INSURANCE LAW

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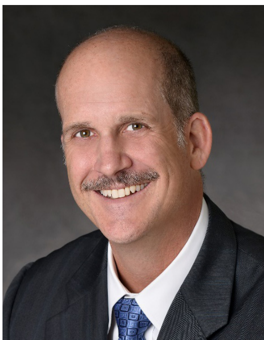

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INTRODUCTION

In 2022, the pendulum of insurance jurisprudence definitely swung in favor of insurance companies. While the year's only California Supreme Court case, regarding personal injury coverage for Telephone Consumer Protection Act ("TCPA) suits, was technically a win for the policyholder, it narrowly rested on a manuscript endorsement, as well as the reasonable expectations of the parties. Meanwhile, the Court of Appeal upheld the denial of a defense under a habitability exclusion in a decision which has the potential to seriously undermine the defense of mixed actions alleging both covered and uncovered claims. Another Court of Appeal rejected coverage for the accidental levelling of land and trees on a neighbor's property, declining to expand the definition of occurrence in Commercial General Liability ("CGL") policies. On the first party side, claims for business interruption due to COVID largely continued to be resolved against policyholders, although a line of cases developed declining to do so at the pleading stage. Whether the winning streak in favor of insurance companies represents a new trend in California law, or merely an aberration, remains to be seen.

THIRD PARTY POLICIES

DO CGL POLICY'S PERSONAL INJURY OR ADVERTISING INJURY PROVISIONS PROVIDE COVERAGE FOR TCPA CLAIMS? MAYBE.

Coverage lawyers were closely watching *Yahoo Inc. v. National Union Fire Insurance Co. of Pittsburgh, PA*[1] for guidance about coverage under a CGL policy for claimed violations of the Telephone Consumer Protection Act that restricts robocalls and junk faxes. Large companies are frequent targets of TCPA suits, and had hoped the Supreme Court would rule in favor of Yahoo!'s claims for coverage–though its policy was a standard National Union CGL policy with a number of negotiated endorsements that could limit the applicability of the Court's holding. While the Court's ruling was technically in Yahoo!'s favor, it was of limited benefit to Yahoo! and even less to policyholders (or carriers, for that matter) looking for authority to support their position.

Yahoo! tendered class action claims for unsolicited text messages to National Union, and after the carrier denied defense and indemnity, Yahoo! sued in federal court. The District Court granted National Union's motion to dismiss and Yahoo! appealed. The Ninth Circuit certified a question of state

law to the California Supreme Court that the Court rephrased as follows:

> Does a commercial general liability insurance policy that provides coverage for 'personal injury,' defined as 'injury . . . arising out of . . . [o]ral or written publication, in any manner, of material that violates a person's right of privacy,' and that has been modified by endorsement with regard to advertising injuries, trigger the insurer's duty to defend the insured against a claim that the insured violated the [TCPA] of 1991 (47 U.S.C. § 227) by sending unsolicited text message advertisements that did not reveal any private information?[2]

Claims for TCPA coverage typically rest on CGL provisions covering "personal and advertising injury," which often includes injury arising from "oral or written publication, in any manner, of material that violates a person's right of privacy."[3] The standard policy excludes injuries arising from TCPA violations, but Yahoo! had in its policy a manuscript Endorsement No. 1 that removed the TCPA exclusion. Endorsement No. 1 also excluded coverage for advertising injuries ("oral or written publication, in any manner, of material in your 'advertisement' that violates a person's right of privacy") but retained it for personal injury arising from "oral or written publication, in any manner, of material that violates a person's right of privacy."[4]

Yahoo! argued Endorsement No. 1 created a potential for coverage triggering National Union's duty to defend the TCPA class action claims. The District Court concluded the policy covered alleged violations of the privacy right of *secrecy*, involving the content of communication disclosing private personal information, but not violations of the right of *seclusion*, which occur when the means, manner, and method of communication disturb the recipient's seclusion. Because the "TCPA claims asserted against Yahoo! focused on the transmission of unsolicited text messages rather than the content of those messages, the federal district court dismissed Yahoo!'s insurance coverage action, entering judgment for National Union."[5]

The Supreme Court agreed that "if the policy at issue here does not cover liability for violations of the right of seclusion, then it does not cover Yahoo!'s potential TCPA liability in the underlying lawsuits."[6] Did it? After lengthy analysis, using standard rules of contract interpretation, the insured's reasonable expectations, and the rule of the last antecedent, the Court concluded National Union's policy did cover the TCPA claims against Yahoo!, "assuming such coverage is consistent with the insured's reasonable expectations."[7]

The Supreme Court considered whether coverage for injuries to the right of privacy was limited to those caused by the "material" the insured published or whether the coverage extended to injuries resulting from the act of publication. The Court found the policy was ambiguous on that point, so the answer depended on "Yahoo!'s objectively reasonable expectations, which must be determined in further litigation."[8]

While this may create a potential for coverage and a duty for National Union to defend Yahoo! against the TCPA claims, it is of limited value to other insurers or insureds with policies containing similar endorsements, because each of those insureds will have to establish its own expectations. Of course, because the Ninth Circuit couldn't "determine Yahoo!'s reasonable expectations and the parties [had] not briefed the issue, [it] remand[ed] for the district court to resolve it, as well as any other issues that arise, in the first instance."[9]

Grammar fans might enjoy the Court's discussion of the rule of the last antecedent (the "Rule"), according to which, "[r]elative and qualifying words and phrase, grammatically and legally, where no contrary intention appears, refer solely to the last antecedent."[10] While California courts have employed the Rule to hold that insurance policies with language similar to the one National Union sold to Yahoo! "cover only right-of-secrecy liability, and not right-of-seclusion liability,"[11] "the rule of the last

antecedent, as articulated in our case law, does not resolve the ambiguity in the policy language at issue here."[12]

So it's back to the trial court for Yahoo!, to gather and present evidence of its reasonable expectations of coverage. The Supreme Court's opinion may provide some guidance to other insureds with the market power and resources to negotiate a manuscript CGL policy without the TCPA exclusion, and to pay the premium for TCPA class action coverage. Helpful hint - make sure to document your expectations.

HABITABILITY EXCLUSION UPHELD EVEN IN THE FACE OF OTHERWISE COVERED CLAIMS

*24*th *& Hoffman Investors, LLC v. Northfield Ins. Co.*,[13] decided by the First District Court of Appeal, may turn out to be one of the most consequential insurance decisions of 2022. Read narrowly, *24*th *& Hoffman* cut off the right to a defense in a habitability case based solely on the specific language of the exclusion at issue in the underlying policy. However, in a broader sense, the case opens the door to insurance companies contracting around their obligation to otherwise defend "mixed" actions, those actions alleging both covered and uncovered claims.

The underlying dispute centered on a CGL policy issued by Northfield Insurance Company to 24th & Hoffman Investors, LLC, which owned an apartment complex. Two tenants alleged multiple habitability claims against the landlord, complaining of substandard conditions caused by renovations at the property, including construction debris and dust, as well as pest and vermin infestations. The tenants also alleged two claims that did not arise from the duty to provide habitable premises, namely, conversion and trespass to chattels, which were based on alleged damage to the plaintiffs' personal property stored in a locker at the complex caused by the landlord.

Northfield refused to defend the case based on its habitability exclusion, which excluded not only claims "arising out of the . . . actual or alleged violation of any federal, state or local law, code regulation, ordinance or rule relating to the habitability of any premises," but any causes of action "alleged in any claim or 'suit' that *also* alleges any violation, breach or wrongful eviction, entry or invasion as set forth . . . above."[14] Given the inclusion of non-habitability claims in the underlying complaint, the effect of the second "catch-all" clause was at the heart of the dispute.

After defending and settling the underlying case on its own, the landlord sued Northfield for wrongfully denying coverage. The trial court found that Northfield breached its duty to defend in light of the non-habitability claims. This was in accordance with the rule established by the California Supreme Court in *Buss v. Superior Court*,[15] that in a "mixed" action where some claims are potentially covered and others are not, the insurer must defend the entire action, subject to a right to partial reimbursement of defense costs following the conclusion of the case.

The Court of Appeal reversed, finding that Northfield had contracted out of the *Buss* rule by including clear language in its exclusion applying to any claims alleged in a suit that "also" included habitability claims. Since there were no other published California cases dealing with such language in a habitability exclusion, the court relied on *S.B.C.C., Inc. v. St. Paul Fire & Marine Ins. Co.*, which included similar catch-all language in an intellectual property exclusion, barring coverage for "any other injury or damage that's alleged in any claim which *also* alleges any such [intellectual property] infringement or violation."[16]

Recognizing the paucity of California cases on point, the court cited a number of federal district court decisions upholding exclusions with similar catch-all clauses, mostly involving intellectual property exclusions. The court also addressed two federal district court opinions which rejected the insurers' reliance on similar and–in one of the cases–identical catch-all exclusions.[17]

Reiterating the maxim that "an insurer is free to limit the risk it assumes by contract," the *24th & Hoffman* court found that none of the causes of action were potentially covered in light of the plain terms of the policy, which excluded all claims in a suit that alleges violations of the duty to provide a habitable premises.[18] According to the court, its conclusion did not run afoul of *Buss* because the habitability exclusion rendered *Buss* irrelevant, since none of the claims were potentially covered. The court recognized "the oddity of an insurance contract that covers certain claims against the insured if those claims are filed in a lawsuit of their own, and not if such claims are brought in a suit that also alleges habitability claims."[19] However, since that is what the clear language of the exclusion required in the court's view, that was its holding. The California Supreme Court denied review.

COURT OF APPEAL APPLIES ISSUE PRECLUSION BASED ON RULING OF DISTRICT COURT INSTEAD OF SUPREME COURT AUTHORITY ON NEGLIGENT HIRING TO FIND NO COVERAGE FOR THIRD-PARTY CLAIMS BECAUSE NO OCCURRENCE

The Thompsons owned property subject to a conservation easement held by Sonoma Land Trust ("SLT"). After the Thompsons' contractors did work on SLT's property, SLT sued the Thompsons, who tendered their defense to Burlington Insurance under their CGL policy. Burlington denied tender, taking the position that the claim did not arise from an occurrence. The Thompsons sued Burlington, which removed their action to federal court. The District Court awarded judgment to Burlington, and the Ninth Circuit affirmed. While the Thompsons' appeal was pending, they tendered defense to Crestbrook, which had issued a homeowners' policy covering damages "due to an occurrence," and Crestbrook also denied tender. The Thompsons sued, and the trial court granted Crestbrook's summary judgment motion, based on the same analysis as the federal court. In *Thompson v. Crestbrook Insurance Co.*,[20] the Court of Appeal affirmed–but based on issue preclusion, not a coverage analysis.

The California Supreme Court's decision in *Liberty Surplus Ins. Corp. v. Ledesma & Meyer Constr. Co., Inc.*[21] anchored the Thompsons' claims against Crestbrook. In *Ledesma*, the Ninth Circuit certified to the California Supreme Court the question: "Whether there is an 'occurrence' under an employer's [CGL] policy when an injured third party brings claims against the employer for the negligent hiring, retention, and supervision of the employee who intentionally injured the third party?"[22] The Supreme Court accepted the certified question before the Thompsons sued Burlington, but it had not answered the question while the suit was pending.

The District Court ruled for Burlington because "[a]n accident does not occur when the insured performs a deliberate act unless some additional, unexpected, independent, and unforeseen happening occurs that produces the damage. Where the insured intended all of the acts that resulted in the victim's injury, the event may not be deemed an 'accident' merely because the insured did not intend to cause injury. . . . where damage is the direct and immediate result of an intended . . . event, there is no accident."[23] Thus, where the Thompsons intended to take up work on the servient parcel, it was irrelevant that they did not intend to cause harm because "[t]he term 'accident' does not apply where an intentional act resulted in unintended harm," so there was no occurrence, and no coverage under the Burlington policy.[24]

By the time the Ninth Circuit heard the Thompsons' appeal of the Burlington judgment, they had lost SLT's lawsuit, and the trial court's statement of decision included a finding that the Thompsons intentionally violated the easement. The Supreme Court had also issued its *Ledesma* opinion, holding coverage may be available under a CGL policy based on the insured's negligently hiring, training, or supervising an employee whose intentional acts caused damage. The Thompsons then raised *Ledesma* before the Ninth Circuit, but the Court of Appeals rejected the argument, finding the California Supreme Court's opinion to be consistent with existing law "that there is no accident where an insured intended the acts that caused the injury, but not the injury." The Ninth Circuit concluded that,

"[b]ecause [the underlying action] does not concern accidental conduct under this state-law standard, Burlington had no duty to defend."[25]

After this loss, and after losing at trial with SLT's motion for $3 million in attorney fees pending, the Thompsons tendered SLT's claims to Crestbrook. Crestbrook denied tender and the Thompsons sued. Crestbrook moved for summary adjudication of its duty to defend, and the Thompsons opposed, arguing they were entitled to a defense under *Ledesma*. The Thompsons reasoned that because some of the harm SLT alleged to its property "could be attributed to their negligent hiring or supervision of the contractors whose negligent restoration work caused that damage or worsened the initial harm,"[26] they were entitled to coverage. The trial court granted Crestbrook's motion, distinguishing *Ledesma* partly on the basis of extrinsic facts discovered during the underlying litigation suggesting the alleged conduct "cannot be narrowed to negligent hiring and supervision over the contractors who performed the injurious work. [The Thompsons'] own conduct was alleged and shown to be intentional, . . . not an 'accident.'"[27]

On appeal, Crestbrook argued the judgment in the *Burlington* case precluded relitigating whether the underlying claim was based on an "accident," and the First District Court of Appeal agreed. In its opinion, the Court of Appeal discussed the five threshold requirements of issue preclusion: (1) an identical issue (2) actually litigated and (3) necessarily decided by (4) a final ruling on the merits (5) against a party or privy, and found that the *Burlington* judgment satisfied all of them.

Challenging prong one of the issue preclusion analysis, the Thompsons contended that the issues in *Burlington* and *Crestbrook* were not identical because they had asserted a new legal theory, based on *Ledesma*, and relied on facts they didn't raise in *Burlington*. The Court of Appeal rejected this view, however, holding that the ultimate issue of whether SLT's alleged injuries arose from an accident was identical, as were the factual allegations in SLT's complaint. "The coverage issue in each case turned on the same underlying universe of facts regarding the acts of the Thompsons and their contractors affecting the easement parcel."[28] The *Burlington* court's decision that SLT's claim was not based on an accident rested on "the same basic facts, whether or not described as fully as the Thompsons now describe them. '[O]nce an issue is litigated and determined, it is binding in a subsequent action notwithstanding that a party may have omitted to raise matters for or against it which if asserted might have produced a different outcome.'"[29]

The Court also viewed *Ledesma* as not having materially changed the law. It noted the Supreme Court had not overruled or disapproved any decision, and even suggested prior precedent foreshadowed the result. "Accordingly, no material change in law since the *Burlington* judgment diminishes its preclusive effect."[30]

More notable than the Court's application of issue preclusion in this case is the fact that the First District declined to apply relatively recent and plainly apposite Supreme Court precedent. In another neighbor property damage case this year, however, the Second District did apply *Ledesma*, but still found no occurrence and no coverage.

NO COVERAGE FOR INSURED'S DELIBERATE ACT OF HIRING CONTRACTORS TO CLEAR AND LEVEL NEIGHBORS' LAND

While the First District, in *Thompson*, effectively dodged the question of how to apply *Ledesma*, the Second District took the question head on in *Ghukasian v. Aegis Security Ins. Co.*[31] Their answer won't please policyholders.

Ghukasian's neighbor sued her for trespass and negligence based on the acts of contractors she hired "to level land and clear trees on land she understood to be a part of her property," but which actually belonged to the neighbor.[32] The trial court granted summary judgment to the insurance company, finding it owed no duty to defend because the neighbor's suit alleged intentional conduct which

was not an occurrence under the policy. The Court of Appeal affirmed.

The Court of Appeal cited multiple cases to support its analysis that "Ghukasian specifically instructed her contractor to level certain land and cut trees, which is exactly what was done. Ghukasian's mistaken belief about the boundaries of her property is irrelevant to determining whether the conduct itself—leveling land and cutting trees—was intentional."[33] The insured conceded the weight of authority supported the trial court's ruling, but she contended *Ledesma* "impliedly disapproved caselaw holding an intentional act is not an 'accident,' as the term is used in the coverage clause of a liability policy, even if the intentional act causes unintended harm."[34] The Court of Appeal was "unpersuaded."[35]

Unlike the alleged negligent hiring of an employee whose molestation of a third party "may be deemed an unexpected consequence of [the employer's] independently tortious acts of negligence," the insured's "intentional conduct (leveling land and cutting trees) was the *immediate* cause of the injury; there was no additional, independent act that produced the damage."[36]

The Court also rejected the insured's argument that the carrier had to cover a cause of action for negligence, because "[t]he scope of the duty [to defend] does not depend on the labels given to the causes of action . . . instead it rests on whether the *alleged facts or known extrinsic facts* reveal a possibility that the claim may be covered by the policy."[37] The neighbor's suit may have alleged a cause of action for negligence, but the factual allegations were of intentional acts.

Based on these cases, California's courts appear to be narrowly construing *Ledesma*'s recent exception to the strict definition of "occurrence" in CGL policies–a strict definition which is itself a relatively recent interpretation.[38]

INDEMNITY FOR SUCCESSOR TO LEAD PAINT MANUFACTURER PROPERLY DENIED BASED ON INSURANCE CODE SECTION 533

In *Certain Underwriters at Lloyd's, London v. ConAgra Grocery Products Co., Inc.*,[39] ConAgra sought indemnity from its liability insurers for over $100 million paid to abate a public nuisance created by lead paint to which its predecessor by merger, W.P. Fuller & Co., had contributed. In the underlying litigation, ConAgra was held liable based on Fuller's intentional promotion of lead paint for interior residential use with knowledge of the danger such use would create. The First Appellate District upheld summary judgment in favor of the insurers, finding that coverage was barred by Insurance Code section 533, which provides that "an insurer is not liable for a loss caused by the wilful act of the insured."

The Court rejected ConAgra's argument that section 533 should not apply because the willful acts were those of its predecessor, reasoning that "application of section 533 is appropriate in this situation because the successor in a merger is on notice that it is purchasing the predecessor subject to the liabilities of that entity."[40] The Court likewise rejected ConAgra's assertion that the loss for which it sought indemnity was too attenuated from Fuller's promotions for section 533 to apply. While ConAgra argued that the statute requires both a "direct causal relationship" and a "close temporal connection" between the willful act and the loss, the Court held that the same causation analysis used to determine liability applied under section 533. Since the underlying litigation conclusively established ConAgra's liability, section 533 barred coverage. Finally, the Court declined to find any requirement that the insurer demonstrate that Fuller's high-level corporate managers acted with the requisite knowledge; it was sufficient that the underlying litigation established that the corporate entity had actual knowledge of the harms associated with lead paint.

COVID-19

CALIFORNIA APPELLATE COURTS CONTINUE TO REJECT COVID-19 BUSINESS INTERRUPTION CLAIMS

In 2022, several state appellate courts followed last year's seminal decision by the Fourth District Court of Appeal in *The Inns By The Sea v. California Mutual Ins. Co.*[41]—rejecting policyholders' lost business income COVID-19 claims because they did not result from a "direct physical loss of or damage to property".

First, in *Musso & Frank Grill Co., Inc. v. Mitsui Sumitomo Ins. USA Inc.*,[42] Division One of the Second Appellate District affirmed the disposal of a COVID-19 claim via demurrer under a business interruption policy Musso & Frank's policy covered loss of business income caused by "direct physical loss of or damage to property at [the covered] premises." The Court construed that language as requiring "some physicality to the loss or damage of property–e.g., a physical alteration, physical contamination, or physical destruction."[43] Citing both *Inns* and *Mudpie, Inc. v. Travelers Casualty Ins. Co. of America*,[44] the Court found, "At this point, there is no real dispute. Under California law, a business interruption policy that covers physical loss and damage does not provide coverage for losses incurred by reason of the COVID-19 pandemic."[45] Since Musso & Frank's claim was not based on any physical alteration of its property, and its closure was not based on any physical loss or damage, it could not prove coverage.

Musso & Frank was followed the next day by *United Talent Agency v. Vigilant Ins. Co.*,[46] in which Division Four of the Second Appellate District similarly affirmed the dismissal of a COVID-19 claim on demurrer. United Talent Agency ("UTA") argued that its losses fell under its business income coverage because the virus limited its use of its insured locations and its properties suffered damage caused by the "alleged presence" of the virus in the air and on surfaces. UTA further sought coverage under its civil authority provision because UTA suffered loss of use resulting from civil closure orders.

Following the reasoning in *Inns*, the Court rejected UTA's argument that loss of use as a result of the "the danger posed by SARS-CoV-2"[47] met the requirement of "direct physical loss or damage" to its premises. UTA sought to distinguish *Inns* by pointing out that it had additionally alleged the physical presence of the virus at the insured premises, but the Court rejected this argument as well, noting that "many courts have rejected the theory that the presence of the virus constitutes physical loss or damage to property."[48] This is because "cleaning or employing minor remediation or preventive measures to help limit the spread of the virus does not constitute direct physical damage or loss."[49] Finally, the Court found no coverage under the civil authority provision, which requires impairment of operations caused by a civil authority where the prohibition of access is "the direct result of direct physical loss or damage to property away from" a covered premises.[50] Once again following *Inns*, the Court found that the closure orders were issued in an attempt to prevent the spread of COVID-19, not as a result of any direct physical loss of or damage to any property.

The First Appellate District, Division Two, followed suit in *Apple Annie, LLC v. Oregon Mutual Ins. Co.*[51] Citing *Inns*, *Musso & Frank*, and *UTA*, the Court added its voice to the chorus finding that COVID-19 closures did not result from "direct physical loss of or damage" to the insured's property, and rejected Apple Annie's contention that the phrase should be read disjunctively so as to differentiate loss from damage.

DOOR TO COVERAGE OPENED WHERE PHYSICAL ALTERATION CAUSED BY THE VIRUS IS PLED

The news was not all bad for policyholders seeking coverage for COVID-19 losses, however. In *Marina Pacific Hotel & Suites, LLC v. Fireman's Fund Ins. Co.*,[52] the Second Appellate District, Division Seven, refused to affirm the grant of a demurrer where the policyholder alleged that the COVID-19 virus had physically transformed portions of the insured properties. Specifically, Marina Pacific cited several journal articles explaining that the virus "actually

bonds and/or adheres to such objects through physio-chemical reactions involving, *inter alia*, cells and surface proteins" and "caus[es], among other things, a distinct demonstrable or physical alteration to property."[53] Nonetheless, the trial court ruled that the insured had failed to allege "direct, physical loss" as required by the policy.

While acknowledging that *Inns* and *UTA* required that the insured property undergo a physical change to come within coverage, the Court found that Marina Pacific's allegations sufficiently satisfied this requirement. "Assuming, as we must, the truth of these allegations, even if improbable, absent judicially noticed facts irrefutably contradicting them, the insureds have unquestionably pleaded direct physical loss or damage to covered property. . . ."[54] The Court recognized that its decision was at odds with *UTA*, but rejected that court's assumption that surface cleaning was the only remediation necessary to restore contaminated property to its original condition. The Court also noted that the Marina Pacific policy specifically included communicable disease coverage, which explicitly contemplated that a virus could cause direct physical loss or damage.[55]

The Court also rejected the trial court's finding that a "Mortality and Disease" exclusion barred coverage. That exclusion provided that the insurer would not pay for any losses caused directly or indirectly by "mortality, death by natural causes, disease, sickness, any condition of health, bacteria or virus." Noting that this language varied from the all-encompassing, industry-standard virus exclusion, the Court found that "the most reasonable interpretation of this language is that it precludes coverage for losses related to the death from any of the listed causes."[56] This limited interpretation of the exclusion was further reinforced by the policy's communicable disease coverage; a broad virus exclusion would render that coverage meaningless. Accordingly, Marina Plaza's case was allowed to proceed to a decision on the merits.

The import of Marina Pacific was soon felt in *Tarrar Enterprises, Inc. v. Associated Indemnity Corp.*, decided by the First Appellate District, Division Two.[57] In *Tarrar*, the insured's business interruption claim was dismissed at the demurrer stage. Citing *Inns*, *Musso & Frank*, *Marina Pacific*, and its own recent decision in *Apple Annie*, the Court found that the demurrer was properly sustained. However, because Tarrar sought leave to amend to add allegations similar to those in *Marina Pacific*, the Court reversed and instructed the trial court to grant leave to amend.

COST TO DISINFECT CONSTITUTES "DIRECT PHYSICAL LOSS OR DAMAGE" UNDER COMMUNICABLE DISEASE COVERAGE AND LOSS AVOIDANCE EXTENSION

Another case to diverge from the string of insurance company victories was *Amy's Kitchen, Inc. v. Fireman's Fund Ins. Co.*,[58] which involved not a business interruption claim, but instead a claim under a communicable disease coverage extension. The insured, Amy's, manufactures organic and vegetarian meals. It purchased a property insurance policy which included coverage for "direct physical loss or damage to Property Insured caused by or resulting from a covered communicable disease event at a location including the following necessary costs incurred to: . . . (c) Mitigate, contain, remediate, treat, clean, detoxify, disinfect, neutralize, cleanup, remove, dispose of, test for, monitor, and assess the effects [of] the communicable disease." The policy defined "communicable disease event" as one in which "a public health authority has ordered that a location be evacuated, decontaminated, or disinfected due to the outbreak of a communicable disease at such location." The policy also included a loss avoidance or mitigation extension, which covered "necessary expense you incur to protect, avoid, or significantly mitigate potential covered loss or damage that is actually and imminently threatening Property Insured."[59]

Amy's alleged that it had incurred costs to mitigate coronavirus at its insured locations, such as by purchasing protective shields, masks and goggles, cleaning supplies, etc. However, the trial court dismissed the case on demurrer, finding that Amy's had failed to allege direct physical loss or damage

to its property. The Court of Appeal rejected this conclusion in light of the specific inclusion of mitigation costs within the communicable disease extension, which would otherwise be rendered "redundant and meaningless."[60] It thus held that "the only plausible interpretation of subparagraph (c) of the communicable disease extension in this policy is that the need to clean or disinfect infected or potentially infected covered property constitutes 'direct physical loss or damage' of that property within the meaning of the policy."[61] Similarly, coverage was potentially available under the loss avoidance or mitigation coverage. The trial court therefore erred in sustaining the demurrer on this basis.

The Court found that Amy's had not sufficiently pled a "communicable disease event," however, because its complaint alleged only that authorities issued jurisdiction-wide orders, rather than orders specific to the insured locations. Because Amy's represented that it could amend to allege that Amy's itself was directed to disinfect its locations, the Court reversed and remanded with leave to amend. While relatively few policies contain similar communicable disease coverage, the *Amy's Kitchen* case nonetheless represents a significant win for policyholders in an area where such victories have been scarce.

FIRST PARTY POLICIES

FAMILY LAW DECREE CAN TRUMP TERMS AND CONDITIONS GOVERNING OWNERSHIP OF LIFE INSURANCE POLICY

Family law and insurance law intersected in *Randle v. Farmers New World Life Ins. Co.*,[62] in which a life insurance policy was the subject of a divorce decree. To resolve their divorce, plaintiff Randle and her ex-husband, McConnell, entered into a stipulated judgment which granted Randle a one-quarter interest in McConnell's life insurance policy, under which she was designated as the beneficiary. However, McConnell was allowed to name other beneficiaries as to the remaining three-quarter interest. The decree further provided that if McConnell did not keep up with the premiums, the policy would be assigned to Randle and she could name any beneficiaries she wished.

Without Randle's knowledge, McConnell submitted a request to change the beneficiaries so that the couple's three sons would receive three-quarters of the benefits and Randle would receive one-quarter. However, McConnell subsequently stopped paying the premiums, and Randle took over the payments, having been assured by Farmers' insurance agent that she was still the only beneficiary. Nonetheless, after McConnell died, Farmers paid the policy proceeds to plaintiff and her three sons. Randle then sued Farmers for breach of contract and bad faith.

The trial court granted summary judgment to Farmers, finding that the terms and conditions of the policy for changing ownership were not followed, but the Court of Appeal, Second Appellate District, reversed. Citing a venerable California Supreme Court case,[63] the Court held that "(1) the insurance policy's requirements for changing ownership do *not* control over the provisions of a contract (here, the divorce decree) of which the insurer has notice, and (2) the question is whether, when it paid out the proceeds, Farmers 'had such knowledge or notice of plaintiff's ownership of the policy as to require a recognition of plaintiff's rights.'"[64] Given the evidence that Farmers knew that plaintiff was paying the premiums and was made aware of the divorce decree before paying out the proceeds, there were material factual disputes precluding summary judgment. Moreover, the repeated assurances by Farmers' agent that Randle remained the sole beneficiary precluded summary judgment on the ground that McConnell had properly changed the beneficiaries.

CARRIER NOT REQUIRED TO PAY MORE THAN ACTUAL CASH VALUE (ACV) FOR TOTAL LOSS OF RENTAL HOME DESTROYED BY FIRE AND REBUILT AT ANOTHER LOCATION FOR NO MORE THAN ACV

Plaintiffs in *Westmoreland v. Fire Insurance Exchange*[65] had a so-called "open policy" with Fire Insurance Exchange (a.k.a. Farmers Insurance) that provided up to 125 percent of coverage to repair, rebuild, or

replace their dwelling.[66] But the policy also provided Farmers would not pay more than actual cash value of the damage until repair or replacement is completed, and it contained a "Loss Settlement" provision limiting benefits to "the smallest of" policy limits, replacement cost "on the same premises," or the amount "actually and necessarily spent to repair or replace the building intended for the same occupancy and use."[67]

Their house burned down in 2015. The estimated replacement cost at the same location was $422,676, but the Westmorelands rebuilt elsewhere, at an actual cost of no more than the ACV of $372,000, and that is what Farmers paid them. At the time of the loss, Ins. Code sec. 2051.5, subd. (c), provided the "measure of indemnity [for a total loss] shall be based upon the replacement cost of the insured property and shall not be based upon the cost to repair, rebuild, or replace at a location other than the insured premises."[68] The Westmorelands argued this provision required Farmers to pay them an additional $50,676, i.e., the difference between the replacement cost at the original location and the ACV of replacing the home at a different location. This interpretation appeared to conflict with subdivision (a) of the statute, which limited the measure of indemnity to full replacement cost up to policy limits. (The current version of the statute limits the measure of indemnity to replacement cost at the original location of the insured structure.)[69]

The trial court overruled Farmers' demurrer, but the Court of Appeal, First Appellate District, tried to reconcile subdivisions (a) and (c) of Section 2051.5, and held the statute did not require reimbursement of replacement costs that were not actually incurred. The statute "provides certainty to both the insurer and the insured that the full scope of a policy's extended replacement cost coverage would be available to the insured no matter where the lost dwelling is replaced."[70] The purpose of Section 2051.5, according to the Court, was to prohibit insurance companies from refusing benefits to policyholders who replaced their lost dwelling at locations other than the original insured premises, and to ensure "that if a policy provided coverage for extended replacement cost or guaranteed replacement cost, the full scope of such coverage would be available to the insured whether the lost dwelling was replaced at the insured location or elsewhere."[71]

The Court of Appeal supported its holding by referring to non-binding federal decisions, and an April 3, 2008, legal opinion from the General Counsel of the Department of Insurance advising against allowing a homeowner building at a new location to recover cash unrelated to actual building cost. The Court approvingly quoted the General Counsel's opinion: "Whether replacing at an original or a new location, the homeowner may not recover amounts above actual cash value not actually and reasonably spent to rebuild."[72]

LOSS OF FUNDS BASED ON FRAUDULENT EMAIL COVERED UNDER COMPUTER FRAUD AND FUND TRANSFER FRAUD PROVISIONS OF POLICY

In *Ernst and Hass Management Co., Inc. v. Hiscox, Inc.*,[73] a property management company sued its insurer after it denied a claim arising from the insured's loss of $200,000 in payments made in response to an email sent by a fraudster impersonating Ernst's founder and managing broker. Hiscox denied tender because the loss occurred due to the action of the insured's employee.

The policy covered "Computer Fraud" "resulting directly from the use of any computer to fraudulently cause a transfer of that property from inside [the insured's premises] . . . . [t]o a person (other than [the insured] outside [those premises]."[74] The insured also had "Funds Transfer Fraud" coverage for losses "resulting directly from a [Fraudulent Instruction] directing a financial institution to transfer, pay or deliver . . . from [an account maintained by Ernst at a financial institution from which Ernst can initiate the transfer, payment, or delivery]."[75] The District Court found the loss did not result directly from fraudulent emails directing an employee to transfer funds to a third party fraudster, and it granted Hiscox's Motion to dismiss.

The Ninth Circuit Court of Appeals reversed, holding that the District Court misapplied *Pestmaster Servs., Inc. v. Travelers Cas. & Sur. Co. of America*,[76] a case that involved funds stolen from the insured by a contractor with authorization to make payroll tax payments for the insured. The Ninth Circuit distinguished *Pestmaster*, highlighting that the authorization for the payment in this case was itself fraudulent; in other words, no one "was ever *properly* authorized to pay anyone the $200,000 that Ernst lost."[77] "Given that this case is about an email fraud scheme, the district court erred by relying on *Pestmaster* to interpret the policy as if the case were about embezzlement."[78] Ultimately, the Ninth Circuit found that, under these circumstances, the insured's loss resulted directly from the fraud because it immediately lost its funds when they were transferred as directed by the fraudulent email.

The Ninth Circuit also found coverage under the policy's Funds Transfer Fraud provisions. Whether a fraudulent instruction was sent directly to a bank or initially received by an employee, a "fraudulent instruction that results in 'directing' a financial institution to transfer funds is covered by the policy."[79]

SUBROGATION

INSURER BARRED FROM PURSUING SUBROGATION CLAIM AGAINST DRIVER WHOSE LIABILITY INSURER WAS INSOLVENT

Mercury insurance filed a subrogation action against an insured driver to recover Mercury's payments to its insured after his carrier became insolvent in *Mercury Insurance Co. v. Golestanian*[80], an opinion from the Los Angeles Superior Court Appellate Division. The trial court entered judgment for Mercury but the Court of Appeal reversed.

The Guarantee Act[81] was passed in 1969, creating the California Insurance Guarantee Association (CIGA) to provide coverage against a loss resulting from an insolvent insurer's failure. Section 1063.1 authorizes an insurer to pursue claims against an insolvent insurer's policyholder, but Section 1063.2 "provides that when an insured has collision coverage on a loss that is covered by an insolvent company's liability policy, then the collision carrier, if it is a member of CIGA, does not have the right to sue the insured of the insolvent insurance company for that collision damage."[82]

The Court of Appeal concluded Section 1063.2, subd. (c)(2) was "intended to preclude an insurer in plaintiff's position from pursuing a subrogation claim against an insured like defendant, whose liability insurer was declared insolvent following the covered incident." [83] "This result," the Court observed,

> furthers the legislative purpose underlying the Guarantee Act: 'CIGA was established to protect members of the public from the insolvency of insurers by spreading throughout the industry a loss suffered by an insured as the result of the insolvency of an insurer. . . . CIGA was *not* intended to protect its member insurers against contribution to a loss by shifting the burden of the loss to a member of the public who otherwise has no insurance available to cover the loss. Indeed, such a result would be contrary to the very purpose for which CIGA was established.[84]

CUMIS COUNSEL

CARRIER THAT DETERMINED ITS INSURED WAS AT FAULT NOT OBLIGATED TO RETAIN AS INDEPENDENT COUNSEL LAWYERS REPRESENTING INSURED ON AFFIRMATIVE CLAIM

Simonyan was driving the middle car in a three car accident. He sued the driver that hit him, and when the driver Simonyan hit sued him, he asked his insurance company, Nationwide, to appoint the firm representing him on the affirmative claim as his defense counsel. Even though Nationwide agreed to defend the case against Simonyan without a reservation of rights, Simonyan argued that Nationwide had to hire the lawyers representing him because the insurer had determined he was at fault for the accident, which created a conflict of interest triggering its duties under Civil Code

§ 2860. Nationwide denied there was a conflict of interest but appointed outside counsel, and it refused to pay Simonyan's chosen counsel. Simonyan sued for breach of contract and bad faith, Nationwide demurred, and the trial court sustained the demurrer without leave to amend and entered a judgment of dismissal.

In *Simonyan v. Nationwide Insurance Co. of America*, the Court of Appeal, Third Appellate District, affirmed.[85] It noted that "not every conflict of interest triggers an obligation on the part of the insurer to provide the insured with independent counsel at the insurer's expense[, and a] mere possibility of an unspecified conflict does not require independent counsel. The conflict must be significant, not merely theoretical, actual, not merely potential."[86] Simonyan's claimed conflict of interest had to do with what he contended was a "significant risk" that representation of his interest by the lawyers Nationwide hired would be "materially limited," a standard derived from Rule 1.7(b) of the Rules of Professional Conduct.[87] Significant risk of material limitation is not the statutory standard, nor is it generally listed in case law among the circumstances that could trigger the right to independent counsel. But the Court of Appeal found that even if it were to assume the right to independent counsel would attach due to such a risk of material limitation, Simonyan's allegations did not establish that risk.

Nationwide's determination that Simonyan was at fault did not relieve the carrier of its duty under the policy to pay for his defense and any damages. It had the same interest as Simonyan to defeat liability and minimize damages. Citing to the recent case of *Nede Mgmt, Inc. v. Aspen American Insurance Co.*,[88] where the court rejected a claim that insurer-appointed counsel's alleged belief that insureds would be bad witnesses did not create a conflict of interest, the Court dismissed Simonyan's hypothetical scenario "where a lawyer appointed by Nationwide 'will prepare him to testify one way based on Nationwide's belief that he was at fault,' and he must 'choose to cooperate with Nationwide's position that he is at fault, or he can choose to speak the truth and lose his defense counsel.'"[89] Rejecting Simonyan's position, the court found that "[a]lleging 'anticipated circumstances' that 'have not occurred yet in the underlying litigation' is insufficient to state a claim that independent counsel is required."[90] So, the Court concluded Simonyan had no claim for breach of contract.

Simonyan's bad faith claim was more interesting. He analogized his case to *Barney v. Aetna Casualty & Surety Co.*,[91] where the Court of Appeal held a viable bad faith claim could be based on a policyholder's allegations that the carrier, with knowledge of her substantial counterclaim, made a settlement of a claim against her without her knowledge that operated to bar the counterclaim through retraxit. Simonyan argued that "it seems probable that Nationwide thinks that by insisting Simonyan has a 'duty to cooperate,' it could later force him to compromise his collateral rights or lose his defense under the policy on the ground that he failed to 'cooperate.'"[92] In other words, Simonyan feared Nationwide and its chosen counsel might pressure him to forego recovery on his affirmative claims or risk losing his defense because of a claimed failure to cooperate. But the Court of Appeal dismissed that fear, "given *Barney*'s holding that an insurance company has 'a duty not to knowingly use its discretionary power under the policy to effect a settlement in a manner injurious of [the insured]'s rights,' we do not see how we can infer a probability that such a breach would occur."[93]

ENDNOTES

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1. (2022) 14 Cal.5th 58 ("*Yahoo*").
2. *Id.* at p. 66.
3. *Id.* at p. 64.

4. *Id.* at p. 65.
5. *Id.* at p. 66.
6. *Id.* at p. 67.
7. *Id.* at p. 64.
8. *Id.* at p. 74.
9. *Yahoo! Inc. v. National Union Fire Ins. Co. of Pittsburgh*, 2022 WL 17433139
10. *Yahoo*, *supra*, 14 Cal.5th at p. 73, *see also*, *Renee J. v. Superior Court* (2001) 26 Cal.4th 735, 743.
11. *Id.* at p. 74.
12. *Id.* at p. 75.
13. (2022) 82 Cal.App.5th 825 ("*24th & Hoffman*").
14. *Id.* at p. 831 (emphasis added).
15. (1997) 16 Cal.4th 35.
16. (2010) 186 Cal.App.4th 383 (emphasis added).
17. *See Saarman Construction, Ltd. v. Ironshore Specialty Insurance Co.* (N.D.Cal. 2017) 230 F.Supp.3d 1068 and *Conway v. Northfield Ins. Co.* (N.D.Cal. 2019) 399 F.Supp.3d 950.
18. *24th & Hoffman*, *supra*, 82 Cal.App.5th at p. 839.
19. *Id.* at p. 840.
20. (2022) 81 Cal.App.5th 115 ("*Thompson*").
21. (2018) 5 Cal.5th 216 ("*Ledesma*").
22. *Thompson*, *supra*, 81 Cal.App.5th at p. 120.
23. *Ibid.* (citations and internal quotations omitted).
24. *Id.* at p. 121.
25. *Id.* at p. 122.
26. *Id.* at pp. 122-123.
27. *Id.* at p. 123.
28. *Id.* at p. 127.
29. *Ibid.*, quoting *Carroll v. Puritan Leasing Co.* (1978) 77 Cal. App.3d 481, 490.
30. *Id.* at p. 128.
31. (2022) 78 Cal.App.5th 270.
32. *Id.* at p. 273.
33. *Id.* at p. 276, citing, *e.g.*, *Albert v. Mid-Century Ins. Co.* (2015) 236 Cal.App.4th 1281, 1291; *Fire Ins. Exchange v. Superior Court* (2010) 181 Cal.App.4th 388, 392.
34. *Id.* at p. 272.
35. *Id.* at p. 276.
36. *Id.* at p. 277.
37. *Ibid.*, citing *Cunningham v. Universal Underwriters* (2002) 98 Cal.App.4th 1141, 1148.
38. Compare *Delgado v. Interinsurance Exchange of Automobile Club of Southern California* (2009) 47 Cal.4th 302; with *Gray v. Zurich Ins. Co.* (1966) 65 Cal.2d 263.
39. (2022) 77 Cal.App.5th 729 ("*ConAgra*").
40. *Id.* at p. 721 (internal quotations omitted).
41. (2021) 71 Cal.App.5th 688 ("*Inns*").
42. (2022) 77 Cal.App.5th 753 ("*Musso & Frank*").
43. *Id.* at p. 758, citing *Oral Surgeons, P.C. v. The Cincinnati Ins. Co.* (8th Cir. 2021) 2 F.4th 1141.
44. (9th Cir. 2021) 15 F.4th 885 ("*Mudpie*").
45. *Musso & Frank*, *supra*, 77 Cal.App.5th at p. 760.
46. (2022) 77 Cal.App.5th 821 ("*United Talent Agency*").
47. *Id.* at p. 830.
48. *Id.* at p. 835.
49. *Id.* at p. 839.
50. *Id.* at p. 840.
51. (2022) 82 Cal.App.5th 919 ("*Apple Annie*").
52. (2022) 81 Cal.App.5th 96 ("*Marina Pacific*").
53. *Id.* at p. 101.
54. *Id.* at p. 109.
55. *Id.* at p. 112.
56. *Id.* at p. 113.
57. (2022) 83 Cal.App.5th 685 ("*Tarrar*").
58. (2022) 83 Cal.App.5th 1062 ("*Amy's Kitchen*").
59. *Id.* at p. 1065.
60. *Id.* at p. 1071.
61. *Ibid.*

62. (2002) 85 Cal.App.5th 53 (“*Randle*”).

63. *Morrison v. Mutual Life Ins. of New York* (1940) 15 Cal.2d 579 (“*Morrison*”).

64. *Randle*, *supra*, 85 Cal.App.5th at p. 63, quoting *Morrison*, *supra*, 15 Cal.2d at pp. 587-588 (emphasis in original).

65. (2021) 73 Cal.App.5th 269 (“*Westmoreland*”).

66. *Id.* at p. 274.

67. *Ibid.*

68. *Id.* at p. 277.

69. Ins. Code § 2051.5, subd. (c).

70. *Westmoreland*, *supra*, 73 Cal.App.5th at p. 278.

71. *Ibid.*

72. *Id.* at p. 281

73. (9th Cir. 2022) 23 F.4th 1192 (“*Ernst and Hass*”)

74. *Id.* at p. 1198.

75. *Ibid.*

76. (9th Cir. 2016) 656 Fed. App’x. 332.

77. *Ernst and Hass*, *supra*, 23 F.4th at p. 1200.

78. *Id.* at p. 1201.

79. *Id.* at p. 1202.

80. (2022) 82 Cal.App.5th Supp. 1 246, 297 Cal.Rptr.3d 246 (“*Golestanian*”).

81. Ins. Code §§ 1063 *et seq*.

82. *Golestanian*, *supra*, at p. 251, 297 Cal.Rptr.3d at p. 251.

83. *Id.* at 251-52, quoting *Black Diamond Asphalt, Inc. v. Superior Court* (2003) 114 Cal.App.4th 109, 114 (citations omitted).

84. *Ibid.*

85. (2022) 78 Cal.App.5th 889 (“*Simonyan*”).

86. *Id.* at p. 897, quoting *Dynamic Concepts, Inc. v. Truck Ins. Exchange* (1998) 61 Cal.App.4th 999, 1007.

87. *Ibid.*

88. (2021) 68 Cal.App.5th 1121.

89. *Simonyan*, *supra*, 78 Cal.App.5th at p. 898.

90. *Ibid.*

91. (1986) 185 Cal.App.3d 966.

92. *Simonyan*, *supra*, 78 Cal.App.5th at p. 900.

93. *Ibid.*, quoting *Barney*, *supra*, 185 Cal.App.3d at p. 978.