

California Court of Appeals Limits Defenses Available to Insurers in Multiple-Insurer and Third-Party Coverage Cases

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The California Court of Appeals for the First District recently issued an opinion that effectively limits the defenses available to insurers in multiple-insurer and third-party coverage cases. The court in *Howard v. American National Fire Insurance Co.*¹ held that in multiple-insurer cases, unlike in single-policy cases, an insurer can breach its duty to settle if it rejects a settlement offer that is in excess of the insurer's individual policy limit but within the total limits available under all the insured's primary policies. The court also held that the genuine dispute doctrine, which can be used as a defense to a claim of bad-faith refusal to settle in first-party coverage cases, is not applicable to third-party coverage cases.

In the underlying case, James Howard brought suit against insured Roman Catholic Bishop of Stockton (Bishop) for negligent retention. Specifically, Howard alleged that from approximately 1977 through 1991, the Bishop employed Father Oliver O'Grady, who Howard alleged repeatedly molested him beginning in approximately 1979 through 1988.²

The Bishop sought defense and indemnity from several insurers, including American National Fire Insurance Company (American), which had issued the Bishop a comprehensive general liability policy with a policy period of November 1, 1978 to November 1, 1979.³ Unlike some of the Bishop's other insurers, American denied coverage based on the timing of the alleged molestation, which American contended occurred after its policy expired.⁴ Howard made several pretrial settlement demands, the lowest being for \$1.85 million.⁵ American's policy limit was \$500,000; the total combined limit of all the Bishop's insurers was \$4.3 million.⁶ American offered no contribution toward settlement, and the case ultimately went to trial.⁷

¹ *Howard v. American National Fire Insurance Co.*, 187 Cal. App. 4th 498 (2010), *reh'g denied*, 2010 Cal. App. LEXIS 1579 (Sept. 9, 2010).

² 187 Cal. App. 4th at 508.

³ *Id.*

⁴ *Id.*

⁵ *Id.* at 509.

⁶ *Id.* at 525.

⁷ *Id.* at 509.

A jury found the Bishop liable and the court entered judgment in the amount of \$5.5 million, \$2.5 million of that amount being for compensatory damages and the remaining \$3 million for punitive damages.⁸ The Bishop struggled to find collateral sufficient for an appeal bond and settled with Howard instead. The settlement involved a partial payment of the judgment by the Bishop and some of his carriers, as well as an assignment of the Bishop's rights against American.⁹

Both the Bishop and Howard brought suit against American. After a bench trial, the court found that Howard "was sexually molested during American's policy period, which triggered coverage under the policy, and that American, in bad faith, breached its duty to defend, settle, and indemnify the underlying litigation brought by [Howard] against the Bishop."¹⁰ Despite American's efforts to challenge the judgment at the appellate level, the appellate court affirmed the trial court's findings with respect to American's breaches.¹¹

Of particular significance, the appellate court flatly rejected American's assertion that it did not breach its duty to settle because "there never was a settlement demand within American's \$500,000 policy limit so it alone could not have settled the Howard case."¹² The court held that while in a single-policy case, an insurer must have received a settlement offer within its limits in order to be found to have breached its duty to settle, the same is not true in third-party cases.¹³ Specifically, in this case, Howard's lowest settlement offer of \$1.85 million was well below the total limits of the Bishop's coverage of \$4.3 million. If American and the other insurers had responded to this offer, the litigation could have been settled. Citing the trial court, the court stated, "[T]he law 'cannot excuse one insurer for refusing to tender its policy limits simply because other insurers likewise acted in bad faith. If this were not the case, insurers on the risk could simply all act in bad faith, thus immunizing themselves from bad faith liability.'"¹⁴

This holding is important to any insured with multiple policies covering the same risk, such as in a progressive loss or coverage tower scenario. Pursuant to this holding, an insurer providing coverage under such a scenario cannot avoid bad-faith liability simply because a settlement demand exceeds the limits of its particular policy.

Likewise, the court also flatly rejected American's assertion that its refusal to settle was reasonable, and, therefore, not in bad faith, because a genuine dispute existed as to the coverage.¹⁵ Specifically, the parties disputed whether the molestation occurred during American's policy period. The court recognized that while an insurer in a first-party case may raise a reasonable dispute over coverage without being guilty of bad faith, "it has never been held that an insurer in a third-party case may rely on a genuine dispute over coverage to refuse settlement."¹⁶ Instead, in third-party cases, "the only permissible consideration in evaluating the reasonableness of the settlement becomes whether, in light of

⁸ *Id.*

⁹ *Id.* at 510–11.

¹⁰ *Id.* at 512.

¹¹ *Id.* at 542.

¹² *Id.* at 524.

¹³ *Id.* at 525.

¹⁴ *Id.*

¹⁵ *Id.* at 530.

¹⁶ *Id.*

