INSURERS CAN'T ESCAPE THROUGH AN ESCAPE CLAUSE

by DAN JACOBSON

Insurance policies often have "other insurance" clauses, which purport to excuse the insurer from defending or indemnifying an insured who is a defendant in a lawsuit if the insured has any other insurance that covers the risks involved in the lawsuit. Recently, Division One of the Fourth District Court of Appeal ruled that such a clause is unenforceable as written, and instead requires the insurance companies to share the defense and indemnification on a *pro rata* basis.

In *Underwriters of Interest v. Probuilders Specialty Ins.*, 241 Cal. App. 4th 721 (2015), both Underwriters and Probuilders insured Pacific Trades Construction & Development for the same risks. There was at least the potential for coverage of those risks in an underlying construction defect lawsuit brought against Pacific Trades. Thus, on the face of things, both insurers owed Pacific Trades a defense. *See Waller v. Truck Ins. Exch., Inc.*, 11 Cal. 4th 1, 19 (1995) ("[A]n insurer has a duty to defend an insured . . . if [there are] . . . facts [alleged in a lawsuit] giving rise to the potential for coverage under the insuring agreement").

Because of the potential for coverage, Underwriters defended Pacific Trades in the underlying case; ProBuilders did not. After the underlying case was settled, Underwriters sued ProBuilders for equitable contribution, claiming that it was owed reimbursement for some of the costs of defending Pacific Trades. "'[T]he right to contribution arises when several insurers are obligated to indemnify or defend the same loss or claim, and one insurer has paid more than its share of the loss or defen[se].'" *Underwriters*, 241 Cal. App. 4th at 728 (quoting *Fireman's Fund v. Maryland Cas. Co.*, 65 Cal. App. 4th 1279, 1293 (1998)). ProBuilders' defense was that it had an "other insurance" clause in its Pacific Trades policy.

That "other insurance" clause was one that is commonly contained in Commercial General Liability insurance policies. It said that ProBuilders had "the right and duty to defend [Pacific Trades] against any suit seeking . . . damages [to which the insurance applied] provided that no other insurance affording a defense against such a suit is available to you." *Id.* at 729 (emphasis omitted). The court cited and adopted the classifications of "other insurance" clauses that were denominated in *Olympic Ins. Co. v. Employers Surplus Lines Ins. Co.*, 126 Cal. App. 3d 593, 598 (1981). The *Olympic Ins.* court said that "other insurance" clauses are generally classified as:

> [T]he issue of "other insurance" clauses is one that can severely affect insurance consumers . . . .

1. *Pro rata*. This clause provides that if there is other valid and collectible insurance, then the insurer shall not be liable for more than his *pro rata* share of the loss.
2. Excess. This clause provides that if there is other valid and collectible insurance, then the insurer shall not be liable except to the extent that the loss exceeds such other valid and collectible insurance (*i.e.*, this policy shall be excess to other valid and collectible insurance.)
3. Escape. This clause provides that *the insurer is not liable for any loss that*

is covered by other insurance (*i.e., the existence of other insurance extinguishes insurer's liability to the extent of such other insurance.*)

Id. at 730 n.5 (emphasis in original).

ProBuilders' "other insurance" clause was an escape clause. *Id.* at 729-30. "The courts have repeatedly addressed—and rejected—arguments by insurers that an 'other insurance' clause in their insuring agreement permitted them to evade their obligations by shifting the entire burden associated with defending and indemnifying a mutual insured onto a coinsurer." *Id.* at 730. Yet insurers have just as insistently continued to put escape clauses in their policies. In 2002, the California Supreme Court admonished insurers as follows:

> "[O]ther insurance clauses" that attempt to shift the burden away from one primary insurer wholly or largely to other insurers have been the objects of judicial distrust. Public policy disfavors "escape" clauses, whereby coverage purports to evaporate in the presence of other insurance. Partly for this reason, the modern trend is to require equitable contributions on a *pro rata* basis from all primary insurers regardless of the type of "other insurance" clause in their policies.

Id. at 730 (quoting *Dart Industries v. Commercial Union Ins. Co.*, 28 Cal. 4th 1059, 1079-80 (2002) (quotation marks, citations, and brackets omitted).

ON TOPIC
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If in 2002 the California Supreme Court warned insurers that their escape clauses were not trusted by the courts, were disfavored by public policy, and were probably not enforceable, then why was the insurance industry still using and defending those clauses thirteen years later, in *Underwriters*?

The answer is axiomatic and unflattering. At least portions of the property/casualty insurance industry are, to say the least, *slow* to follow the law. The Supreme Court's *Dart Industry*'s decision was not the first—or even close to the first—California opinion that told the insurance industry to straighten up when it came to their onerous "other insurance" clauses. Consider the numerous cases cited by the *Underwriters* court where the courts would not enforce escape clauses, or even excess clauses, as written. They date back to the 1990s, and one as far back as 1956: *Commerce & Indus. Ins. Co. v. Chubb Custom Ins. Co.*, 75 Cal. App. 4th 739, 744 (1999) (insurer with "escape" clause required to contribute to loss); *Travelers v. Century Surety Co.*, 118 Cal. App. 4th 1156 (2004) (insurer with purported "excess" clause required to contribute to defense and settlement costs); *Century Surety Co. v. United Pacific Ins. Co.*, 109 Cal. App. 4th 1246 (2003) (same); *Fireman's Fund v. Maryland Cas. Co.*, 65 Cal. App. 4th 1279 (1998) (same); *CSE Ins. Group v. Northbrook Prop. & Cas. Co.*, 23 Cal. App. 4th 1839 (1994) (same); *Peerless Cas. Co. v. Cont'l Cas. Co.*, 144 Cal. App. 2d 617 (1956) (insurer with hybrid escape/excess clause required to contribute). *Underwriters*, 241 Cal. App. 4th at 730-31.

Whereas *Underwriters* was set in an equitable contribution battle between two insurers, the issue of "other insurance" clauses is one that can severely affect insurance consumers, also. Certain types of cases naturally lend themselves to more than one insurer having potential liability, and thus lend themselves to the requirement that the insurers defend their insureds. *See Waller v. Truck Ins. Exch., Inc.*, 11 Cal. 4th 1, 19 (1995).

Take the construction defect case that was the underlying case in *Underwriters*, for example. Without appropriate policy language to the contrary, "successive insurers on the risk when continuous or progressively deteriorating property damage first manifests are separately and independently obligated to indemnify the insured." *California Pacific Homes*, 70 Cal. App. 4th 1187 (1999). By their nature, construction defect damages are usually "continuous or progressively deteriorating damages." So, an insured could get the strength of two, three, or even more insurers to defend and indemnify it in a construction defect case, or in another case where the allegation is of "continuous or progressively deteriorating property damage." (But, the insured has to make sure to make an appropriate *Armstrong* election in order to avoid multiple deductibles. *See* The *Armstrong* Election: A Misnomer with a Powerful Purpose, *Orange County Lawyer*, Sept. 2011, Vol. 53, No. 9, p. 16).

In a strong judicial slap to ProBuilders, the *Underwriters* court found, "ProBuilders largely disregards the numerous cases, cited [by the *Underwriters* court], which have upheld the defending insurer's right to seek equitable contribution from a noncontributing primary insurer notwithstanding an escape clause in the noncontributing primary insurer's policy." *Underwriters*, 241 Cal. App. 4th at 732. Instead, ProBuilders pushed three cases, all of which the *Underwriters* court quickly dispatched as being off-point.

At *Travelers Cas. & Surety Co. v. American Equity Ins. Co.*, 93 Cal. App. 4th 1142, 1149 (2001) the court said that "the language of excess 'other insurance' clauses [will generally be honored.]" But, *Underwriters* found this language to be dicta in light of the fact that the *Travelers* court went on to uphold the equitable contribution claim against the non-contributing insurer. *Underwriters*, 241 Cal. App. 4th at 733. ProBuilders cited *Nabisco v. Transport Indemnity Co.*, 143 Cal. App. 3d 831 (1983), but *Underwriters* quickly shot that citation down because, "the plaintiff [in *Nabisco*] had expressly contracted with the insurer to provide an umbrella policy that would have been triggered only after the plaintiff satisfied its self-insured retention, and the court merely enforced the terms of the policy for which the plaintiff had knowingly contracted." *Underwriters*, 241 Cal. App. 4th at 733. "The final case quoted by ProBuilders, *Hartford Cas. Ins. Co. v. Travelers Indemnity Co.*, . . . appears to have involved such peculiar facts and specialized endorsements that it provides little guidance." *Id.*

The *Underwriters* court sided with what appears to be the vast majority, if not all, of on-point cases, and went with what the California Supreme Court called the "modern trend" in *Dart Industries*. Citing *Dart Industries*, the *Underwriters* court decided that the law is to require "equitable contributions on a *pro rata* basis from all primary insurers regardless of the type of 'other insurance' clause in their policies." *Id.* at 731. Thus, property/casualty insurance companies are again being told, when it comes to "other insurance" clauses that are escape clauses, or even excess clauses if the insurer is found to be a "primary insurer," knock it off! Your "other insurance" policy will result in a *pro rata* sharing of the costs owed under the policy.

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