Ninth Circuit Finds that Insured's Umbrella Liability Insurance Must Drop Down to Co-Primary Coverage with Commercial General Liability Policy

In American States Insurance Company v. Insurance Company of the State of Pennsylvania, No. 18-15770, 2020 WL 70491, the Ninth Circuit issued a decision about the role umbrella insurance policies have when there is a gap in insurance coverage, thereby opening the possibility for equitable contribution claims.

In 2007, Sierra Pacific Industries hired subcontractor Howell Forest Harvesting to help harvest trees on a plot of land in Plumas County, California. Howell obtained an insurance policy for the project from American States Insurance Company ("American States"). The American States policy required American States to defend its additional insured, Sierra, against any "suit seeking damages from Sierra, but only "to the extent" Sierra is vicariously liable for the named insured's operations." Sierra also maintained a separate umbrella policy through the Insurance Company of the State of Pennsylvania ("ICSOP").

In September 2007, Howell employees were allegedly operating bulldozers on the land when sparks ignited nearby that caused the "Moonlight Fire." The Moonlight Fire destroyed roughly 65,000 acres and resulted in multiple lawsuits against both Sierra and Howell. American States paid $13.2 million defending Sierra until the actions settled in 2012. However, ICSOP did not participate in the defense.[1] As a result, in 2012, American States sought a declaratory judgment and order against ICSOP to cover Sierra's defense fees and costs spent defending Sierra.

In March 2016, the District Court ruled that ICSOP should have defended Sierra in suits that did not name Howell. Therefore, American States had an equitable contribution claim against ICSOP.

The Ninth Circuit relied on American State's policy language. American State's primary indemnity coverage and duty to defend Sierra did not extend to Sierra's potential non-vicarious liability for property damage from the fire, creating a gap in the scope of American State's defense obligation in the Moonlight Fire lawsuits.

Also, the Ninth Circuit stated that "any gaps in coverage left open by underlying insurance may be filled by other insurance." (Powerine Oil Co. v. Superior Court, 118 P.3d 589, 603 (2005)). When claims are covered by an umbrella insurance policy but not by the underlying primary insurance, the umbrella insurer must drop down to provide primary coverage. ICSOP's umbrella policy includes

[1]ICSOP did eventually agree to pay $3.4 million for the independent counsel Sierra retained that American States would not pay for in full.

a clause stating that ICSOP will cover “the total of all damages" resulting from property damage covered by the policy but not covered by any underlying insurance up to a $10 million occurrence limit." Since American States' policy includes a duty to defend only claims alleging Sierra's vicarious liability, the District Court correctly determined that ICSOP had a duty to drop down and defend underlying suits in a co-primary capacity with American State.

Then the Ninth Circuit addressed American State's equitable conversion claims. American States appealed the District Court's decision to apportion the costs in equal shares, and to not allow American States to collect prejudgment interest. The Ninth Circuit held that because American States and ICSOP shared the same level of obligation on the same risk as to the same insured, American States was entitled to equitable contribution of defense costs from ICSOP. Furthermore, the Ninth Circuit held that splitting the costs equally between American States and ICSOP is within the trial court's discretion “to select a method of allocating costs among insurers … based on the facts and circumstances of the particular case." The District Court chose the equal shares approach, which is one of six recognized approaches[2] in California. The Ninth Circuit stated that, based on the facts and circumstances of this case, the District Court's decision to split the costs 50-50 was well within its discretion. However, the Ninth Circuit stated the trial court should have allowed the American States to collect prejudgment interest based on the date Sierra's total defense costs for the Moonlight Fire litigation became fixed.

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[2]According to 39A Cal. Jur. 3d Insurance Contracts § 673, the six ways of apportioning costs among multiple insurers are:
(1) apportionment based upon the relative duration of each primary policy as compared with the overall period of coverage during which the incident occurred (the “time on the risk" method);
(2) apportionment based upon the relative policy limits of each primary policy (the “policy limits" method);
(3) apportionment based upon both the relative durations and the relative policy limits of each primary policy, through multiplying the policies' respective durations by the amount of their respective limits so that insurers issuing primary policies with higher limits would bear a greater share of the liability per year than those issuing primary policies with lower limits (the “combined policy limit time on the risk" method);
(4) apportionment based upon the amount of premiums paid to each carrier (the “premiums paid" method);
(5) apportionment among each carrier in equal shares up to the policy limits of the policy with the lowest limits, then among each carrier other than the one issuing the policy with the lowest limits in equal shares up to the policy limits of the policy with the next-to-lowest limits, and continuing in the same fashion until the entire loss has been apportioned (the “maximum loss" method); and
(6) apportionment among each carrier in equal shares (the “equal shares" method).