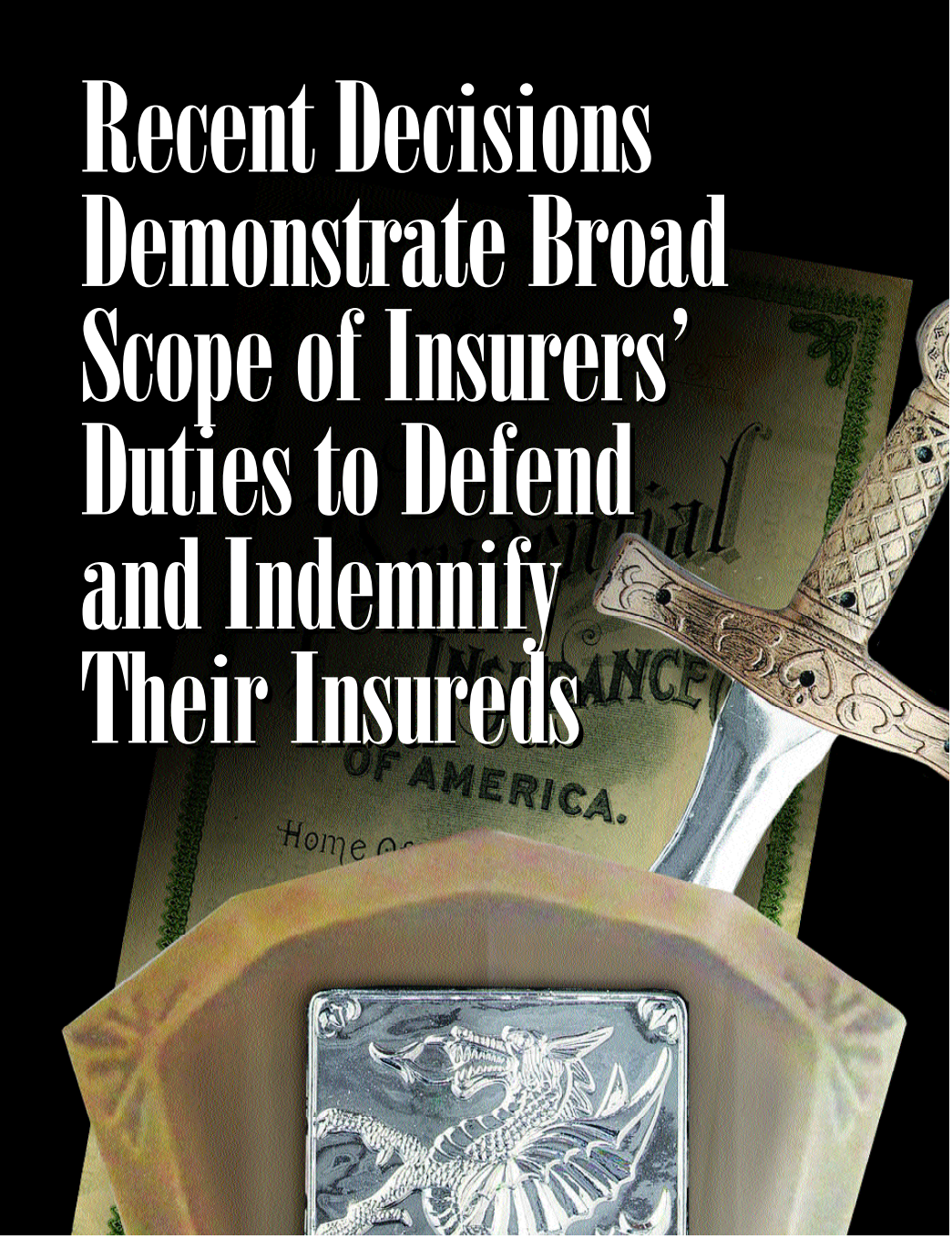
Recent Decisions Demonstrate Broad Scope of Insurers' Duties to Defend and Indemnify Their Insureds



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by Aneeta Kumar and Randy G. Gerchick

Several types of liability insurance policies require the insurer to defend the insured against any suit seeking damages that fall within the scope of the policy's coverage. It is well settled in California that an insurer's duty to defend is much broader than its duty to indemnify. For example, the insurer is required to defend the insured against suits that *potentially* seek damages within the coverage of the policy, regardless of whether the policy actually would cover a judgment against the insured.

Some may believe than an insurer's duty to defend is determined solely by reviewing the allegations of a complaint filed in a lawsuit against the insured. However, this is far from correct, as confirmed by recent decisions by state and federal courts in California. A recent decision by the California Supreme Court holds that a "suit" as the term is used in a general liability insurance policy may include an administrative proceeding, as well as a lawsuit filed in a court. Another recent decision confirms that an insurer may have to defend the insured even if the third-party's complaint against the insured does not specifically state the particular type of claim that is covered by the policy, and even if the complaint does not include all of the elements of a covered claim. Thus, both of these decisions demonstrate important ways in which liability insurance policies can be used to help companies pay for the expenses of responding to lawsuits or government administrative proceedings.

The Ameron Decision

In *Foster-Gardner, Inc. v. National Union Fire Ins. Co.,* 18 Cal.4th 857 (1998), the California Supreme Court addressed whether an order from a government environmental agency notifying the insured that it is a responsible party for pollution and requiring remediation is a "suit" triggering the insurer's duty to defend under a general liability insurance policy. Courts in some other states had adopted a "functional" view, holding that the receipt of any EPA-type cleanup letter or order constitutes a "suit." Other states took a "hybrid" approach, holding that an agency's letter, order or pre-complaint action is a "suit" if it is sufficiently coercive and threatening. Rejecting the "functional" or "hybrid" methodology that other states had adopted, the California Supreme Court in *Foster-Gardner* held that the term "suit" meant "a court proceeding initiated by the filing of a complaint." *Id.* at 878.

The California Supreme Court followed a similar approach a few years later in *Certain Underwriters at Lloyd's of London v. Superior Court*, 24 Cal.4th 945, 960–61 (2001) ("*Powerine I*"), where the Court considered the insurer's duty to indemnify the insured under standard general liability insurance policies. In this case, an insured oil refinery sought coverage from its liability insurers for costs incurred in complying with orders issued during administrative environmental proceedings. Like the insurance policies in *Foster-Gardner*, the policies in *Powerine I* used the terms "suit" and "damages" but did not define either. *Powerine I* limited the insurer's duty to indemnify for all sums the insured was "legally obligated to pay as damages" to sums ordered by a court, as opposed to expenses required by an agency's cleanup order. *Id.* at 951. In *Powerine Oil Co., Inc. v. Superior Court*, 37 Cal.4th 377 (2005) ("*Powerine II*"), the coverage provisions included the word "expenses," as well as "damages." Thus, the California Supreme Court held that under a literal reading of these policies, the insurers were required to indemnify the insured for expenses incurred in complying with an administrative agency's orders to clean up and abate pollution at contaminated sites. *Id.* at 383, 398–405. The

Court reached the opposite conclusion in *County of San Diego v. Ace Property & Casualty Ins. Co.*, 37 Cal.4th 406 (2005) to find no coverage for expenses incurred in responding to an administrative agency order to remediate environmental contamination because the literal insuring language of the excess/umbrella policies in that case neither referenced nor incorporated the term "expenses." *Id.* at 411.

Recently in *Ameron Intern. Corp. v. Ins. Co. of The State of Pennsylvania,* 50 Cal.4th 1370 (2010), the California Supreme Court took a different approach. The insured sought coverage under numerous primary, excess, and umbrella insurance policies for defense expenses and a settlement reached in connection with a federal administrative adjudicative proceeding before an administrative law judge of the former United States Department of Interior Board of Contract Appeals ("IBCA"). The trial court and the Court of Appeal relied on *Foster-Gardner* and ruled that the policies that used the undefined term "suit" provided no coverage because the IBCA proceeding was not a "suit" filed in a court of law.

However, the California Supreme Court reversed the Court of Appeal and held that the IBCA proceedings did constitute a "suit" for purposes of coverage under a liability policy. The Court observed that the proceedings before the administrative law judge in *Ameron* were initiated by a complaint and involved many of the same types of procedures that would be followed in a lawsuit filed in a court, and there were 22 days of trial, numerous witnesses, and substantial evidence presented. The Court unanimously held that this "quasi-judicial adjudicative proceeding, employed to resolve government demands against insured parties, is a 'suit' as a reasonable insured would understand that term."

Justice Kennard asserted in a concurring opinion that the California Supreme Court in *Ameron* appears to have implicitly rejected *Foster-Gardner*'s reasoning that a "suit" refers only to court proceedings. In light of this decision, policyholders would be well-advised to consider seeking coverage for any type of administrative proceeding and challenging any insurer's denial of coverage on grounds that the insured is not involved in a "suit."

The Hudson Decision

In *Hudson Ins. Co. v. Colony Ins. Co.*, 624 F.3d 1264 (9th Cir. 2010), NFL Properties sued All Authentic Corporation for allegedly making and selling counterfeit NFL jerseys. All Authentic had liability insurance policies with two insurers, Hudson and Colony. Hudson defended All Authentic, but Colony refused to defend. The suit between NFL Properties and All Authentic settled and Hudson sued Colony for equitable contribution and sought to recover 50% of the costs it incurred to defend All Authentic. The district court ruled for Hudson and the Ninth Circuit affirmed. It held that under California law, Colony had a duty to defend All Authentic because the NFL Properties complaint alleged facts showing that All Authentic was potentially liable for slogan infringement, which was a claim covered by the Colony insurance policy. In doing so, the Ninth Circuit rejected three arguments that Colony asserted to avoid having to reimburse Hudson.

First, Colony argued that although the NFL Properties complaint against All Authentic listed several specific causes of action for trademark infringement, trademark counterfeiting, trademark dilution, unfair competition, and deceptive acts and practices, the complaint did not include a cause of action for "slogan infringement." The Ninth Circuit stated that this argument failed because under California law the insurer's duty to defend "is not measured by the technical legal cause of action pleaded in the underlying third party complaint, but rather by the *potential* for liability under the policy's coverage as revealed by the *facts* alleged in the complaint or otherwise known to the insurer." *Hudson,* 624 F.3d at 1267 (quoting *CNA Cas. of Cal. v. Seaboard Sur. Co.*, 222 Cal.Rptr. 276, 280 (1986)). The Ninth Circuit then explained how the facts alleged in the NFL complaint, such as that All Authentic sold a "Steel Curtain Limited Edition Steelers Jersey" on its website which read "Steel Curtain" across the back of the jersey, potentially stated a claim for slogan infringement. The Court ruled that "it does not matter that the NFL complaint never referred to "Steel Curtain" as a slogan and never listed slogan infringement as a cause of action. *Id.* at 1269.

Colony also argued that the Court should not find potential liability for slogan infringement because NFL Properties and its "powerhouse international law firm" supposedly were aware of the cause of action for slogan infringement but consciously chose not to assert it in the complaint. The Ninth Circuit rejected this argument and stated "there is no merit for this 'election' or 'conscious avoidance' theory in the case law." *Id.* at 1269. The reason for omitting a particular cause of action from a complaint is not relevant. "It only matters whether the facts alleged or otherwise known by the insurer suggest potential liability or whether they do not." *Id.*

Colony's final argument was that NFL Properties supposedly had "disclaimed" any rights to the "Steel Curtain" slogan, and the facts alleged in the NFL complaint were insufficient to support a claim for slogan infringement because NFL Properties did not allege ownership of the "Steel Curtain" slogan or that it had standing to enforce the slogan rights. The Ninth Circuit rejected this argument because "California courts have cast doubt on the notion that a complaint must support all elements of a cause of action to state potential liability." *Id.* at 1269. In addition, in cases where a complaint alleges facts that support a duty to defend, "California courts have concluded that there is no duty to defend only when the third-party complaint unambiguously disclaims or concedes an element." *Id.* The Ninth Circuit then concluded that NFL Properties did not unambiguously concede in its complaint that it lacked standing to bring a slogan infringement claim and that NFL Properties did not expressly disclaim a slogan infringement claim, or standing to bring such a claim. Rather, the allegations of the NFL Properties complaint argued that NFL Properties did have standing to enforce the rights of the Steelers to the phrase "Steel Curtain," and under California law any ambiguity in the complaint or doubt regarding the duty to defend must be resolved in favor of coverage. *Id.* at 1270.

The *Hudson* decision serves as a reminder that an insurer's duty to defend cannot be determined just by examining the titles of the causes of action set forth on the first page of a complaint or by the headings within a complaint. If an insurer refuses to defend a lawsuit, it may be worthwhile to ask the insurer to review its position based on a careful consideration of all of the factual allegations against the policyholder. Depending on the circumstances, it might also help to provide the insurer with additional information such as the plaintiff's discovery responses, letters from the plaintiff's counsel, deposition transcripts or other documents in which the plaintiff describes the facts it is relying upon, the legal theories it is asserting, or the relief it is seeking.

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