Insurer Learns It Can't Wriggle Out of Its Duty to Defend

Focus Column

By Daniel Lee Jacobson

The words used in the law are sometimes clear in meaning, yet confusing in sound. But not always.

The first two words of a recent decision were all that an insurance company seeking to avoid its obligations needed to hear: "No dice." *The Standard Fire Insurance Co. v. The Spectrum Community Association,* 141 Cal.App.4th 1117 (2006).

The case was a declaratory relief action filed by the insurer of developers of a condominium project in which a key question was whether an "occurrence" had taken place during an insurance policy period.

The developers had been sued by the development's Home Owners' Association for damages allegedly caused by defective construction. The developers tendered defense of the lawsuit to Standard under an occurrence-based policy during construction. The trial court found for Standard, and an appeal followed.

An occurrence-based policy protects only against damage that is caused by an occurrence taking place during the policy period. *Montrose Chemical Corp. of California v. Admiral Insurance Co.,* 10 Cal. 645 (1995) (*Montrose II*). Standard's policy defined an occurrence as "an accident, including continuous or repeated exposure to substantially the same general harmful conditions."

Because an HOA cannot exist before a condominium complex is constructed, Standard argued that whatever may have occurred during the policy period could not have resulted in damage to the then-nonexistent HOA. Standard also argued that the HOA did not own a cause of action resulting from anything that happened during the Standard policy.

But, the developers prevailed by arguing that whether the HOA owned the property or even existed during the Standard policy period was irrelevant. What mattered was that damage was alleged to have occurred during the policy period. The court also rejected Standard's argument that the HOA could not own a cause of action based on anything that happened before it was formed.

The battle over whether an occurrence took place during the Standard policy period turned on whether a complaining third party is allegedly damaged during the policy period, or whether there is any alleged damage during the policy period.

In arguing that the concentration should be on the complaining party, Standard cited *Remmer v. Glenn Falls Indemnity,* 140 Cal.App.2d 84 (1956), which holds that occurrence happens "when the complaining party was actually damaged." But, the court suggested that this bare quotation is misleading because the damages still must have occurred during the policy.

In *Montrose II,* the Supreme Court cited *Remmer* for the proposition that, "California courts have long recognized that coverage in the context of a liability insurance policy is established at the time the complaining party was actually damaged." But *Montrose II* still affirmed that "the standardized CGL policy language . . . coverage is triggered by damage or injury occurring during the policy period."

Montrose II did not involve a complaining party that did not exist when the

property damage occurred, but *Garriott Crop Dusting v. Superior Court,* 221 Cal.App.3d 783 (1990), did. That case involved a change of ownership between the time of the damage and the time that the complaining third party suffered from that damage. The *Garriott* court explained, "The *Remmer* court could refer to damage to 'the complaining party' instead of damage to 'the property' because the complaining party owned the property throughout all relevant time periods. Taking the *Remmer* opinion as a whole, the holding turns on when the property damage for which relief was sought occurred."

The *Standard* court also discussed at length whether the HOA owned a right to sue the developers at all. It analyzed several cases that dealt with who owns the right to sue in tort for construction defects when there has been a change of ownership of the property. While there are different rules stated in different cases, the differences in those rules appear to have been fact-driven. For example in *Siegel v. Anderson Homes*, Inc. 118 Cal.App.4th 994 (2004), the court ruled, "The answer seems to be that the cause of action belongs to the owner who first discovered, or ought to have discovered, the property damage."

But, in finding that the HOA did have a right to sue the developers, the *Standard* court hung its hat on certain statutory provisions regarding standing, as explained in *Orange Grove Terrace Assn. v. Bryant Properties,* 176 Cal.App.3d 1217 (1986), and *Windham at Carmel Mountain Ranch Assn. v. Superior Court,* 109 Cal.App.4th 1162 (2003).

In any event, the *Standard* court probably did not need to decide whether the HOA owned a cause of action against the developer. Once the court found that a defense was owed under the facts as alleged, didn't the insurer owe a defense?

Generally speaking, an insurance policy imposes on an insurer the duties to indemnify and defend. The duty to defend is broader than the duty to indemnify, and it exists whenever a third party seeks damages for which the insurer potentially owes indemnification. *Gray v. Zurich Ins. Co*., 65 Cal.2d 263 (1965).

In *Montrose Chemical Corp. v. Superior Court*, 6 Cal.4th 287 (1993) (*Montrose I*), the Supreme Court said that an insurer "must defend in some lawsuits where liability under the policy ultimately fails to materialize." *In A-H Plating Inc. v. American National Fire Insurance Co.*, 57 Cal.App.4th 427 (1997), the court said, "The duty to defend does not evaporate simply because the insurer has decided that the insured will ultimately be exonerated. ... In short, an insurer's determination that an insured is not liable on a third party claim does not provide a basis for escaping the duty to defend. That duty extends to those insureds whom the insurer believes to be innocent of the conduct alleged in the third party complaint." So, when dealing with an occurrence-based insurance policy, damage that happened during the policy period, and an insurer who had the ability to assess its risks, can an insurer not defend its insured? The not-so-pedantic, yet powerful legal answer is now, "No dice."

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