

BINDING AUTHORITY

Insurance Coverage Decisions: Issued Today - Impact Tomorrow



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Note: For those that follow Pennsylvania construction defect, see bottom for word about a just-issued Pennsylvania coverage decision that addresses *Gambone*.

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Next Stop for *Buss*: California Appeals Court Addresses Coverage for Attorney's Fees Awarded for the Recovery of Uncovered Damages

Decision a Thriller for Insurers and Off the Wall for Policyholders

For just about everyone, Jerry Buss's claim to fame is that he invented The Laker Girls. Of course, we insurance types all know better.

Buss's real legacy is that his case against Transamerica Insurance Company -- seeking coverage for a defamation claim, in conjunction with multiple non-covered counts surrounding an advertising dispute -- gave rise to the Supreme Court of California's decision granting an insurer the right to seek reimbursement of defense costs for uncovered claims. In other words, in a so-called "mixed" action, in which some claims are potentially covered and others are not -- thereby triggering a duty to defend the action in its entirety -- the court held that an insurer may seek reimbursement of defense costs for claims that are not potentially covered.

By the way, ordinarily I am a big fan of Wikipedia. But having just read Mr. Buss's Wikipedia entry, and seeing no mention whatsoever of *Jerry Buss v. Transamerica Ins. Co.*, 939 P.2d 766 (Cal. 1997), the site just slipped several notches in my book.

Since *Buss* was decided in 1997, its reach has been tested by California courts, and it is a frequent go-to decision for courts in other states that are confronted with the question of reimbursement of defense costs for uncovered claims. Many states resolve this issue by examining *Buss* and deciding if they want to jump on board.

In general, courts that reject reimbursement of defense costs see it as inconsistent with their state's long-standing broad duty to defend rules. And courts that allow reimbursement have developed rationales to support their decisions. Reimbursement of defense costs has become a classic "Two Schools of Thought" coverage issue -- e.g., late notice: prejudice required or not; pollution exclusion: applies solely to traditional pollution or not, etc.

In general, insurers have been winning a few more of the reimbursement cases than they've been losing. The score is close. But even when insurers succeed in establishing that the right to reimbursement exists, they sometimes find that practical problems associated with the implementation of this right diminish its actual value. Thus, in some cases, an insurer's right to reimbursement of defense costs has more bark than bite. For much more on the debate over reimbursement of defense costs, and some practical problems associated with it, click here :

<http://www.whiteandwilliams.com/CM/Publications/CS%20Public%20Liab.pdf>

Yesterday the California Court of Appeal issued a published opinion in *State Farm v. Mintarsih*. The decision presented another opportunity for a California court to examine the reach the *Buss*. At issue, does *Buss* apply to preclude coverage for attorney's fees awarded to an underlying plaintiff if such fees are associated with the recovery of damages for which no coverage is owed?

Mintarsih involved coverage under a State Farm homeowners and personal umbrella policy for a claim brought by a domestic servant against her employers – State Farm’s insureds. The plaintiff alleged claims for, among other things, false imprisonment and wage and hour violations under the Labor Code. A jury awarded \$87,000 for false imprisonment and other common law claims. The jury also awarded damages and penalties under the Labor Code in the amount of \$745,000. Then, as a prevailing party under the Labor Code for the wage and hour claims, the court awarded the plaintiff \$733,000 in attorney’s fees and \$161,000 in other costs.

The plaintiff, as an assignee under the policy, conceded that State Farm had no obligation to indemnify for the amounts awarded for wage and hour violations. However, the plaintiff argued that State Farm was nonetheless obligated to pay the attorney’s fees awarded as costs, even though the right to recover such fees arose from a claim for which there was no coverage under the policies (the wage and hour claims).

The California Court of Appeal disagreed. While the opinion is detailed, and has a lot to say about *Buss* in driving toward at its destination, the long and short of the decision is as follows:

Accordingly, we conclude that the *contractual* obligation to pay costs awarded against an insured arises only if there is a contractual duty to defend. The contractual duty to defend extends only to those claims for which there is at least potential coverage under the policy, as we have stated. An insurer has no contractual duty to defend the insured as to claims that are not even potentially covered. (*Buss, supra*, 16 Cal. 4th at p. 51.)

An insurer’s implied-in-law duty to defend an entire “mixed” action, including claims that are not even potentially covered, does not give rise to an obligation under a supplemental payments provision to pay costs awarded against the insured that can be attributed solely to claims that were not potentially covered. This is because the duty to defend claims in a “mixed” action that are not potentially covered is not a contractual duty, and the reference in the supplemental payments provision to “suits we defend” encompasses only those claims that the insurer agreed to defend under the terms of the policy. Just as an insured could not reasonably expect to retain the benefit of an insurer’s payment of defense costs that can be allocated solely to claims that were not even potentially covered (*Buss, supra*, 16 Cal.4th at pp. 51, 53), an insured could not reasonably expect an insurer to pay costs that can be allocated solely to claims that were not even potentially covered. Attorneys fees awarded as costs against the insured can be allocated solely to claims that were not even potentially covered if (1) the fees were incurred *solely* to defend against claims that were not even potentially covered or (2) the right to recover fees arose *solely* from claims that were not even potentially covered.

Mintarsih at 14-15 (emphasis in original).

While the rationale for yesterday’s California Court of Appeal decision was clearly tied to *Buss*, a court can nonetheless follow the lead of *Mintarsih*, and preclude coverage for attorney’s fees awarded to an underlying plaintiff, where such fees are associated with the recovery of damages for which no coverage is owed, all the while not limiting the insured’s right to a complete defense for ongoing litigation – *i.e.*, the part about *Buss* that its opponents find objectionable. In other words, the decision is potentially significant because it may be persuasive even in states that have rejected *Buss*.

A copy of yesterday’s California Court of Appeal decision in *State Farm v. Mintarsih* can be accessed here:

<http://www.courtinfo.ca.gov/opinions/documents/B202888.PDF>

Gambone Update

On June 18, 2009 the Eastern District of PA issued an opinion that addressed coverage in the context of a very traditional residential construction water intrusion case (Homeowner v. General Contractor v. Window Subcontractor). The court found no coverage, based on *Gambone* and *Kvaerner* and the same rationale seen in other cases of late. Given that the decision broke no new ground on the *Gambone* issue, I did not make it the subject of a *Binding Authority* issue. If

you'd like a copy of this new E.D. PA *Gambone* decision, just send me an e-mail and I'll be

happy to pass it along.

Please let me know if you have any questions.

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