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## ***In Action For Contribution Insurer Which Refused To Indemnify Had Burden Of Proving Absence Of Coverage***

Summary by Rebecca B. Aherne, Esq.

On October 6, 2010, the Second Appellate District filed its opinion in *Arrowood Indemnity Company v. Travelers Indemnity Company* holding Arrowood was entitled to contribution for amounts paid to satisfy a judgment against a contractor insured by Arrowood and Travelers because Travelers failed to meet its burden of proving the absence of coverage under its policy.

### *Factual and Procedural Background*

Ron and Maureen Ashley filed a complaint against Ruth and George Dunmore alleging the following: In November 2002, the Ashleys agreed to purchase an apartment complex from the Dunmores. Prior to the sale Five Star Services was hired to remediate dry rot at the complex. It discovered a substantial amount of dry rot which compromised the integrity of the complex and posed a serious safety risk. The hazards were not corrected, but concealed by adding trim to defective wood or covering the dry rot with new paint. The Dunmores cross-complained against the property manager and Five Star alleging that by contract entered into on or about November 2002, Five Star agreed to perform dry rot remediation at the complex, but negligently failed to locate and replace or remediate the structures affected by dry rot.

Five Star was insured by Travelers for the period July 1, 2000 to July 1, 2001, and by Arrowood for the period July 1, 2002 to July 1, 2003. Each policy had limits of \$1 million per occurrence and \$2 million in the aggregate. Both CGL policies provided the insurers would pay those sums the insured becomes legally obligated to pay as damages because of property damage and defend against suits seeking covered damages. The policies applied to property damage occurring during the policy period. Property damage was defined as physical injury to tangible property including loss of use of the property. The supplementary payments provisions provided coverage for all costs taxed against the insured and for prejudgment and post judgment interest.

Five Star tendered the defense of the Dunmore action to Arrowood which agreed to defend under a reservation of rights. Arrowood tendered the defense to Travelers based on information provided by Five Star and the property manager indicating work was also performed by Five Star during Traveler's policy period. Travelers agreed to participate in the defense subject to a reservation of rights.

The jury found Five Star negligent and awarded the Dunmores attorney fees and costs. The total award against Five Star, including compensatory damages, attorney fees, costs, and interest, was \$619,105. Travelers contributed to the attorney fees award, and to the fees and costs incurred in defending Five Star, but refused to indemnify Five Star for the compensatory damages award. Arrowood indemnified Five Star for the balance of the judgment and paid the balance of the fees and costs incurred to defend Five Star.



Arrowood subsequently sued Travelers for reimbursement. Travelers denied liability on the ground the property damage did not occur during its policy period, and asserted it was entitled to reimbursement from Arrowood for the sums it contributed to Five Star's defense and indemnity amounts paid. The trial court agreed with Travelers holding it had no duty to defend or indemnify and that it was entitled to reimbursement. The Court of Appeal reversed the judgment.

*Judicial Holding and Analysis*

The court held Travelers owed a duty to defend because the allegations in the underlying complaint and cross complaint created a potential for coverage. Although the complaints alleged the insured's tortious conduct occurred "on or about" November 2002, Five Star had also performed dry rot repair at the complex in August and October 2000. Travelers' knowledge that the insured performed work during its policy period was sufficient to trigger a duty to defend notwithstanding the fact the underlying complaints did not rely on the 2000 repairs as a basis for liability. The complaints could have been amended to state a claim against Five Star in connection with the work it performed in 2000.

Pursuant to the "Supplementary Payments" provision, because Travelers had a duty to defend, it was obligated to pay all costs, including attorney fees, taxed against the insured, prejudgment interest awarded against the insured and all interest on the amount of the judgment.

Travelers also had a duty to indemnify the insured. The court rejected Travelers' argument that Five Star did not become legally obligated to pay damages because of property damage that occurred during the Travelers' policy period. Travelers contended that because the claim was based solely on the work the insured did in 2002, the damages were based on property damage the plaintiffs suffered in 2002. Arrowood contended the jury awarded damages against Five Star for negligence occurring in 2000 and 2002. Because of the peculiar wording of the special verdict form, the scope of what the jury decided was not clear. However, there was testimony at trial about the insured's work in 2000 and 2002, and none of the instructions directed the jury to limit its verdict to the repairs performed in 2002.

The court held that in an action for equitable contribution brought by an insurer who has defended and indemnified an insured against a coinsurer who has not defended or has not indemnified the insured, the participating insurer has met its burden of proof when it makes a prima facie showing of coverage under the nonparticipating insurer's policy-the same showing necessary to trigger the recalcitrant insurer's duty to defend. The burden then shifts to the nonparticipating insurer to prove the absence of actual coverage.

Arrowood satisfied its burden of proof by making a prima facie showing of coverage-that Travelers had a duty to defend. The burden thus shifted to Travelers to prove the absence of actual coverage. The court concluded Travelers failed to meet its burden and therefore had a duty to indemnify the insured. At trial, evidence was introduced regarding the insured's alleged negligence in 2000. The jury was instructed that plaintiffs claimed they were harmed by the insured's performance of its "contract," and that it must award damages for each item of harm that was caused by defendant's wrongful conduct. Nothing in the special verdict form directed the jury to limit its consideration to negligence related to the insured's 2002 work. Thus, the court could not conclude that it was more likely than not that the jury based its negligence finding exclusively on work performed in 2002.



Travelers was obligated to defend and indemnify Five Star. Arrowood was entitled to equitable contribution from Travelers. The court remanded the action to the trial court to determine how most equitably to allocate defense and indemnity costs between Arrowood and Travelers.

*Comments and Implications*

The court indicated that no California court had previously considered the relative burdens of proof in a contribution action between insurers when the underlying case has gone to trial and been resolved by a jury. It relied on the reasoning in *Safeco v. Superior Court* (2006) 140 Cal App. 4<sup>th</sup> 874 in which the underlying claim was resolved by settlement. *Safeco* noted that contribution is an equitable rule intended “to accomplish substantial justice by equalizing the common burden shared by coinsurers, and to prevent one insurer from profiting at the expense of others.” The court stated that applying the *Safeco* burden-shifting rule tends to spread risk among insurers and prevent one insurer from profiting at another’s expense. Shifting the burden also discourages insurers from attempting to avoid their responsibilities to their insureds and by extension to their coinsurers.