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APPROVAL OF THE APPELLATE DIVISION

SUPERIOR COURT OF NEW JERSEY
APPELLATE DIVISION
DOCKET NO. A-5407-09T3

FIDELITY & DEPOSIT COMPANY OF MARYLAND,

Plaintiff-Appellant,

v.

HAROLD STAMATERIS, HB ASSOCIATES, ESTATE OF WILLIAM D. EATON, JR., MARY JANE EATON, ENERNET, INC., LIGHT SOURCE ENERGY SERVICES, INC., ANANT PATEL, YOGINI PATEL, QAI ENGINEERING INC., OPTIMA, INC. a/k/a OPTIMA CO., ENERGY PLUS ASSOCIATES, INC., GIRISH PATEL a/k/a GARY PATEL, ENERGY REDUCTION ASSOCIATES a/k/a ENERGY REDUCTION, OSBOURNE MCINTOSH, MCINTOSH ELECTRICAL CONTRACTORS, INC., WICLIFF REID, SR., a/k/a WYCLIFFE REID, SR., QAI INSPECTION ASSOCIATES, a/k/a QA INSPECTION ASSOCIATES, WYCLIFFE O. REID, JR. a/k/a WICLIFF REID, JR., SWA ASSOCIATES, DWIGHT WILLIAMS, ONYX UTILITIES, ERIC BELL, ORBIT ELECTRICAL CONTRACTORS, LLC, CLAUDIUS BROWN, ALL SAFE ELECTRICAL CO., RONALD JOHNSON, R.G. ASSOCIATES,

Defendants,

and

HONEYWELL INTERNATIONAL INC., and HONEYWELL DMC SERVICES, INC.,

Defendants-Respondents.

Argued January 26, 2011 - Decided July 25, 2011

Before Judges Fuentes, Ashrafi and Nugent.

On appeal from Superior Court of New Jersey, Law Division, Morris County, Docket No. L-3703-07.

Andrew Samson argued the cause for appellant (Baron Samson LLP, attorneys; Mr. Samson, on the brief).

John C. Garde argued the cause for respondents (McCarter & English, LLP, attorneys; Mr. Garde, Debra M. Perry, of counsel and on the brief; Steven Beckelman, of counsel; Gary Tulp and Maritza Braswell, on the brief).

PER CURIAM

Plaintiff Fidelity & Deposit Company of Maryland ("Fidelity") brought this subrogation action to recover almost $10 million in crime insurance compensation it paid to Jersey Central Power and Light Company ("JCP&L"). Fidelity appeals from two April 9, 2010 orders denying its motion for summary judgment and granting summary judgment to defendant Honeywell International Inc. ("Honeywell"), which employed one of the main perpetrators of a massive fraudulent scheme against JCP&L. We affirm in part and reverse in part.

I.

The facts relevant to the issues on appeal are not in dispute. The New Jersey State Board of Public Utilities had established the New Jersey Smart Start Buildings Program to stimulate energy-efficient and renewable-energy technologies.

The program provided rebates to electricity customers who retrofitted commercial buildings to become more energy efficient. JCP&L and other utilities administered the program and charged a fee in customer bills to fund it.

In 1991, a predecessor company of Honeywell entered into a written contract with JCP&L to provide personnel to work on JCP&L's energy efficiency programs. When Honeywell acquired the predecessor company, it succeeded to the contract and later extended it through 2006. The parties on this appeal stipulated to the several documents that comprised the Honeywell-JCP&L contract.

Under the contract, Honeywell assigned employees to JCP&L to work on its energy programs in exchange for a fixed sum paid by JCP&L to Honeywell. The assigned employees worked exclusively for JCP&L, but Honeywell continued to pay their salaries and benefits. Article 10 of the contract documents stated:

> It is agreed and understood that Contractor [Honeywell] shall employ for the services required hereunder persons known to it, who shall be trained, experienced, qualified and <u>trusted</u> employees. (Emphasis added.)

The right of final selection or replacement of the designated Honeywell employees remained with JCP&L.

In 1996, Honeywell designated defendant Anant Patel to work with JCP&L as a commercial program coordinator on its energy savings programs. Patel had been employed by Honeywell and its predecessor since 1985. He was "well-liked," "produced high quality work," and had a "very strong work ethic." Honeywell had no reason to distrust his honesty.

In 2001, Patel was assigned to work with the Smart Start Buildings Program. Among his duties was to inspect and verify claims for energy efficiency rebates in accordance with the program's guidelines. He was to ensure that rebates were properly due, and he was required to report any fraudulent claims to the top JCP&L manager for the program. During the five years that Patel worked with the Smart Start Buildings Program, he was supervised directly by defendant Harold Stamateris, a JCP&L employee. Stamateris's duties included approving rebate checks to be issued to customers or vendors.

In May 2001, Stamateris and an outside contractor, William Eaton, began to defraud the program, and Stamateris soon enlisted Patel to join their scheme. Over the next five years, Patel set up fraudulent companies to submit false or inflated invoices to JCP&L claiming they provided technical, consulting, or installation services to JCP&L’s customers for energy efficiency savings. Patel’s role was to approve the work shown

on the invoices, and Stamateris's role to approve issuance of the rebate checks. In addition to setting up three fraudulent companies of his own to receive the rebate funds, Patel induced others to set up such companies but typically controlled their financial affairs himself. From the rebate funds, Patel kicked back money to a company owned by Stamateris.

In May 2006, JCP&L received an anonymous letter revealing the fraud. It conducted an internal audit and investigation, in the course of which both Stamateris and Patel admitted their roles in the fraud. Stamateris provided a spreadsheet with detailed information reconstructing the fraudulent transactions in which he participated. JCP&L's investigation revealed that the fraud involved more than 8,000 transactions, causing fraudulent payments estimated at $9.7 million.

In 2007, Stamateris and Patel pleaded guilty to crimes arising from the fraud. Stamateris was sentenced to ten years' imprisonment and ordered to pay restitution of $3.7 million. Patel was sentenced to fifteen years' imprisonment and ordered to pay restitution of $1.4 million.

In January 2008, JCP&L paid $10,639,050.16 "to reimburse the State of New Jersey with interest for monies taken fraudulently from the New Jersey Clean Energy Program." Earlier, JCP&L had submitted a claim and proof of loss on a

crime insurance policy issued by Fidelity seeking reimbursement of the amount owed to the State. After adjustments, JCP&L's claim consisted of $9,658,814.12 in stolen funds, $900,000 in interest owed, and $109,300.87 for attorney's fees. Fidelity paid JCP&L $9,408,814.12, representing the full amount of the theft minus the $250,000 policy deductible. Later, Fidelity paid additional amounts to settle JCP&L's claims for interest and attorney's fees. In total, Fidelity paid to JCP&L $9,994,114.99 in insurance proceeds.

In exchange for these payments, JCP&L assigned to Fidelity all its rights against those responsible for its losses. As of December 9, 2009, Fidelity had recovered about half of what it had paid, including $2,726,667.68 from Stamateris and $774,282 from Patel.

II.

Fidelity's subrogation causes of action against Honeywell alleged breach of contract, negligent hiring of Patel, and respondeat superior liability for Patel's fraud. After the cross-motions for summary judgment were filed, Fidelity abandoned its claim of negligent hiring and proceeded only on the other two causes of action. Relying on several provisions of the Honeywell-JCP&L contract, Fidelity sought summary judgment against Honeywell for recovery of $5,160,254.82 in

benefits paid to JCP&L. The trial court denied Fidelity's motion and instead granted summary judgment to Honeywell dismissing the causes of action for breach of contract and respondeat superior liability.

We now affirm in part the court's summary judgment orders. We reverse in part and reinstate some of Fidelity's claims for breach of contract.

A.

We affirm dismissal of Fidelity's respondeat superior cause of action for the reasons stated by the trial judge in his oral opinion. We briefly summarize the basis for our decision.

By its claim for respondeat superior liability in tort, Fidelity asserted that Honeywell is vicariously liable for the fraud committed by its employee, Patel. In the circumstances of this case, Patel was a borrowed or "special employee." See Pacenti v. Hoffman-La Roche, Inc., 245 N.J. Super. 188, 190-92 (App. Div. 1991). In Galvao v. G.R. Robert Construction Company, 179 N.J. 462 (2004), the Court discussed a two-part test for the vicarious liability of a general employer such as Honeywell for the conduct of a special employee such as Patel. The plaintiff must show both that the general employer controlled the special employee and that the employee furthered the business of the general employer. Id. at 471-72. Here,

Patel furthered the business interests of Honeywell because Honeywell was compensated for his services to JCP&L. The trial court also concluded there was no genuine issue of fact for trial on the issue of who controlled Patel, finding that JCP&L controlled Patel's services, not Honeywell. We need not resolve the parties' dispute as to that conclusion because an alternative basis clearly applied to preclude vicarious liability of Honeywell.

An employer is vicariously liable for tortious conduct of an employee that is within the scope of his employment. Id. at 473 n.4; see Carter v. Reynolds, 175 N.J. 402, 409, 410-12 (2003). Conduct of an employee is within the scope of employment when "it is of the kind that he is employed to perform; it occurs substantially within the authorized time and space limits; [and] it is actuated, at least in part, by a motivation to serve the master." Roth v. First Nat'l State Bank, 169 N.J. Super. 280, 285 (App. Div.), certif. denied, 81 N.J. 338 (1979). Conversely, conduct is not within the scope of employment "if it is different in kind from that authorized, far beyond the authorized time or space limits, or too little actuated by a purpose to serve the master." Id. at 286.

Here, Patel's massive fraudulent conduct was clearly outside the scope of his employment. Fidelity relies on Patel's

statement that he was motivated to commit fraud in part because it would increase the amount of business done by Honeywell in the rebate program, but that statement is inherently unworthy of credence and insufficient to create a genuine issue of material fact as to the scope of his employment. See Brill v. Guardian Life Ins. Co. of Am., 142 N.J. 520, 540 (1995) (summary judgment is appropriate where "evidence 'is so one-sided that one party must prevail as a matter of law'") (quoting Anderson v. Liberty Lobby, Inc., 477 U.S. 242, 252, 106 S. Ct. 2505, 2512, 91 L. Ed. 2d 202, 214 (1986)). Honeywell cannot be held vicariously liable for Patel's criminal conduct intended to reap millions of dollars in illegal proceeds for himself and his co-conspirators.

B.

We also reject Fidelity's breach of contract claims based on the previously-quoted Article 10 of the contract documents and on Article 19, which prohibited payment of gratuities to JCP&L employees.

Article 10 required that Honeywell designate for assignment to the JCP&L programs only employees who were "trained, experienced, qualified and trusted." There is no factual dispute that Patel met those qualifications in 1996 when Honeywell designated him to work on the programs. Fidelity argues that Article 10 set forth a continuing duty of Honeywell

to provide only trusted employees, and Patel did not meet that requirement after 2001 when he began defrauding JCP&L. According to Fidelity, whether Honeywell knew or did not know that Patel was dishonest and committing fraud after 2001 is irrelevant to Fidelity's claim for breach of contract. The fact is that Patel could not be trusted and that constitutes a breach of Article 10 by Honeywell.

In making that argument, Fidelity seeks to change the specific wording of Article 10 to state, in effect, that the designated employee had to be trustworthy and honest, not just trusted by Honeywell. The construction of a contract term is a question of law. Bosshard v. Hackensack Univ. Med. Ctr., 345 N.J. Super. 78, 92 (App. Div. 2001). A trial court's legal interpretation of the meaning of a contract is subject to plenary appellate review. Fastenberg v. Prudential Ins. Co. of Am., 309 N.J. Super. 415, 420 (App. Div. 1998). We must give the terms of the contract their plain and ordinary meaning. See M.J. Paquet v. N.J. Dep't of Trans., 171 N.J. 378, 396 (2002).

We agree with the trial court's interpretation that the plain meaning of "trusted" refers to Honeywell's knowledge or reason to know that employees it was designating for service on the JCP&L programs were honest and reliable. There is no genuine issue of fact on this record as to whether Honeywell had

reason to distrust Patel until 2006 when JCP&L disclosed his fraudulent conduct. Prior to that, Patel had a favorable work record, and there is no evidence that Honeywell should have discovered the fraud any earlier than JCP&L did.

The scope of legal review of a contract includes determining whether a term is clear or ambiguous. Nester v. O'Donnell, 301 N.J. Super. 198, 210 (App. Div. 1997). A contract provision is ambiguous if it is "susceptible to at least two reasonable alternative interpretations." Here, even if Article 10 is considered ambiguous as to the meaning of "trusted," the contract term must be strictly construed against JCP&L, which was the drafter of the contract. See Driscoll Constr. Co., Inc. v. State Dep't. of Transp., 371 N.J. Super. 304, 318 (App. Div. 2004). Because Fidelity steps in the shoes of JCP&L as its subrogee, and its claims are no greater than those of JCP&L would have been, the ambiguity must be construed against Fidelity. See Standard Accident Ins. Co. v. Pellecchia, 15 N.J. 162, 172 (1954) ("The subrogee . . . is subject to all legal and equitable defenses that the third party may have either against him or the insured").

Applying these several rules of contract interpretation, Fidelity cannot prove Honeywell's liability under Article 10 of the contract documents.

Fidelity also argues that Honeywell breached Article 19 of the contract, which stated:

> Contractor [Honeywell] or its employees shall not, under circumstances which might reasonably be interpreted as an attempt to influence the recipients in the conduct of their duties, extend or accept any gratuity or special favor to or from employees of Owner [JCP&L].

Fidelity argues that Patel paid gratuities to Stamateris. It relies upon Patel's certified statements that he "compensated Stamateris for his role in this scheme through the payment of kickbacks to his company . . . to ensure his dishonesty."

The trial court rejected Fidelity's contention, reasoning:

> the criminal plotting that occurred between Stamateris and Patel cannot be shoehorned into the definition of gratuity or special favor. In other words, Patel was not acting alone and simply paying off either Stamateris or Eaton so that they would keep silent while Patel, in fact, profited by his own criminal actions, rather Patel joined a conspiracy that was already in existence between Stamateris and Eaton, and any payments that Patel made to either were because all three were wholly and actively involved in an elaborate scheme to defraud JCP&L.

We agree. The arrangement between Patel and Stamateris was a sharing of the proceeds of the fraud, not payment of gratuities to Stamateris to ensure his dishonesty. Stamateris admitted he and Eaton initiated the scheme, and he enlisted Patel to join. Even if the kickbacks from Patel were to be considered

gratuities paid to Stamateris, they were not an attempt to influence Stamateris in the conduct of his duties. They were payment for misconduct that Stamateris himself initiated. Article 19 did not apply to the scheme.

C.

Fidelity contends that Honeywell breached Article 36, the indemnification provision of the contract, which provided in relevant part:

> Contractor [Honeywell] shall indemnify, defend, and hold harmless Owner [JCP&L], its agents, officers and employees, from and against any and all claims, demands, actions, causes of action, suits, damages, expenses (including attorneys' fees) and liabilities whatsoever based upon, resulting from, or arising out of (a) any injury to or death of any person . . . or any damage to or loss of use of property, or damage to the environment, which may occur or be alleged to have occurred as a result of or in connection with any acts or omissions or otherwise of Contractor, its employees and/or agents, or anyone acting under its direction or control or in its behalf in the course of its performance or arising under this Contract.

In rejecting Fidelity's claim under this provision, the trial court reasoned that indemnity clauses do not apply to first-party losses, and Fidelity's claim as subrogree sought recovery for JCP&L's own losses. We disagree with that understanding of the undisputed factual record.

The trial court correctly stated that Article 36 applied to liability incurred to a third party and not for any other direct economic losses of JCP&L. See Travelers Indem. Co. v. Dammann & Co., 592 F. Supp. 2d 752, 766-67 (D.N.J. 2008) ("It is axiomatic that a claim for indemnification, whether contractual or common law, must be based upon the indemnitee's claim to obtain recovery from the indemnitor for liability incurred to a third party"), aff'd, 594 F.3d 238 (3d Cir. 2010). However, Fidelity sought indemnity for JCP&L's third-party liability to the State of New Jersey, not for its direct economic losses, such as the contract price paid to Honeywell for Patel's services during the five years of his fraudulent activity.

After receiving insurance proceeds from Fidelity of $9,994,114.99, JCP&L paid $10,639,050.16 to the State. JCP&L paid that amount because it was liable to reimburse the State for "monies taken fraudulently from the New Jersey Clean Energy Program." Fidelity sought from Honeywell indemnification for JCP&L's liability to the State, not to compensate any other loss suffered by JCP&L. Any direct losses of JCP&L other than liability to the State would not be covered by the indemnification article of the contract.

Honeywell asserts two additional grounds that Article 36 was inapplicable to Fidelity's claim. First, it contends that,

under the law, JCP&L's own negligence defeated its right of recovery under the indemnification term of the contract. Honeywell relies on Ramos v. Browning Ferris Industries of South Jersey, 103 N.J. 177, 191 (1986), in which the Court held that "a contract will not be construed to indemnify the indemnitee against losses resulting from its own negligence unless such an intention is expressed in unequivocal terms."

It is true that Article 36 did not provide a right of indemnification for losses caused by JCP&L's own negligence. See Mantilla v. NC Mall Assocs., 167 N.J. 262, 272-73 (2001) (defendant owner of premises, whom the jury determined to be forty percent negligent and a proximate cause of plaintiff's injuries, could not recover its defense costs under an indemnification agreement with the cleaning contractor). But whether JCP&L was negligent in failing to discover the fraud, and whether that negligence was a cause of its losses, are disputed issues of fact that cannot be resolved by the cross-motions for summary judgment. See Barbetta Agency, Inc. v. Evening News Publishing Co., 135 N.J. Super. 214, 223 (App. Div. 1975) ("ordinarily negligence is a question of fact for the jury to determine").

Second, Honeywell contends that the phrase "damage to or loss of use of property" in Article 36 did not apply to theft or

loss of money. Although ambiguous clauses in indemnification agreements are strictly construed against the party seeking indemnity, Ramos, supra, 103 N.J. at 191; Leitao v. Damon G. Douglas Co., 301 N.J. Super. 187, 191 (App. Div.), certif. denied, 151 N.J. 466 (1997), the law recognizes that the term "property" normally includes money. See, e.g., N.J.S.A. 1:1-2; State v. Rodgers, 230 N.J. Super. 593, 601-02 (App. Div.), certif. denied, 117 N.J. 54 (1989); Duke Power Co. v. State Bd. of Tax Appeals, 129 N.J.L. 449, 450, 456-57 (Sup. Ct. 1943). The State lost use of its energy efficiency funds as a result of the fraudulent scheme. By analogy, if the State had lent equipment to JCP&L to use in implementing a State program and Patel had stolen that equipment, Honeywell would be required to indemnify JCP&L against the State's claim for loss of use of the equipment. The State funds were not conceptually different. Honeywell cites insurance cases from other jurisdictions holding that economic loss is not the equivalent of "damage to property," but those cases are not applicable to the facts here.

We hold that Article 36, the indemnification provision of the Honeywell-JCP&L contract, required that Honeywell indemnify JCP&L for loss of State funds that "occurred as a result of or in connection with any acts or omissions" of its employee, Patel, and for which JCP&L was liable to the State.

D.

We also conclude that Fidelity had direct economic claims for Honeywell's breach of contract under other provisions of the contract documents that were not specifically addressed in the trial court's decision.

We need not quote at length Articles 5, 35, 41, and 43 of the contract upon which Fidelity relies. The crux of those contract terms was to require that Honeywell remedy defective "Work" performed under the contract. "Work" was defined broadly in Article 3 as:

> all engineering, design, construction, testing, labor, services, materials, equipment, supplies, and acts required to be done, furnished, or performed by Contractor.

Honeywell argues that the term "Work" referred only to its duty to provide personnel to JCP&L. That reading of the contract is too narrow. Because Honeywell was receiving periodic compensation under the contract for the services of Patel, the term "Work" applied to the services that Patel was providing as the agent of Honeywell. His job description included the following duties:

> the incumbent will be required to report on all [commercial/industrial] program activities in an accurate and timely fashion; the incumbent will insure that all program requirements are adhered to by contractors and program participants and will report all discrepancies to the Data

> Base Sales Manager; . . . the incumbent is responsible for all C/I rebate processing; will monitor all C/I program activities and will review all contractor invoices for accuracy and program compliance.

Patel did not perform in accordance with these requirements from May 2001 until the fraud was discovered. Fidelity alleges that Honeywell did not remedy Patel's defective performance after it was discovered. Honeywell can be held liable to JCP&L, and hence to Fidelity, if the finder of facts determines that it breached the cited provisions of the contract.

Fidelity also argues in the alternative that every contract must be interpreted as containing an implied covenant that the parties will provide honest service. Such a covenant is similar to, or subsumed within, the implied covenant of good faith and fair dealing. See, e.g., Sons of Thunder v. Borden, Inc., 148 N.J. 396, 420 (1997). Having reached the conclusion that Fidelity can proceed under the express provisions of the Honeywell-JCP&L contract to recover its economic losses, we need not consider this alternative argument.

E.

Our interpretation of the contract leads us to conclude that Honeywell was not entitled to summary judgment under Article 36 providing for indemnification of JCP&L and the other cited Articles of the contract pertaining to defective "Work."

Honeywell's alleged breach, however, does not prove the amount of JCP&L's losses for which Honeywell could be liable. Losses caused by a breach of contract can be subject to comparative fault principles, as in tort causes of action. See Dunn v. Praiss, 139 N.J. 564, 577-78 (1995); Johnson v. American Homestead Mortg. Corp., 306 N.J. Super. 429, 437 (App. Div. 1997); Giri v. Rutgers Casualty Ins. Co., 273 N.J. Super. 340, 352 (App. Div.), certif. denied, 139 N.J. 185 (1994).

In this case, Stamateris, who was a JCP&L employee, and other participants in the fraud were also responsible for JCP&L's losses. The parties have not argued how comparative responsibility for the losses should be determined or apportioned in the circumstances presented. We leave those issues for the trial court to determine on remand.

For purposes of this appeal, we reverse only that portion of the orders of April 9, 2010, that granted summary judgment to Honeywell for breach of contract under Article 36, pertaining to indemnification, and Articles 5, 31, 41, and 43, pertaining to Honeywell's "Work," under the contract documents. We affirm dismissal of Fidelity's other claims and causes of action.

Affirmed in part, reversed in part.

I hereby certify that the foregoing is a true copy of the original on file in my office.

CLERK OF THE APPELLATE DIVISION