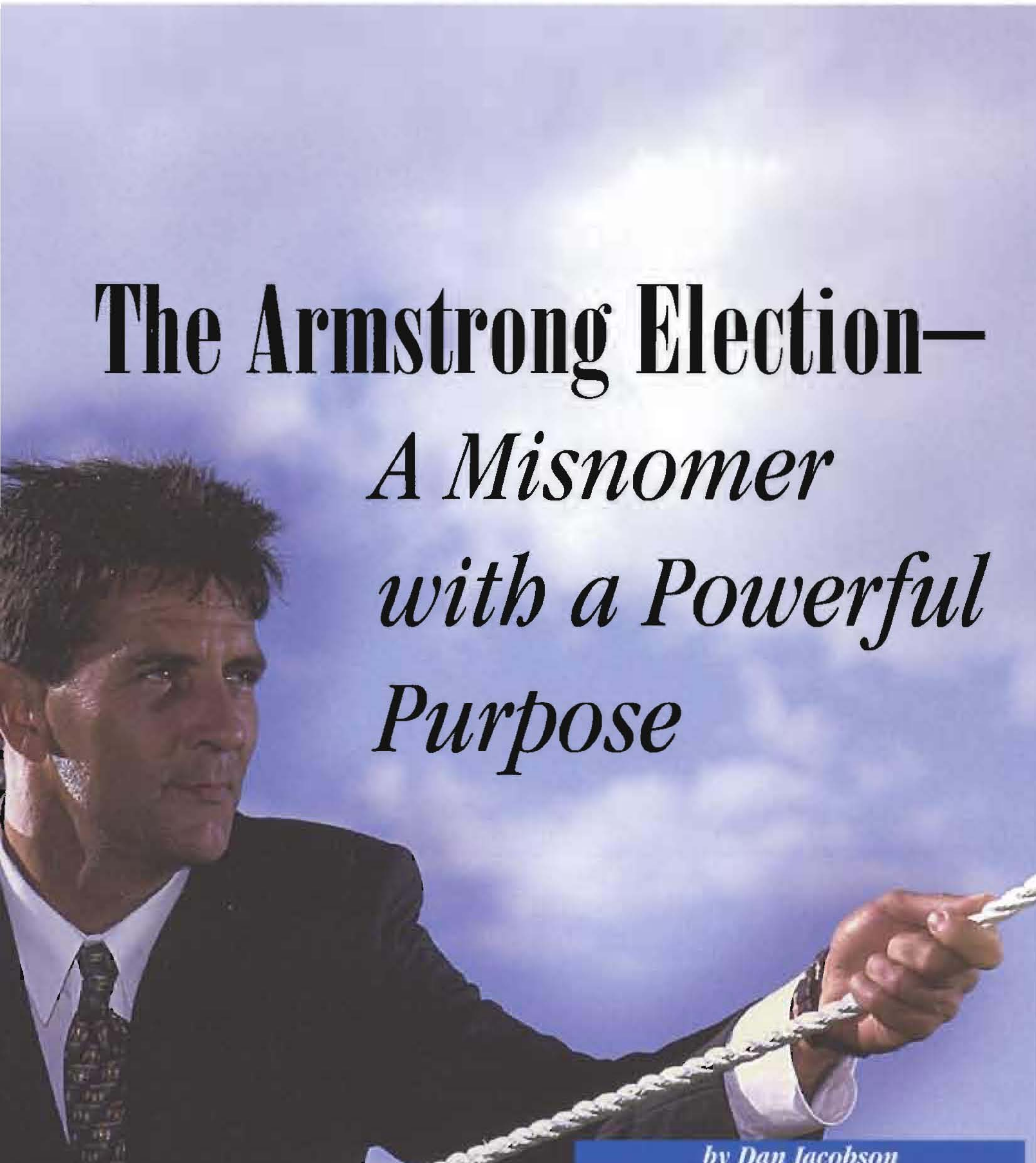

The Armstrong Election—

A Misnomer with a Powerful Purpose

by Dan Jacobson

When Christopher Columbus came to America, he thought that he had reached India. So, he called America's inhabitants "Indians." To this day Native Americans are known as Indians, even though everyone knows that Native Americans are from America, not India. As an adult, have you ever met a friend of your parents who you originally met as a child? Try calling Mr. Jones "John." It's tough. Once a name is imprinted in our minds, it's just hard to change that imprint. With that in mind, this article will point out a misnomer, without attempting to it. However, it is hoped that recognition of the misnomer will lead to a better understanding of the procedure that bears the poor moniker.

As will be seen, when an insured is sued for progressively deteriorating damages that span more than one year of insurance coverage, all of the relevant insurers must cover the insured, but the insured can choose which deductible to pay. That choice is misnamed an "*Armstrong* election."

You see, *Armstrong World Industries v. Aetna Casualty*, 45 Cal.App. 4th 1 (1996) dealt with the choice of which policy limits an insured chose to invoke, and had nothing to do with an insured's choice of a deductible. *Armstrong* at 49–50. Indeed, when an insured chooses which policy limits to invoke, the use of the term "*Armstrong* election" is not a misnomer.

But, when an insured chooses which deductible to pay, the term "*Armstrong* election" only applies . . . because it applies, because its use is ingrained into the insurance world's nomenclature. It is *California Pacific Homes, Inc. v. Scottsdale Insurance Company*, 70 Cal.App.4th 1187 (1999) that dealt with which deductible the insured chooses to pay. *California Pacific Homes*, at 1190. (Note that the insurance policies at issue in *California Pacific* had self-insured retentions, colloquially known as "SIRs," as opposed to deductibles; however, for the purposes at hand, there is no difference between a SIR and a deductible. *See Black Diamond Asphalt v. Superior Court*, 114 Cal.App.4th 109 (2003) for a fuller understanding of SIRs.

The key to the *California Pacific Homes* opinion is its finding that "stacking" deductibles is illegal. *California Pacific Homes* at 1194–96. (*Armstrong* dealt with the illegality of stacking policy limits. *Armstrong*, at 50.)

In order to understand this, one should begin with *Montrose Chemical Co. v. Admiral Ins. Co.*, 10 Cal.4th 645 (1995). That case had to "determine whether four comprehensive general liability (CGL) policies issued by defendant [insurer] to plaintiff obligate[d] [that insurer to] defend [its insured] in lawsuits seeking damages for continuous or progressively deteriorating . . . damage that occurred during [] successive policy periods." (*Montrose*, at 654.) Six other insurers provided insurance during the time that the alleged progressively deteriorating damage potentially took place. (*See Montrose*, at 656.)

The Supreme Court answered its own issue, "In the case of successive policies, [ ] . . . damage that is continuous or progressively deteriorating throughout several policy periods is

Orange County Lawyer
09/11 Vol.53, No. 9

potentially covered by all policies in effect during those periods. Stated in the insurance industry's parlance, we conclude the 'continuous injury' trigger of coverage should be adopted for third party liability insurance cases involving continuous or progressively deteriorating losses." (*Montrose*, at 655.) Since an insurer "bears a duty to defend its insured whenever [the] facts . . . give rise to the *potential of liability* under the policy," *Gray v. Zurich Ins. Co.*, 65 Cal.2d 263, 276–77 [emphasis added], Montrose decided that all of the insurers on the risk during the time of the alleged progressively deteriorating loss must defend the insured.

Armstrong World Industries v. Aetna Casualty, 45 Cal.App. 4th 1 (1996) was a coverage dispute between asbestos manufacturers/installers and the various insurers who insured them over decades. In fact, the Armstrong company began installing asbestos-laden products in the 1940s. (*Armstrong*, at 64–65.) The election in Armstrong was not an election to which deductible to pay; but was rather an election to which policy limit would apply. (*Armstrong*, at 50.) The issue of which policy limit would apply probably arose because there was probably a big difference in policy lim-

Orange County Lawyer
09/11 Vol.53, No. 9

its over the numerous years of coverage.

As is required by *Montrose*, in *Armstrong* all of the insurers who had provided insurance over the years were on the risk, notwithstanding which policy limits the insured chose. "Once triggered, each policy covers an insured's liability." [Internal quotation marks removed.] (*Armstrong*, at 49.) Interestingly, *Armstrong* made clear that policy limits from more than one policy year of primary insurance (as opposed to excess insurance) cannot be "stacked." *Armstrong*, at 50, fn.15. So, if an insured has a policy limit of $500,000 for one policy year and $1,000,000 for another, that insured cannot claim $1,500,000 in policy limits. *California Pacific Homes*, 70 Cal.App.4th 1187 (1999) decided that horizontal, primary insurance deductibles cannot be "stacked." *California Pacific Homes*, at 1194–96.

California Pacific Homes was a coverage dispute that concerned a construction defect case wherein the insured (California Pacific Homes) was sued by the homeowners of a housing development built by the insured. (*California Pacific Homes*, at 1189.) Eleven years of coverage, during which the insured was covered by various insurers were at play. As is required by *Montrose*, in *California Pacific Homes* all of the insurers who had provided insurance over that 11–year period had to cover the insured. (*California Pacific Homes*, at 1190.) As mentioned, but bears re-mentioning, the key to the *California Pacific Homes* opinion is its finding that "stacking" deductibles is illegal.

California Pacific elected to pay only one SIR (deductible) to only one insurer for only one policy year. That one deductible was $250,000. Two of the insurers' balked, claiming that their insured was required to pay a deductible to each of them for each policy year. (*California Pacific Homes*, 1190.)

The Court of Appeal quoted and affirmed the trial court. "'[E]ach of the Defendant Insurers is and was obligated to indemnify California Pacific Homes for that portion of the [construction defect case] settlement that exceeds a single retained limit of $250,000.'" (*California Pacific Homes*, at 1193.) (As required by *Montrose*, the amount that the insurers had to pay included defense costs. *California Pacific Homes*, at 1190, fn.3.)

The Court explained the folly of the insurers' argument that their insured had to pay more than the one deductible that it elected to pay. "[The insurers] raise a 'strawperson' when they complain that [the insured] has simply lumped all [of the] policies issued by [the insurers] together and treated them as 'a single excess policy subject to one $250,000' [deductible] 'for the entire [relevant] period.' Their contention conflates several inquiries. . . . [S]uccessive insurers on the risk when continuous or progressively deteriorating property damage first manifests itself are separately and independently obligated to indemnify the insured." (*California Pacific Homes*, at 1194–95.)

It bears noting that the *California Pacific Homes'* insured tendered to all of its insurers for the relevant 11 year period. (*California Pacific Homes*, at 1190.) "How these insurers choose to proceed as between themselves is not before us." (*California Pacific Homes*, at 1195.)

"The insurers are in the anomalous position of arguing for stacking of the [deductibles]. Just as stacking of polic[y limits] may have the result of providing far more coverage than an insured has purchased, so stacking of [deductibles] would have the effect of affording an insured far less coverage for occurrencebased claims than the insured has purchased. (*See FMC Corp. v. Plaisted & Company,* [] 61 Cal.App.4th 1132, 1188–90.)" (*California Pacific Homes*, at 1194.)

And so, the crux of an *Armstrong* election to a deductible is affirmed—stacking of deductibles is prohibited. (*California Pacific Homes*, at 1194.) As the Division Three of the Fourth District Court of Appeal, sitting in Santa Ana said, "'[S]tacking' of [deductibles] in [multiple] triggered policies [is illegal] as this practice would furnish the insured far less coverage than it purchases." *Forecast Homes*, 181 Cal.App.4th 1466, 1474 (2010), *citing Montgomery Ward & Co. v. Imperial Casualty& Indemnity Co.*, 81 Cal.App.4th 356, 370 (2000).

It is important to note what an *Armstrong* election to a deductible is not. It is not a selection of which insurer will defend the insured; and, it is not a selection of which insurer will indemnify the insured. All insurers on the risk during the time when progressively deteriorating damages took place must indemnify their insured. (*Montrose*, at 655.) The duty to defend arises when there is a potential for indemnity. (*Montrose*, at 660, fn.9.) Since generally it is unknown when progressively deteriorating damages actually occur, there is the potential that such occur during any of the policy years when the condition that caused those damages existed. (From when the asbestos was first placed, from when construction of the allegedly defective house began, etc. *See Montrose*, at 677–78, *citing Gruol Construction v. Insurance Co. of North America*, 11 Wn.App. 632 (1974).)

In fact, in *Montrose*, *Armstrong*, and *California Pacific Homes* all of the insurers were all required to defend their insureds.

So, an insured is allowed to make a misnamed "*Armstrong* election" to which deductible it will pay when it is sued for progressively deteriorating damages that span more than one policy year. That election only defines which deductible the insured will pay; all of the insurers on the risk during the time when any of the damages potentially occurred must defend the insured, notwithstanding which deductible the insured chooses to pay.

Dan Jacobson is an attorney in Tustin, and a professor at Pacific West College of Law.