The action for subrogation in Article 43 of the Insurance Contracts Act: latest case law in the First Chamber (Civil Division) of the Supreme Court

Comment on the Supreme Court Judgments of 21 July and 22 November 2021

José Antonio Badillo Arias
Territorial Representative of the CCS in Madrid

Introduction

Actions for subrogation are one of the most usual brought by insurers against third parties liable for a loss event and, in many cases, when these parties have a civil liability insurer, against such firms.

As with the cases which are examined in the High Court judgments of 21 July and 22 November 2021, it is common for such an action to be pursued in the context of residents' associations given the frequency of losses that they experience, where the association's insurer who indemnifies the losses to common property is subrogated to the position of its insured (the residents' association) and brings an action for recovery against the perpetrator of the loss. Thus, after the insurer for own damage has indemnified its insured for this particular amount, it is subrogated to their position and exercises the rights and remedies which that insured party might have available against the party liable for the loss if this has indeed been caused by a third party.

Therefore, the first thing that we must take into account is that it is not an autonomous action but is instead the same remedy which the insured had available against the third party, which has different legal effects, above all as regards the period of the statute of limitations, since the time which the insured had to bring a claim against the perpetrator for damages counts for the insurer to bring the action. This is why, if the insurer delays paying out to its insured, its action against the liable third party may have become time-barred, except where the insured themselves have interrupted the prescriptive period in which to act against the third party.

Actions for subrogation are regulated under Article 43 of the Insurance Contracts Act, which stipulates that "having paid out the indemnity, the insurer can exercise those rights and remedies to which the insured might be entitled to pursue on account of the loss event against the persons liable for it, up to the limit on indemnity."

Therefore subrogation of the insurer to the insured's position in relation to the third party who has perpetrated the loss shall arise if three conditions are present: a) the insurer has paid out the indemnity by dint and as a result of the insurance contract, b) the option has arisen for the insured of suing the third party for liability, where the latter is neither the policyholder nor an insured party, and c) the requirements are satisfied for civil liability to exist, be this of whatever kind (contractual, extra-contractual or *ex delicto*).

Since this is regulated under Heading I of the Insurance Contracts Act, such a remedy is only viable for insurance against loss or damage, which this Heading oversees. As a result, this does not apply to insurance of persons, except as regards healthcare expenses (Art. 82 of the Insurance Contracts Act). This exception is justified on the grounds that such costs merit legal consideration as damage.

Nature and prerequisites of actions for subrogation

Actions for subrogation are regulated under Article 43 of the Insurance Contracts Act, which stipulates that "having paid out the indemnity, the insurer can exercise those rights and remedies to which the insured might be entitled to pursue on account of the loss event against the persons liable for it, up to the limit on indemnity."

Therefore subrogation of the insurer to the insured's position in relation to the third party who has perpetrated the loss shall arise if three conditions are present: a) the insurer has paid out the indemnity by dint and as a result of the insurance contract, b) the option has arisen for the insured of suing the third party for liability, where the latter is neither the policyholder nor an insured party, and c) the requirements are satisfied for civil liability to exist, be this of whatever kind (contractual, extra-contractual or *ex delicto*).

For it to be possible to pursue such legal action, besides the insurer having paid out the indemnity, there must be a liable third party and the insured must have become entitled to sue the third party for liability. The third party is thus the person who, on causing detriment to the insured, incurs an obligation to pay an indemnity which, via the mechanism of subrogation, the insurer comes to assume. Even so, this may not be a third party who has insured status at the same time. Consequently, the insurer would not be entitled to pursue any remedy against the latter. Specifically, the Supreme Court Judgment of 21 July 2021 (Case Law 2021, 251607) explains the situation thus when it says that "subrogation requires that the insured and the loss perpetrator be separate persons, given that subrogation is not possible against the insured themselves, since this would amount to saying that a right exists to act against oneself."

On the other hand, such an action cannot be exercised to the detriment of the insured, nor either against any of the persons whose acts or omissions produce liability for the insured according to the law, except if liability stems from intentional misconduct or if it is enshrined under an insurance contract (Article 43, paragraph 3 of the Insurance Contracts Act).

Likewise, neither shall the insurer be entitled to subrogation against a perpetrator of the loss who is a relative via a direct or collateral line within the third degree of civil kinship by blood, a father by adoption or adoptive offspring who live with the insurer, save where liability stems from intentional misconduct or if it is enshrined under an insurance contract (Article 43, paragraph 3 of the Insurance Contracts Act).

Judgment No. 557/2021 by the Civil Division of the Supreme Court of 21 July 2021

Introduction

This judgment considers an action for subrogation by the insurer to the rights of a home-owners' community in relation to damage to communal parts as a result of a fire that started on the premises of an owner in the community.

In the case of insurance for home-owners' communities, given that these lack a legal personality, for the purposes of the policy homeowner status changes. On the one hand, homeowners are insured parties with respect to the policy for loss or damage to the owners' community, while on the other hand, for the purposes of civil liability arising from communal elements insurance contracts treat them as third parties in relation to the owners' community.

In my view, from a legal standpoint they are neither fully insured with respect to the common property (as the judgment which we are discussing appears to suggest) nor either are they third parties in the full sense as far as liability is concerned that is attributable to the communal parts. In my understanding they can only be insured parties in proportion to their share in the owners' community and, by the same reasoning, they should be treated as third parties with regard to liability in respect of the full amount of communal property minus their proportionate share in it. In this case, for example, there should be a possibility of deducting a fellow home-owner's proportionate share as regards the losses which the communal property causes to the latter.

The events that occurred and the lower court judgments

The case examined in the judgment we are discussing concerns a fire which started on the premises of a fellow owner and caused damage to the residents' community. These losses are indemnified by the insurer of the owners' community under the own damage insurance which it had taken out.

Having indemnified the home-owners' community for the loss and damage, by dint of an action for subrogation regulated under Article 43 of the Insurance Contracts Act the insurer was subrogated to the position of its insured (i.e. the community) and brought the action against the person responsible for the damage, who was one of the fellow owners in the community.

The judgment which the court of first instance delivered dismissed the suit since it was of the opinion that the cause of the fire was accidental and that there was no risk-producing activity on the premises which the defendant owned that might enable a reversal of the burden of proof. As a result, it was not possible to find for the claimant if there was no liability that could be enforced of the defendant.

In response to the claimant's ordinary appeal, contrary to the contention of the lower court, the Provincial Higher Court held that it was legally possible to attribute the damage caused to the defendant. According to the appeals division "it appears evident that the civil liability arising from the fire which took place on the defendant's premises is not covered under the policy cited since it is not consistent with any of the circumstances described."

The appeal to the Supreme Court

Following this judgment, the defendant filed an appeal with the Supreme Court, essentially using the line of argument that the subrogation to which Art. 43 of the Insurance Contracts Act refers operates in respect of claims which the insured parties have available against the third party who perpetrated the damage, and that, in the event of litigation, filing such a suit would not be in order, given that the defendant has insured status under the policy. In short, subrogation assumes that there is a third party in relation to the insurance contract, against whom the company can bring an action for recovery of the pay-out it made. Moreover, in this particular case the defendant had the status of an owner who was insured against the loss event which was covered, and the insurer cannot exercise the right to which it has been subrogated to the detriment of the insured.

As is self-evident, the bone of contention focusses on determining whether or not an insurer of an owners' community can bring an action for subrogation against one of the fellow owners who is liable for the damage to the

communal areas. In summary, we should resolve the issue of whether or not this fellow owner is considered to be an insured party in the community policy, which, if so, according to Article 43.2 of the Insurance Contracts Act, would produce a situation where the insurer cannot exercise the rights to which it has been subrogated to the detriment of the insured.

The legal basis which the Supreme Court cites

After referring to its body of case law on actions for subrogation resulting from several judgments, the Civil Division dismissed the insurer's claims on the grounds that it believed that subrogation requires that the insured and the loss perpetrator should be separate persons. This is because it is not possible to bring an action for subrogation against the insured themselves, since this would amount to saying that a right exists to act against oneself.

The judgment holds that the insurance contract was arranged by the home-owners' community for the building which the defendant is a part of given his status as the owner of a premises. According to the general conditions in the policy, specifically in Article 10 thereof, the insured is understood to mean "any person who has an economic interest in the property that is the object of the insurance." The defendant indisputably has such status in his capacity as owner of the premises which caught fire, as well as given the fact that he is a co-owner of the building and therefore a joint owner of the communal parts of the building that has coverage.

Therefore, in the opinion of the Civil Division of the Supreme Court, given that it is not possible for the insurer to bring an action for recovery against the insured, it appears appropriate to allow the appeal, bearing in mind the general conditions agreed in the insurance policy which govern the relations of the parties and corresponding interpretation thereof.

Judgment No. 798/2021 by the Civil Division of the Supreme Court of 22 November 2021

Introduction

The judgment which we reviewed in the previous section settles a case that is similar to that which we shall see in this judgment here. As we have indicated, the judgment of 21 July 2021 also concerns an action for subrogation by the insurer of a home-owners' community which, following the breakout of a fire in a housing unit, was subrogated to the position of its insured —namely the community– and brought a claim against the owner of that dwelling. On the other hand, in the judgment of the Civil Division of the Supreme Court of 22 November, the action for subrogation was brought against the tenant of a premises where the fire originated. We will see how the outcome is different when the action for subrogation is brought against a tenant rather than an owner of a dwelling or premises within the owners' community.

The events that occurred and the lower court judgments

The case at hand now is similar, although the premises where the fire broke out that caused damage to both communal areas and the premises was rented. This is why the community's insurer brought a claim for damages for this loss, not from the owner, but instead from the tenant of the premises, who, as regards the community's insurance contract, is considered to be a third rather than an insured party.

In this case the debate essentially turns on the contractual or extra-contractual nature of the action for subrogation which the community's insurer brought, to the extent that deciding that this involves one or the other affects the limitation period. If it is considered that the insurer is subrogated to the position of the home-owners' community, the action brought against the tenant and their insurer is extra-contractual, whereas if it is held that it is subrogated to the position of the owner of the premises (also insured in the community's policy), the action would be contractual.

Both the court of first instance and the Provincial Higher Court were of the view that what we have here is an extra-contractual action, for which the limitations period is one year. The claim was therefore dismissed at both court levels given that it was found that the exceptional limitation period of one year which Art. 1968.2 of the Civil Code stipulates should apply.

The appeals to the Supreme Court and against a decision of the Provincial Higher Court based on a mistake in law

For this reason, in its appeal to the Supreme Court against the decision of the Provincial Higher Court based on a mistake in law, the appellant insurer alleges that the Provincial Higher Court was wrong and altered the cause of action in stating that the claimant insurer was subrogated to the actions which were the preserve of the home-owners' community, when in fact it was subrogated to those which fell to the owner of the premises to bring in the latter's capacity as landlord.

Thus, the insurer which had brought the action for subrogation against the tenant of the premises and the latter's insurer maintains that the suit is contractual, and that it was subrogated to the owner of the premises (also insured under the community policy), since he was the injured party as a result of the fire. The appellant therefore considers that the Provincial Higher Court is attributing injured party status to somebody who was not such a party, because the person who actually has such status is whoever has been indemnified by the insurer, and in this case, this was the owner and landlord of the premises.

The legal basis which the Supreme Court cites

While alluding to its judgment No. 557/2021 of 21 July, which we have made reference to in the previous section, the Civil Division states that according to Art. 43 of the Insurance Contracts Act the claim which the insurer acquires is derivative (it comes from the insured) and is identical to that which the insured has against the third party that caused the loss or damage, which means that bringing it is subordinated to the same legal requirements upon which the insured's claim against the third party depends. And such subrogation entails the actions which the insurer can bring being the same as those which the insured/injured party could pursue.

With regard to this the Court Division believes that even if he is not the policy-holder, the owner of the premises had an economic interest in the property that was the object of the insurance policy in his two-fold capacity as both joint owner of the building (of the communal elements thereof) and owner/landlord of the premises where the fire took place.

On this basis the damage which the insurer indemnified was that which occurred to both the communal parts of the building and the particular premises. This is why it should be understood that, in accordance with Art. 43 of the Insurance Contracts Act, the insurer was subrogated to both of the actions that stemmed from the loss indemnified, to wit (i) that associated with liability in tort which fell to the home-owners' community to bring against the tenant of the premises and insurer thereof for the damage to communal elements of the building (Art. 1902 of the Civil Code) and (ii) the action for contractual liability which the member of the owner's community/landlord had available

against the same tenant for damage to the actual premises rented (Art. 1563 of the Civil Code), which was the action brought in the suit that originated these proceedings.

Matters being thus, the period of limitation, the point at which this starts being calculated and the possibility of interruption will depend on the nature of the claim which gives rise to the action that the insured conveys to the insurer. In other words, if the claim was of a contractual nature, the limitations period in Art. 1964-2 of the Civil Code would apply (or that in the specific regulation governing the particular contract), whereas if it was extra-contractual, the period would come to apply that is envisaged in Art. 1968.2 of the Civil Code.

The Court concludes that when concurrent actions derive from a single detrimental event (the fire), in this case (i) one for contractual liability with the owner of the premises and (ii) another for liability in tort with the home-owners' community, each action has a separate limitations period: that in Art. 1964.2 of the Civil Code in the first instance and that in Art. 1968.2 of the Civil Code in the second. And the decisive factor in this case is that in the lawsuit only the action for subrogation deriving from contractual liability was brought, this being that to which the landlord was entitled to bring against the tenant, meaning that the limitations period is five years, as stipulated in Art. 1964.2 of the Civil Code.

Consequently the High Court gave leave to proceed to the appeal which the insurer had filed to it and ruled that, due to being contractual in nature and having a limitations period of five years, the action had not become time-barred, although it did not actually deliver a judgment on the underlying issue, given that it understood that an appeal to the Supreme Court to review an appellate court judgment is not a new trial which (in the same way as a high court review of a judgment issued by a court of first instance) would have permitted a full hearing of all the background facts de *facto* and de *jure* for consideration thereof. Therefore, the ruling delivered by this particular court had to (as Article 487.2 of the Civil Procedure Act authorises) confine itself to quashing the judgment that was appealed against so that the appeals court might, as a court with full powers to hear all the issues de *facto* and de *jure* in the proceeding, settle these in a judgment, given that it was no longer possible to accept time-barring of the specific action brought in the suit.

Conclusions

After analysing the two judgments returned by the First Chamber (Civil Division) of the Supreme Court, the High Court lays down the requirements regarding actions for subrogation regulated under Article 43 of the Insurance Contracts Act. As we have said, what we have is not an autonomous action which the insurer can bring against the third party with liability, but instead the same action which the insured had available to move against the latter, for which reason the limitations period is the same as that which the insured had in which to act against the third party who had caused the loss or damage. By the same token, the nature of the action (whether contractual or extra-contractual) is the same as that available to the insured against the liable third party, as was effectively stated in the second of the judgments we have discussed.

We have also seen that the action is conditional upon three requirements:

a. The insurer must have paid out the indemnity by dint and as a consequence of an insurance contract.

b. The option of suing the third party for liability must have arisen for the insured in law, where the former is neither the policy holder nor an insured party.

c. The requirements for civil liability to exist must have been satisfied, of whatever nature this might be (contractual, extra-contractual or *ex delicto*).

On the other hand, in the first judgment discussed (that of 21 July 2021) the action for subrogation is brought against one of the members of the owners' community. In this case we have observed that the High Court considers the fellow owners to be the insured in the owners' community policy, and thus believes that the insurer cannot be subrogated when this is to the detriment of the insured, despite the latter being liable for the loss or damage to the community.

In my view this is a controversial matter, because I believe that the fellow owners are insured parties in the community policy only to the extent of their proportional share in the community. They have no insurable interest beyond this proportional share, given that the rest of the community property does not belong to them but instead to the other fellow owners. For this reason, it could be held that the insurer could claim all the losses paid out from the community (the other fellow owners) except for those corresponding to their proportional share, given that they are really the owner and insured as regards the losses.

On the other hand, in the second judgment (that of 22 November 2021) the insurer of the owners' community brings the action for subrogation against a tenant, who was the person responsible for the fire that caused loss and damage to the community property. In this case the Supreme Court does consider him to be a third party and therefore passively entitled to be sued and ordered to pay damages. We have also seen that, as regards the limitation period, the Supreme Court understands that the action which the insurer brings against the tenant is contractual, because this is the action which was available to the owner of the premises to bring against the tenant liable for the fire.