Insurance Law Update

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WHEN AN OCCURRENCE IS CLEARLY NOT INCLUDED WITHIN THE COVERAGE AFFORDED BY AN INSURING CLAUSE, IT NEED NOT ALSO BE SPECIFICALLY EXCLUDED. [Filed February 3, 2016]

In the case styled Haering v. Topa Insurance Company (2016) 244 Cal.App.4th 725, 198 Cal.Rptr.3d 291, the Court of Appeal, Second District, held that an insured's claim for underinsured motorist (**"UIM"**) benefits was not within the coverage provision of an excess liability policy defining a covered "loss" as "the sum paid in settlement of losses for which the Insured is liable" because the UIM claim was not a third party liability claim.

Larry Haering was an insured under a primary insurance policy issued by State National Insurance Company (**"State National"**) and concurrently an insured under an excess liability policy issued by Topa Insurance Company (**"Topa"**). The Topa policy designated the State National policy as the underlying primary policy. The Topa policy excluded coverage for "any liability or obligation imposed on the Insured under ... any uninsured motorists, underinsured motorists or automobile no-fault or first party personal injury law." Haering was injured in a motor vehicle accident caused by a negligent third party driver who was an insured under a policy with a $25,000 liability limit. Haering settled his claim against the negligent driver by accepting the $25,000 limit under the driver's policy and then submitted a claim to State National and eventually recovered the policy limit under the $1 million UIM endorsement to the State National policy. Haering then submitted a claim to Topa for $1 million in excess coverage, arguing that the Topa policy "followed form" to the State National policy and incorporated the $1 million UIM endorsement. Topa denied coverage for the claim on two principal grounds: (1) the policy's insuring agreement limited coverage to third party (not first party) liability claims, and (2) a policy exclusion barred coverage for liability imposed under any UIM law.

In the ensuing coverage bad faith litigation, the parties stipulated to judgment in favor of Topa after Haering unsuccessfully moved for summary judgment. In undertaking its review, the appellate court noted that the requirement in Insurance Code § 11580.2(a)(1) that auto policies contain UIM coverage does not apply to excess policies. Consequently, Haering's right to UIM coverage from Topa depended entirely on whether the Topa policy provided such coverage.

In teeing up its findings, the court distinguished first and third party coverages, and stressed that UIM coverage is a form of first party coverage, explaining that: "[A] first party insurance policy provides coverage for loss or damage sustained directly by the insured …. A third party liability policy, in contrast, provides coverage for liability of the insured to a 'third party' …. In the usual first party policy, the insurer promises to pay money to the insured upon the happening of an event, the risk of which has been insured against. In the typical third party liability policy, the carrier assumes a contractual duty to pay judgments the insured becomes legally obligated to pay as damages because of bodily injury or property damage caused by the insured." In finding that UIM coverage is "strictly" first party' coverages, the court focused on the fact that "the insurer's duty is to compensate its own insured for his or her losses, rather than to indemnify against liability claims from others."

In discussing "following form" excess insurance and how courts resolve inconsistencies between the language of the primary and the excess policy, the court clarified that a "following form" excess policy incorporates by reference the terms and conditions of the underlying primary policy and generally will contain the same basic provisions as the underlying policy, with the exception of those provisions that are inconsistent with the excess policy. Any inconsistency or conflict between the provisions of a following form excess policy and the provisions of an underlying primary policy is resolved by applying the provisions of the excess policy. "It is well settled that the obligations of following form excess insurers are defined by the language of the underlying policies, except to the extent that there is a conflict between the two policies, in which case, absent excess policy language to the contrary, the wording of the excess policy will control." Applying the provisions of the Topa policy, the court found that the Topa policy did not incorporate the UIM provisions in State National's policy. Since the Topa policy covered only "the sum paid in settlement of losses for which the Insured is liable," it covered only liability claims against the insured. Moreover, the Topa policy language incorporating the provisions of the primary policy was subject to an exception for "any other provisions therein which are inconsistent with the provisions of this policy," and the "following form" provision of the Topa policy stated that it would follow the form of the primary policy "subject to the terms, conditions and limitations of all other provisions of this policy." Additionally, the Topa policy did not include a "broad as primary" endorsement, which expressly includes coverage for losses within the scope of the underlying primary policy, even though the loss would otherwise have been excluded under the terms of the excess policy.

CALIFORNIA PUBLIC POLICY PRECLUDES ENFORCEMENT OF AN "OTHER INSURANCE" CLAUSE TO PRECLUDE AN INSURER'S EFFORTS TO ESCAPE ITS DUTY TO DEFEND. [Filed March 11, 2016]

In the case styled Certain Underwriters at Lloyds, London v. Arch Specialty Insurance Co. (2016) 246 Cal.App.4th 418, 200 Cal. Rptr.3d 786, the Court of Appeal, Third District, held that California public policy precluded an insurer that provided primary liability coverage for a later period from enforcing "other insurance" language limiting the duty to defend to situations where no other primary insurer afforded a defense, and thus the "other insurance" language did not bar an earlier primary insurer's claim for equitable contribution, since the language amounted to an improper "escape clause," even though the later insurer included the "other insurance" language in both the "coverage" section of the policy and the "limitations" section.

Underwriters at Lloyds, London (**"Underwriters"**), and Arch Specialty Insurance Company (**"Arch"**), issued successive commercial general liability (**"CGL"**) policies to Framecon, a carpentry and framing subcontractor. Underwriters' policies covered the period from October 28, 2000 to October 28, 2002. Arch's policy covered October 28, 2002, to October 28, 2003. Both insurers' policies named KB Homes, a residential developer with which Framecon contracted to provide carpentry and framing services, as an additional insured.

Purchasers of homes from KB Homes sued KB Homes for construction defects, some of which were attributable to Framecon's work. KB Homes filed a cross-complaint against Framecon and both Framecon and KB Homes sought a defense from both Underwriters and Arch under the Framecon policies. Although

both insurers acknowledged their obligations to indemnify against liability in the lawsuits, only Underwriters agreed to provide a defense. Arch took the position that its policy excused it from defending when another insurer is providing a defense. Arch relied on language in its policy's "Insuring Agreement" limiting Arch's duty to defend to lawsuits in which "no other insurance affording a defense against such a suit is available to you." Arch further relied on language in its policy's "Conditions" section stating that Arch would have no duty to defend "any claim or suit that any other insurer has a duty to defend."

After the construction defect lawsuits were settled, with Underwriters and Arch contributing a pro rata share based on "time on the risk," Underwriters sued Arch for declaratory relief and equitable contribution to defense costs. On cross-motions for summary judgment, the trial court ruled in favor of Arch. The trial court accepted Arch's position that the so-called "exclusive defense" provisions in its policy relieved it of a duty to defend if another insurance carrier has a duty to defend. The trial court reasoned that placing the "other insurance" clause in the "Insuring Agreement" portion of the insurance policy defining coverage, as opposed to merely placing it in the conditions/limitations portion of the contract, created an enforceable exception to coverage, rather than a disfavored escape clause in violation of public policy.

The appellate court reversed and remanded, reminding the trial court that equitable principles designed to accomplish ultimate justice, not the language of the relevant insurance contracts, governs contribution actions between insurers. The court equated the language in Arch's Insuring Agreement with an "escape" clause, which relieves a primary insurer of any obligation to provide coverage if another insurer provides primary coverage. In the court's view, the fact that Arch's escape language appeared in the Insuring Agreement, rather than the conditions section of the policy, did not justify excusing Arch from paying a share of Framecon's and KB Homes's defense costs. The court found nothing in the case law suggesting that the location of the other insurance clause matters. Indeed, the court criticized undue reliance upon the location of the other insurance language, as "tend[ing] to encourage insurers to jockey for best position in choosing where to locate other insurance language, needlessly complicating the drafting of policies, inducing wasteful litigation among insurers, and delaying settlements—all ultimately to the detriment of the insurance-buying public."

DESPITE A CGL CARRIER PROSECUTING IN THE NAME OF ITS INSURED DEVELOPER AN INDEMNITY ACTION AGAINST A SUBCONTRACTOR FOR THE REIMBURSEMENT OF DEFENSE FEES AND COST, THE DEVELOPER'S CARRIER WAS THE REAL PARTY IN INTEREST AND COULD NOT AVOID LIABILITY FOR THE SUBCONTRACTOR'S CONTRACTUAL ATTORNEY'S FEES WHEN THE SUBCONTRACTOR DEFEATED THE REIMBURSEMENT CLAIM. [Filed May 2, 2016]

In the case styled Hearn Pacific Corporation v. Second Generation Roofing Inc. (2016) --- Cal.App.4th ---, --- Cal. Rptr.3d ----, 16 Cal. Daily Op. Serv. 4637, 2016 WL 1757290, the Court of Appeal, First District, held that a claim for equitable contribution may be asserted by multiple insurers of the same insured and the same risk, each of which has an independent standing to assert a right for equitable contribution when it has undertaken the defense or indemnification of their common insured though this right is not the equivalent of standing in the shoes of the insured.

Hearn Pacific Corporation (**"Hearn"**) was a general contractor on a project in Sonoma County for the construction of a mixed-use building. In 2007, the project's owner brought suit for design and construction defects against multiple parties, including Hearn and Second Generation Roofing, Inc. (**"Second Generation"**). Hearn cross-complained against Second Generation and other subcontractors, alleging causes of action for breach of contract, professional negligence, express indemnity, implied indemnity, equitable indemnity, breach of warranties, comparative negligence and contribution.

Two years later Hearn executed an agreement assigning its rights and interests under its subcontracts to two insurers, including North American Specialty Insurance Company (**"North American"**). Thereafter, Hearn settled with the plaintiff and all but two subcontractors, one of which was Second Generation. Later in the case, one of Hearn's attorneys filed a declaration in support of a motion for summary adjudication stating that, "Hearn's defending insurers are suing in Hearn's name as transferees of Hearn's contractual indemnity rights, including the right to obtain equitable contribution for defense costs incurred herein from co-indemnitors such as Second Generation Roofing, Inc."

Eventually the litigation terminated successfully in Second Generation's favor, with dismissal of the cross-complaint against it on procedural grounds. In the same order, the trial court awarded it $30,256.79 in costs and granted a motion for attorney fees pursuant to a prevailing party attorney fee clause contained in the subcontract. The trial court entered a later order awarding attorney fees in the amount of $179,119. Second Generation then moved under both Code of Civil Procedure §§ 187 and 368.5, and pursuant to the trial court's inherent powers, to amend both orders to name one of Hearn's two insurers, North American, as a judgment debtor owing the amounts awarded against Hearn.

The appellate court found that Second Generation had a liquidated right — adjudicated by the trial court's order — to collect its attorney fees and costs as a prevailing party. It is, reasoned the court, an abuse of discretion to refuse Second Generation's request to add the name of the real party in interest, Hearn's assignee, who pressed claims in the name of the party nominally adjudged liable by those orders. That relief is consistent with the law governing contractual attorney fees. Had Hearn's insurer exercised its right to formally substitute in as the real party in interest, rather than remain on the sidelines and sue in Hearn's name, it could have been held directly liable for Second Generation's prevailing party attorney fees under the subcontract, as an assignee. That is because an assignee's acceptance of the benefits of a contract containing an attorney fees clause, by bringing suit, constitutes an implied assumption of the attorney fee obligations, unless there is evidence the parties did not intend to transfer those fee obligations. And that is true even if, like here, there is only a partial assignment of contractual rights. Indeed, even outside the attorney fee context, an assignee's voluntary acceptance of the benefits of a contract may obligate the assignee to assume its obligations as a matter of law, even if the assignment agreement expressly excludes the obligations. Hearn's insurer – North American – cannot evade responsibility for paying Second Generation's costs and legal fees solely because of its tactical choice to keep Hearn's name, not its own, on the case caption. Concluded the appellate court, "We do not think the discretion afforded a trial court to continue an action in the transferor's name under [CCP] section 368.5 was meant as a get-out-of-jail-free card, to insulate the real party in interest from exposure to liability for costs and fees when the litigation they pursue concludes unfavorably. ◆