *
>
> It is a condition of this Policy that the Company shall be subrogated to all the Insured's unwaived rights of recovery, if any, against any third party Architect or Engineer, whether named as an Insured or not, for any loss or damage arising out of the performance of professional services in their capacity as such and caused by any error, omission, deficiency or act of the third party Architect or Engineer, by any person employed by them or by any others for whose acts they are legally liable.
>
> (C548-549 at §12).

Where the right to subrogation is created by an enforceable subrogation clause in an insurance policy, the contract terms, rather than common-law principles control. *American Fam. Mut. Ins. Co. v. Plunkett*, 2014 IL App (1st) 131631, ¶ 36. *See also, James River Ins. Co. v. Canal Ins. Co.*, 534 F. Supp. 3d 962, 968-969 (N.D. Ill. 2021) (collecting

cases and noting that where there is a subrogation clause in the insurance policy, "the Court need not take into account elements of equitable subrogation"). "In fact, the existence of the unambiguous subrogation contract provision bars the application of the common law doctrine." *Zurich Am. Ins. Co.*, 2023 IL App (1st) 230147 at ¶ 33. *Compare Dix*, 149 Ill. 2d at 319 (discussing whether "it would be inequitable" to enforce a policy's subrogation if doing so would conflict with an implied term in a landlord-tenant agreement).

For example, in *American Family Mut. Ins. Co. v. Northern Heritage Builders, L.L.C.*, 404 Ill. App. 3d 584, 585-586 (1st Dist. 2010), a property insurer paid for necessary repairs when its' insured's home sustained water damage. To recover those claim payments, the insurer sued the home builders under various theories including equitable subrogation. *Id.* The circuit court dismissed the claim for equitable subrogation because the insurance contract included a subrogation clause. *Id.* at 587-588. That ruling was appealed. *Id.* at 587.

In affirming the circuit court's decision, the appellate court held that "where the right of an insurer to subrogation is expressly provided for in the policy, its right must be measured by, and depend solely on, the terms of such provisions." *Id.* at 588 (quoting 16 Couch on Insurance Law § 222:23, at 222-51 (3rd ed. 2000)). Under this well-established Illinois law, the subrogation clause in Zurich's policy "must be enforced as written." *Trogub*, 366 Ill. App. 3d at 842.[2]

Moreover, the preeminence of express subrogation terms over inconsistent implied or common-law terms is firmly rooted in Illinois contract law. *Chubb Ins. Co. v.*

[2] IEI argues that Zurich "forfeited" any argument that it has a right to subrogation based on the express terms in the builder's risk policy. (IEI Brf., p. 26). The First District correctly rejected that argument because Zurich has repeatedly asserted that its right to subrogation arises from and is controlled by the terms of its policy. *Zurich Am. Ins. Co.*, 2023 IL App (1st) 230147 ¶¶19-27; (C10095 V7; C10097-98 V7; C10698-10700 V7; R18).

DeChambre, 349 Ill. App. 3d 56, 67 (1st Dist. 2004) ("[t]he laws and public policy of the State of Illinois permit freedom of contracting between competent parties"); *Resolution Trust Corp. v. Holtzman*, 248 Ill. App. 3d 105, 111 (1st Dist. 1993) ("[t]he rules of contract provide that the parties to a contract are presumed to have intended what their language clearly imports so that a trial court has no discretion to require parties to accept any terms other than those in their contract"); *Foster Enterprises, Inc. v. Germania Federal Sav. & Loan Asso.*, 97 Ill. App. 3d 22, 31 (3d Dist. 1981) ("contract terms implied in law cannot supplant express contract terms").

C. Based on the subrogation clause in Zurich's policy, Zurich is subrogated to the recovery rights of City Colleges and CMO.

An insurance policy must be construed as a whole, giving policy words their plain, ordinary, and popular meaning, at the same time striving to fulfill the intent of the parties. *United States Fire Ins. Co. v. Hartford Ins. Co.*, 312 Ill. App. 3d 153, 155 (1st Dist. 2000). "An insurance policy is not intended to be interpreted in a factual vacuum without regard to the purpose for which the insurance policy was written." *Pekin Ins. Co. v. Pulte Home Corp.*, 404 Ill. App. 3d 336, 343 (1st Dist. 2010). To ascertain the intent of the parties and the meaning of the words used in the insurance policy, the court must construe the policy as a whole and the circumstances surrounding its issuance, such as the type of insurance purchased, the nature of the risks involved, relationship situation of the parties, and the purpose for which the policy was obtained. *Id. See also*, *Crum & Forster Managers Corp. v. Resolution Trust Corp.*, 156 Ill. 2d 384, 391 (1993); *Outboard Marine Corp.*, 154 Ill. 2d at 108-9.

i. City Colleges and CMO intended to protect their insurable interests in the construction project with a builder's risk policy.

A person has an "insurable interest" in property if it would stand to gain some advantage or profit by its continued existence, or if he would stand to suffer some loss or disadvantage by its destruction. 5 New Appleman on Insurance Law Library Edition § 41.05 (2023). "The general rule in construction cases is that both the owner and the contractor have insurable interests in the property until the construction is complete." *Intergovernmental Risk Mgmt. ex rel. Vill. Of Bartlett v. O'Donnell, Wicklund, Pigozzi & Peterson Architects*, 295 Ill. App. 3d 784, 790-791 (1st Dist. 1998); *see also Builder's Risk Insurance Policies*, 94 A.L.R.2d 221, 2 (property owner who has made an agreement with a contractor for the construction of a building has an insurable interest in the building during the progress of construction). Consequently, in the case at bar, both the project owner City Colleges and the general contractor CMO had an insurable interest in the subject building during its construction.

A builder's risk policy is a type of first-party property insurance. 5 James P. Bobotek and Stephen S. Asay, New Appleman on Insurance Law Library Edition § 50.01 (2009); *Rosemont v. Lentin Lumber Co.*, 144 Ill. App. 3d 651, 664 (1st Dist. 1986). It provides coverage for a building under construction before it becomes insurable as a completed structure. *Id*. If the building is physically damaged during construction, the builder's risk policy pays for the necessary repairs. *Id*. Essentially, builder's risk coverage shifts the risk of repair costs to the first-party property insurer "to facilitate timely completion of the project and avoid the prospect of time-consuming and expensive litigation, regardless of which party is at fault." *Empress Casino Joliet Corp. v. W.E. O'Neil Constr. Co.*, 2016 IL App (1st) 151166, ¶ 71.

Here, the construction contract makes clear that City Colleges and CMO intended to protect their insurable interests in the construction project with a builder's risk policy. They agreed that CMO would purchase property insurance for the building under construction and that City Colleges would reimburse CMO for the premiums. (C10342 V7 § 5.1; C 10346 V7 at § 7.6.1; C10388-10389 V7 at §§11.3.1, 11.3.1.1). They could have agreed just as easily that City Colleges would obtain the policy. They agreed it would be "property insurance written on a builder's risk "all-risk" or equivalent policy form." (C10388-10389 V7 at §§11.3.1, 11.3.1.1). City Colleges and CMO agreed that the builder's risk coverage would be maintained until final payment was made "or until no person or entity other than the Owner [City Colleges] has an insurable interest in the property," whichever was later. (C10388-10389 V7 at §§11.3.1). They agreed that the builder's risk policy would "include the interests of the Owner, the Contractor, Subcontractors and Sub-subcontractors in the Project." *Id.* City Colleges' and CMO's mutual interest in builder's risk coverage should be considered in deciding whether both were an "Insured" within the meaning of the policy's subrogation clause. *See Crum & Forster*, 156 Ill. 2d at 391 (when interpreting an insurance policy, the circumstances surrounding its issuance must be considered).

ii. City Colleges and CMO are both named insureds on Zurich's policy.

In the instant case, Zurich's builder's risk policy named more than one insured, which is to be expected given that more than one party had an insurable interest in the Malcolm X College building during its construction. *See*, *e.g.*, *Intergovernmental Risk Mgmt.*, 295 Ill. App. 3d at 790-791 (both the owner and the contractor have insurable interests in a building under construction). CMO purchased the policy and is named as an

insured on its first page. (C526-569; C530 at §3). The policy defined "Additional Named Insured" to include all project owners "as required by any contract, subcontract or oral agreement." (C530 at §3B; C10388-10389 V7 at §§11.3.1, 11.3.1.1). Accordingly, City Colleges is an Additional Named Insured on Zurich's policy because the construction contract required the builder's risk policy to protect City Colleges' insurable interest in the building under construction. (C10388-10389 V7 at §§11.3.1, 11.3.1.1). Stated differently, Zurich's policy names both CMO and City Colleges as insureds.

Notably, the same would be true if City Colleges had purchased the policy and been named an insured on the first page. The policy defines "Additional Named Insured" to include all contractors "as required by any contract, subcontract or oral agreement." (C530 at §3B; C10388-10389 V7 at §§11.3.1, 11.3.1.1). Thus, if City Colleges had purchased the policy, CMO would have been an Additional Named Insured because the construction contract also required the builder's risk policy to protect CMO's insurable interest in the building. (C10388-10389 V7 at §§11.3.1, 11.3.1.1). Regardless of which entity purchased Zurich's policy, the policy would name both City Colleges and CMO as insureds.

iii. The subrogation clause in Zurich's policy does not limit Zurich's subrogation rights to the first named insured's recovery rights.

"[A]n 'insured' in a policy is not limited to the named insured but includes anyone insured under the policy." *Chubb Ins. Co.*, 349 Ill. App. 3d at 64. *See also*, *James McHugh Construction Co. v. Zurich American Insurance Co.*, 401 Ill. App. 3d 127, 132-33 (1st Dist. 2010) (interpreting the term "the insured" to include both the named insured and any additional insured qualifying for coverage under the policy). Where the terms of an insurance policy are plain and unambiguous, the court will afford them their plain, ordinary

meaning and apply them as written. *Crum & Forster*, 156 Ill. 2d at 391. "The court will not search for ambiguity where there is none." *Id*.

Here, the subrogation clause in Zurich's policy draws no distinction between types of insured. (C548-549 at §12). The clause clearly *does not* say that Zurich is only subrogated to the recovery rights of the first named insured or that Zurich is not subrogated to the recovery rights of an additional named insured. Likewise, none of the other policy terms indicate any intention to limit Zurich's subrogation rights to the first named insured's recovery rights. Therefore, based on the plain language of the subrogation clause, "Insured" must mean the first named insured and any of the additional named insureds. "Insured" means insured and applies to all the insureds. There is no language in the policy mandating or even suggesting that the term "Insured" be construed in anything other than its plain, ordinary meaning. *James McHugh Construction*, 401 Ill. App. 3d at 132-33 ("the insured" means all insureds under the policy); *accord Chubb Ins. Co.*, 349 Ill. App. 3d at 64. As such, based on the policy's unambiguous language, Zurich is subrogated, to the extent of its payment, to the recovery rights of City Colleges and CMO.

This interpretation finds additional support in the type of policy involved and other circumstances surrounding its issuance. *See Crum & Forster*, 156 Ill. 2d at 391. As owner and contractor, City Colleges and CMO both had an insurable interest in the Malcolm X College Building during its construction. *Intergovernmental Risk Mgmt.*, 295 Ill. App. 3d at 790-791. Both stood to gain some advantage or profit from that building's continued existence, and they both stood to suffer some loss or disadvantage from its damage or destruction. City Colleges and CMO agreed to protect their simultaneous interests with one property insurance policy, specifically a builder's risk policy that afforded first-party

coverage for the building under construction. (C10388-10389 V7 at §§11.3.1, 11.3.1.1). They decided that CMO would obtain the insurance and that City Colleges would reimburse CMO for the premiums, which made CMO the first named insured and City Colleges an additional named insured under Zurich's policy. (C530 at §3; C10342 V7 § 5.1; C10346 V7 at § 7.6.1; C10388-10389 V7 at §§11.3.1, 11.3.1.1). When the building was damaged during construction, they both benefitted from having property insurance that paid nearly $3,000,000.00 for the necessary repairs. (C526-569; C10664 V7 at 183:23-184:7).

All those circumstances make clear that Zurich's policy was designed, intended, purchased, and maintained to protect both City Colleges and CMO, which it did. None of those circumstances even remotely suggest any intention to limit Zurich's subrogation rights to CMO's recovery rights as the first named insured. Based on the plain language of Zurich's policy and the circumstances surrounding its issuance, Zurich is subrogated to both City Colleges and CMO. *Trogub*, 366 Ill. App. 3d at 842. Most salient here, Zurich is subrogated to City Colleges' recovery rights against IEI. *Id*. Consequently, the First District followed Illinois law by deciding that Zurich is subrogated to City Colleges' recovery rights against IEI based on the subrogation term in Zurich's policy. *Zurich Am. Ins. Co.*, 2023 IL App (1st) 230147 at ¶ 39.

II. The First District correctly ruled that Zurich's claim for contractual subrogation does not depend on Zurich's ability to establish the distinct elements of a claim for equitable subrogation.

A. Contractual subrogation and equitable subrogation are separate and distinct causes of action.

Contractual subrogation arises from an agreement between the parties. *AAMES Capital Corp.*, 315 Ill. App. 3d at 706. Therefore, the existence and scope of a right to

contractual subrogation depends entirely on contract law, as discussed at length in Argument I, *supra*.

Equitable subrogation arises from common law. *Dix*, 149 Ill. 2d at 319. "There is no general rule that can be laid down to determine whether a right of equitable subrogation exists, since the right depends upon the equities of each particular case." *Id*. *See also, AAMES Capital Corp.*, 315 Ill. App. 3d at 706 (recognizing the elusiveness of equitable subrogation in Illinois case law).

B. *Home Ins. Co. v. Cincinnati Ins. Co.*

This Court addressed the right of equitable subrogation in *Home Ins. Co. v. Cincinnati Ins. Co.*, 213 Ill. 2d 307, 310 (2004), which involved a dispute between two liability carriers. One carrier paid to settle an underlying claim and then sued the other on a theory of equitable subrogation to recover those payments. *Id*. In analyzing the second carrier's liability, this Court set forth three elements of an equitable subrogation claim:

> the elements of an equitable subrogation claim [are] as follows: (1) the defendant carrier must be primarily liable to the insured for a loss under a policy of insurance; (2) the plaintiff carrier must be secondarily liable to the insured for the *same loss* under its policy; and (3) the plaintiff carrier must have discharged its liability to the insured and at the same time extinguished the liability of the defendant carrier.

Id. at 323. Contractual subrogation was not at issue in *Home Ins. Co.*, and this Court did not discuss or even refer to that subject.

C. The cases relied upon by IEI are both legally and factually distinguishable.

In *dicta*, some appellate court decisions after *Home Ins. Co.* have confused the distinction between contractual and equitable subrogation. These cases merit close analysis because IEI's appeal relies on them almost exclusively.

i. *SwedishAmerican*

In *SwedishAmerican Hosp. Ass'n v. Ill. State Med. Inter-Insurance Exchange*, 395 Ill. App. 3d 80 (2d Dist. 2009), the appellate court addressed the right of equitable subrogation in a case with the same basic fact pattern as *Home Ins. Co.* One liability carrier paid to settle an underlying claim and then sought to recover those payments from another liability carrier in a claim for equitable subrogation. *Id.* at 83-85, 97. In analyzing the second carrier's liability, the appellate court cited *Home Ins. Co.* for the elements of a common-law action for equitable subrogation. *Id.* at 105. However, the appellate court restated those elements as follows:

> A claim for equitable **or contractual** subrogation requires the following elements: (1) the defendant carrier must be primarily liable to the insured for a loss under an insurance policy; (2) the plaintiff carrier must be secondarily liable to the insured for the same loss under its policy; and (3) the plaintiff carrier must have discharged its liability to the insured and at the same time extinguished the liability of the defendant carrier.

Id. at 105 (emphasis added). Contractual subrogation was not at issue in *SwedishAmerican*, and the appellate court did not discuss that subject. *Id*. at 105-106. Consequently, it is unclear why the appellate court added "or contractual" in stating the elements of a claim for equitable subrogation.

ii. *Economy Premiere*

In *Economy Premiere Assurance Co.*, 2021 IL App (1st) 192364-U, the appellate court once again addressed the right of equitable subrogation in a case with the same basic fact pattern. One liability carrier paid to settle an underlying claim and then sought to recover its payments from another liability carrier. *Id.* at ¶¶ 16, 64. Just like the plaintiff carriers in *Home Ins. Co.* and *SwedishAmerican*, the plaintiff carrier in *Economy Premiere* made a claim for equitable subrogation. *Id.* at ¶¶ 16, 64. Unlike those other carriers, the

plaintiff carrier in *Economy Premiere* also made a claim for contractual subrogation. *Id.* at ¶¶ 65-66. The appellate court analyzed both subrogation claims without any reference to or discussion of their distinct elements. *Id.* Instead, the appellate court quoted *SwedishAmerican* for the elements of "[a] claim for equitable **or contractual** subrogation." *Id.* at ¶ 65 (emphasis added). Ultimately, the appellate court ruled in favor of the defendant carrier after finding that its policy did not afford coverage for the underlying incident. *Id.*

iii. *Trogub*

In *Trogub*, 366 Ill. App. 3d at 842, the appellate court addressed the right of contractual subrogation. The plaintiffs sustained personal injuries in a minor two-car collision. *Id*. at 839. The plaintiffs' insurer paid the resulting medical bills under its automobile policy that included a subrogation clause. *Id.* at 839. The plaintiffs brought a personal injury action against the at-fault driver, which they settled for $10,000.00. *Id*. at 839-840. The insurer subsequently asserted a claim against the plaintiffs' settlement proceeds based on the subrogation clause contained in its policy. *Id*. The circuit court ruled in favor of the insurer. *Id*.

The plaintiffs made several arguments on appeal as to why the subrogation clause in their insurer's policy should not be enforced. *Id.* at 842-847. Before discussing those arguments individually, the appellate court generally stated:

> In the case of an insurance contract, subrogation rights arise where (1) a third party has caused a loss and is primarily liable to the insured for the loss, (2) the insurer is secondarily liable to the insured due to an insurance policy, and (3) the insurer pays the insured under that policy, thereby extinguishing the debt owed by the third party.

Id. at 842.

The appellate court then proceeded to analyze the enforceability of the subrogation clause based on contract law. *Id.* at 839-844. For example, the plaintiffs argued, in part, that the subrogation clause required their insurer to sue the at-fault driver before acquiring any subrogation rights.[3] *Id*. at 839-840. The appellate court rejected the plaintiffs' argument based on well-established contract law:

> We do not consider the [insurer's] policy to be equivocal, uncertain, or ambiguous; nor do we consider the [plaintiffs'] "inference" to be a reasonable interpretation of the clearly worded policy. A policy term is not ambiguous because the term is not defined within the policy or because the parties can suggest creative possibilities for its meaning.

Id. at 843-844 (internal citations and quotations omitted). Equitable subrogation was not at issue in *Trogub*, and the appellate court did not discuss that subject. *Id*. at 843-844.

iv. The First District correctly distinguished the above-discussed appellate court decisions from the case at bar.

For purposes of determining Zurich's subrogation rights in the case at bar, it is important to note that in *SwedishAmerican*, *Economy Premiere*, and *Trogub*, the appellate court never discussed the distinction between contractual and equitable subrogation.[4] Moreover, in none of those cases did the appellate court express any interest in abandoning the well-settled distinction. *Dix*, 149 Ill. 2d at 319. In *SwedishAmerican* and *Economy*

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[3] The policy provided:

When we make a payment under this coverage, we will be subrogated (to the extent of payment made by us) to the rights of recovery the injured person or anyone receiving the payments may have against any person or organization. Such person will do whatever is necessary to secure our rights and will do nothing to prejudice them. This means we will have the right to sue for or otherwise recover the loss from anyone else who may be held responsible. *Id.* at 840.

[4] The same holds true for two other cases cited by IEI. *See State Farm Mut. Auto. Ins. Co. v. Easterling*, 2014 IL App (1st) 133225; *State Farm Gen. Ins. Co. v. Stewart*, 288 Ill. App. 3d 678, 681 (1st Dist. 1997).

Premiere, the appellate court simply misstated the elements of a claim for equitable subrogation. Meanwhile, in *Trogub*, which involved contractual subrogation, the appellate court stated the elements of a claim for equitable subrogation but correctly determined the insurer's subrogation rights based on contract law. Therefore, the First District correctly distinguished those cases when it determined that "insofar as those cases hold that the three general prerequisites for equitable subrogation control over the express terms of a subrogation clause in a contract, we disagree with their holdings." *Zurich Am. Ins. Co.*, 2023 IL App (1st) 230147 at ¶ 36.

D. IEI relies heavily on *SwedishAmerican*, *Economy Premiere*, and *Trogub*.

IEI relies on *SwedishAmerican*, *Economy Premiere*, and *Trogub* to support its argument that Zurich's rights in this case should not be determined based on the subrogation clause in Zurich's policy. For example, IEI relies on *Trogub* in arguing that Zurich's subrogation rights depend on Zurich's ability to establish three elements:

> In the case of an insurance contract, subrogation rights arise where (1) a third party has caused a loss and is primarily liable to the insured for the loss, (2) the insurer is secondarily liable to the insured due to an insurance policy, and (3) the insurer pays the insured under that policy, thereby extinguishing the debt owed by the third party.

(IEI Brf., p. 26) (quoting *Trogub*, 366 Ill. App. 3d *Id*. at 842).

Additionally, IEI argues that Zurich did not establish that third element ("the insurer pays the insured") because Zurich issued its claim payments to the general contractor CMO, rather than the project owner City Colleges. (IEI Brf., pp. 17-18). More broadly, IEI argues that CMO sustained a "loss" and City Colleges did not because CMO bought the

builder's risk policy and handled the insurance claim. (IEI Brf., Argument III). Although IEI's Brief repeats this argument many times,[5] the following is a representative example:

> The fact that CMO was the only party to sustain a loss in connection with the August 17, 2015 flood event is manifest from the submission and handling of the subject claim. The undisputed evidence shows that CMO (not City Colleges) submitted a claim for loss under the Zurich policy; that CMO (not City Colleges) paid the deductible under the Zurich policy; and that CMO (not City Colleges) received 100% of the loss payment from Zurich. (C. 9898 V6, 9944 V6, 9999 V7). The undisputed evidence also shows that City Colleges had no involvement whatsoever in the claim submitted under the Builders Risk Policy; did not make a claim under the Builders Risk Policy; did not correspond with Zurich's claims adjuster regarding the claim; and did not receive any loss payment from Zurich.

(IEI Brf., p. 17).[6]

E. IEI's reliance on *SwedishAmerican*, *Economy Premiere*, and *Trogub* is misplaced.

SwedishAmerican, *Economy Premiere*, and *Trogub* offer zero support for IEI's argument that determining Zurich's subrogation rights should be based on anything other

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[5] IEI's Brief uses the word "loss" 192 times.

[6] For the sake of argument, if the elements of a claim for equitable subrogation were applied here, Zurich would still be subrogated to City Colleges' rights of recovery against IEI. As stated by the appellate court in *Trogub*, the elements of a claim for equitable subrogation are as follows:

> In the case of an insurance contract, subrogation rights arise where (1) a third party has caused a loss and is primarily liable to the insured for the loss, (2) the insurer is secondarily liable to the insured due to an insurance policy, and (3) the insurer pays the insured under that policy, thereby extinguishing the debt owed by the third party.

366 Ill. App. 3d at 842. Here, IEI is a third party that allegedly damaged City Colleges' property. City Colleges could have sued IEI to recover the repairs costs. In that sense, IEI was "primarily liable" to City Colleges. However, City Colleges did not have to sue IEI because City Colleges had property insurance, namely Zurich's builder's risk policy. In that sense, Zurich was "secondarily liable" to City Colleges. Zurich paid the repair costs under its policy, thereby extinguishing IEI's debt to City Colleges.

than Zurich's policy and the circumstances under which it was issued. However, in none of those cases did the appellate court question or even discuss the well-settled distinction between contractual and equitable subrogation. IEI's reliance on those cases is misplaced for the reasons discussed above in Argument II., C., iv. Moreover, IEI's misplaced reliance on those cases has compelled IEI to make some tortured arguments.

i. IEI argues that Zurich's subrogation rights are controlled by contract terms unrelated to subrogation.

The construction contract included a term that required CMO to purchase the builder's risk policy and a term that required City Colleges to reimburse CMO for the policy premiums. (C10342 V7 § 5.1; C 10346 V7 at § 7.6.1; C10388-10389 V7 at §§11.3.1, 11.3.1.1). CMO and City Colleges could have agreed just as easily that City Colleges would purchase the policy. As the first named insured on Zurich's policy, CMO was obliged to administer any insurance claims including the receipt of claim payments.[7] (C530 at §3). None of these contract terms even relate to, let alone limit, Zurich's subrogation rights. None of these terms support disregarding the express subrogation term in Zurich's policy.

Nevertheless, IEI suggests that these unrelated contract terms somehow limit Zurich's subrogation rights. A brief hypothetical demonstrates the absurdity of IEI's proposed interpretation of these contract terms. If City Colleges had purchased the builder's risk policy, then it would have been responsible as the first named insured for

[7] Zurich's policy provides:

The first Named Insured shown in A. above [CMO] shall be deemed the sole and irrevocable agent of each and every Insured hereunder for the purpose of giving and receiving notices to/from the Company [Zurich], giving instruction to or agreeing with the Company [Zurich] as respects Policy alteration, for making or receiving payments of premium or adjustments to premium, and as respects the payment for claims. (C530 at §3).

handling the insurance claim and receiving the claim payments. According to IEI, City Colleges would have then suffered a "loss" and Zurich would be subrogated to City Colleges' recovery rights against IEI. It would be absurd to conclude that Zurich's subrogation rights depend on a fact as unrelated and random as whether the project owner or general contractor buys the builder's risk policy. IEI's argument in favor of that absurd conclusion should be rejected. *See United States Fire Ins. Co. v. Hartford Ins. Co.*, 312 Ill. App. 3d 153, 155 (1st Dist. 2000) ("a strained, forced, unnatural, or unreasonable construction [of an insurance policy], or one which would lead to an absurd result, must not be adopted").

ii. IEI argues that Zurich's subrogation rights depend on whether City Colleges sustained a financial loss as a result of the flooding incident.

This case involves a builder's risk insurance policy that afforded first-party property coverage for damage to the Malcolm X College building during its construction. As the property insurer, Zurich paid the cost of necessary repairs without regard to who was at fault for the building damage. (C10630-10631 V7 at pp. 48-49; C10641 V7 at p. 92; C10664 V7 at 183:23-184:7). Thus, the only loss relevant to Zurich's subrogation rights is the building damage covered under Zurich's policy. *See, e.g. Beman v. Springfield Fire & Marine Insurance Co.*, 303 Ill. App. 554, 556, 563 (1st Dist. 1940) (concluding that plaintiffs suffered "no loss" based upon the coverage afforded by their insurance policy).

IEI ignores the type of insurance involved here by arguing that Zurich's subrogation rights depend on whether City Colleges sustained a *financial* loss because of the flooding incident. Though IEI contends that City Colleges did not sustain a financial loss here, it is difficult to discern IEI's basis for that contention. To the extent that IEI bases its contention on the fact that Zurich issued the claim payments to CMO, IEI's contention lacks merit for

the reasons discussed in Argument II., E., i., *supra*. To the extent that IEI contends City Colleges sustained no financial loss here because Zurich covered the cost of necessary repairs, IEI ignores the fact that on the day after the flooding incident, City Colleges was the owner of a damaged building in need of extensive repairs.[8]

F. The First District properly rejected IEI's arguments.

IEI squarely opposes Illinois law by arguing that Zurich's subrogation rights should be determined based the elements of a claim for equitable subrogation rather than the subrogation clause in Zurich's policy. *Dix*, 149 Ill. 2d at 319. Moreover, IEI's argument finds no support in *SwedishAmerican*, *Economy Premiere*, *Trogub* or the other cases it relies upon. Consequently, the First District correctly ruled that Zurich's contractual subrogation rights do not depend on Zurich's ability to establish the elements of a claim for equitable subrogation. *Zurich Am. Ins. Co.*, 2023 IL App (1st) 230147 at ¶¶ 32-34.

CONCLUSION

IEI misunderstands the distinctions in Illinois law between contractual subrogation and equitable subrogation and continues to rely on equitable principles that are inapplicable to Zurich's claim. Even when IEI attempts to analyze Zurich's contractual subrogation rights pursuant to its policy terms, IEI ignores the basic rules of contract interpretation and again focuses on irrelevant equitable principles, such as who received claim payments.

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[8] IEI also seeks support from *New York Bd. of Fire Underwriters v. Trans Urban Constr. Co.*, 91 A.D.2d 115 (N.Y. App. Div. 1983), where the builder's risk carrier improperly claimed a right of subrogation against one of its own insured. Here, IEI is not an insured under Zurich's policy. (C526-5690). Moreover, in *New York Bd. of Fire Underwriters*, the contractor protected the owner against loss by agreeing to accept all risk of loss, repairing the damages, and making a claim with the builder's risk carrier for reimbursement of those repair costs. In stark contrast, IEI did none of those things in the instant case.

Zurich's contractual subrogation rights are determined by its policy, and it was inappropriate for the circuit court to consider equitable factors when granting summary judgment. Nevertheless, even if equitable prerequisites are deemed to apply to this case, Zurich has satisfied those prerequisites to pursue subrogation against IEI. As such, Zurich respectfully requests that this Court affirm the First District's decision reversing the circuit court's summary judgment order.

Respectfully submitted,

/s/ *Patrick C. Hess*
One of Plaintiff-Appellee's Attorneys

Patrick C. Hess
Jenna L. Mahoney
NIELSEN, ZEHE & ANTAS, P.C.
55 West Monroe Street, 1800
Chicago, Illinois 60603
(312) 322-9900
phess@nzalaw.com
jmahoney@nzalaw.com
Attorneys for Plaintiff-Appellee

CERTIFICATE OF COMPLIANCE

I certify that this brief conforms to the requirements of Rules 341(a) and (b). The length of this brief, excluding the pages contained in the Rule 341(d) cover, the Rule 341(h)(1) table of contents and statement of points and authorities, the Rule 341(c) certificate of compliance, the certificate of service, and those matters to be appended to the brief under Rule 342(a), contains 29 pages.

/s/ *Patrick C. Hess*
Patrick C. Hess

NOTICE OF FILING and PROOF OF SERVICE

In the Supreme Court of Illinois

ZURICH AMERICAN INSURANCE COMPANY, as subrogee of Community College District No. 508, d/b/a City Colleges of Chicago and CMO, a Joint Venture *Plaintiff-Appellee,* v. INFRASTRUCTURE ENGINEERING, INC., *Defendant-Appellant.*	)	No. 130242

The undersigned, being first duly sworn, deposes and states that on April 3, 2024, there was electronically filed and served upon the Clerk of the above court the Brief of Appellee. On April 3, 2024, service of the Brief will be accomplished via the filing manager, Odyssey EfileIL, to the following counsel of record:

Newton C. Marshall
Douglas R. Garmager
KARBAL, COHEN, ECONOMOU SILK & DUNNE, LLC.
nmarshall@karballaw.com
dgarmager@karballaw.com

Within five days of acceptance by the Court, the undersigned states that 13 paper copies of the Brief bearing the court's file-stamp will be sent to the above court.

/s/ Patrick C. Hess
Patrick C. Hess

Under penalties as provided by law pursuant to Section 1-109 of the Code of Civil Procedure, the undersigned certifies that the statements set forth in this instrument are true and correct.

/s/ Patrick C. Hess
Patrick C. Hess