

IV. Additional Insured And Contractual Liability Coverage

Prepared and Presented by:

**John H. Podesta, Esq.
Branson, Brinkop, Griffith
& Strong, LLP**

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1. Does The Insurer Have A Duty To Defend The Tendering Additional Insured?

Upon initial receipt of a tender, the insurer must immediately decide whether it has a duty to defend. While this duty is broad, there are limitations. For example, there is no duty to defend if the tendering party is not qualified as an Additional Insured. Also, there must be a potential that liability “arises out of” the Named Insured’s work or products. In sum, there must be “a claim, that is at least potentially covered because it may possibly embrace some triggering harm of the specified sort within the policy period caused by an included occurrence.” Aerojet-General Corp v. Transport Indemnity Co. (1997) 17 Cal. 4th 38, 68.

a. A Party Must Be Qualified As An Additional Insured Before The Duty To Defend Arises.

The first way to qualify as an Additional Insured is by being expressly named on an Additional Insured Endorsement. The endorsement “modifies the insurance” by extending certain protections to the party listed as the Additional Insured (See Insurance Service Organization Form CG 2010 11/85).

In Safeco Insurance Co. of America v. Parks (2004) 122 Cal.App.4th 779 the court held that when an carrier is investigating whether or not someone qualifies as an insured “[i]f it has made an informed decision on the basis of the third party complaint and the extrinsic facts *known* to it at the time of tender that there is no potential for coverage, the insurer may refuse to defend the lawsuit.”

i. Named As An Additional Insured.

For one to be named as an additional insured, there must be an additional insured endorsement issued by the insurance company. In many instances, claims are received by parties who purport to be insureds under policies issued by the company. They base their status as insureds fully upon the existence of a certificate of insurance. There is, to our knowledge, no decided case in the State of California addressing this issue either with or without reference to California Insurance Code §384. A limited number of cases have addressed similar issues in the context of loss payee endorsements, but even those cases are not directly on point.

ii. Additional Insured Endorsements

For one to be able to claim additional insured status, an additional insured endorsement must be issued by the subcontractor's insurance company. In general, there are two types of additional insured endorsements which purport to name a general contractor or a developer as an additional insured under a subcontractor's policy. These endorsements are known by their form numbers of "2009" or "2010."

(1). Form 2009

The most important consideration regarding this form is that it does not provide completed operations coverage. It is only intended to apply to injury or damage occurring when work is in progress.

The pertinent language from this form reads as follows:

It is agreed that:

- i The persons insured provision is amended to include as an insured the person or organization named above (hereinafter called 'additional insured'), but only with respect to liability arising out of (1) operations performed for the additional insured by the

named insured at the location designated above or (2) acts or omissions of the additional insured in connection with his general supervision of such operations.

...

- ii. Additional exclusions. This insurance does not apply:
 - (a) To bodily injury or property damage occurring after
 - (1) All work on the project (other than service, maintenance or repairs) to be performed by or on behalf of the additional insured at the site of the covered operations has been completed; or
 - (2) That portion of the named insured's work out of which the injury or damage arises has been put to its intended use...

Again, pursuant to Form 2009, an owner or contractor can be named as an additional insured under a subcontractor's policy. However, the 2009 form specifies that it only applies to injury or damage occurring when work is in progress, it does not apply to completed operations.

Most construction defect actions pertain to completed operations. Therefore, if a tender is made pursuant to a 2009 form, that tender in all probability will be denied because it does not provide completed operations coverage to the additional insured.

(2). Form 2010

The most prevalent ISO Form Additional Insured Endorsements, utilized by the industry, provides protection to the Additional Insured but only with respect to "liability arising out of" the work of the Named Insured. (See, e.g., Insurance Services Organization. Form CG 2010 11/85.)

(a) 11-85 Edition

This form provides broader coverage for owners or contractors named as additional insureds. There is no exclusion in this form for completed operations. This form provides in pertinent part as follows:

It is agreed that:

- a. The 'persons insured' provision is amended to include as an insured the person or organization named below but only with respect to liability arising out of your work performed for such insured by or on behalf of the named insured.

The 11-85 edition of the 2010 form uses the language "for that insured by or for you". This language acts to include in the insurance policy all subcontractors working under the named insured's policy.

A tender under this form requires more thought and analysis in order to properly respond to the purported additional insured without assuming coverage for all of the additional insured's liability.

(b) 10-93 Edition

This form provides in pertinent part as follows:

"WHO IS AN INSURED is amended to include as an insured the person or organization shown in the Schedule, but only with respect to liability arising out of your ongoing operations performed for that insured."

This form limits coverage for the additional insured to ongoing operations, and does not apply to completed operations losses claimed by the additional insured.

(c) 10-01 Edition

This form provides in pertinent part as follows:

“WHO IS AN INSURED is amended to include as an insured the person or organization shown in the Schedule, but only with respect to liability arising out of your ongoing operations performed for that insured.”

The 10-01 Endorsement tracks the 2009 additional insured endorsement form and the 10-93 form which limits coverage for additional insured to ongoing operations.

iii. “Blanket” Additional Insured Endorsement

A second way of providing coverage is with a “blanket” additional insured endorsement. A blanket does not expressly name an additional insured, but will identify the party with language such as, “blanket additional insured as required by contract or agreement.” Therefore, as long as there is a valid contract or agreement with the named insured requiring additional insured coverage, the endorsement will provide coverage to the additional insured.

iv. Certificate of Insurance

The third way to qualify as an Additional Insured is through a certificate; however, the certificate alone does not modify insurance. Instead, a certificate is “merely evidence that a policy has been issued.” (*Ins. Code §384.*) It is not a contract between the insurer and the certificate holder.” Pardee Construction Co. v. Insurance Co. of the West (2000) 77 Cal.App.4th 1340, 1347 fn.2.

If there is typewritten or specific language on the certificate indicating that the certificate holder is an Additional Insured and the person issuing the certificate is an authorized agent of the insurer, then the holder qualifies as an Additional Insured. Also, if there is some act on behalf of an authorized agent that would lead an insured to believe

coverage existed, a certificate may qualify a party as an Additional Insured. In most other cases, a party with only a certificate will not be qualified as an Additional Insured. *See* California Civil Code §2295 et seq.

California Civil Code §2300 provides that “[a]n agency is ostensible when the principal intentionally, or by want of ordinary care, causes a third person to believe another to be his agent who is not really employed by him.”

Where a certificate purports to name an additional insured or to expand the scope of coverage, the insured will argue the applicability of the doctrine of estoppel and/or agency principles. In American Casualty Co. v. Krieger (9th Cir. 1999) 181 F.3d 1113, such an argument was successfully pursued by the putative insured.

b. Duties of Additional Insured Carrier to Additional Insured

Under policies with completed operations coverage, an insurer owes a duty to defend an additional insured for liability arising out of a project completed prior to the issuance of such policies, unless the policy or additional insured endorsement includes explicit exclusionary language to the contrary. The court by implication emphasized the long standing rule that the insurance contract will be interpreted according to its literal terms, absent an ambiguity. Extrinsic evidence will not be admitted to refute an interpretation that is reasonable under the circumstances at the time the contract was entered into and is contrary to the terms of the policy. *See, e.g. Pardee Construction Co. v. Ins. Co. of the West* (2000) 77 Cal. App. 4th 1340.

Plaintiff builder sued Defendant insurer for failure to defend it in a construction defect action. The trial court granted the insurer’s Motion for Summary Adjudication and the builder appealed. The underlying action involved the subcontractor insured whose

insurance policies were endorsed to name the builder as an Additional Insured. Although the insurer agreed to pay a share of the builder's defense costs, it claimed it had a duty to defend only the claims relating to the subcontractors' work. See Presley Homes, Inc. v. American States Ins. Co. (2001) 90 Cal.App.4th 571.

The appellate court held that the builder was entitled to have the insurer provide a defense to the entire action as a matter of public policy. Where the insurer had a duty to defend, the obligation generally applied to the entire action, even though the suit involved both covered and uncovered claims. By amending the policies' definition of the term "Insured" to include the builder, the insurer assumed a duty to defend in actions seeking damages for injury to the property. While the Endorsements limited the indemnity coverage for the builder to "liability" arising from the subcontractors' work, nothing in either the policies, or the endorsements, limited the insurer's defense obligation. See Presley Homes, Inc. v. American States Ins. Co. (2001) 90 Cal.App.4th 571.

Various Ways For The Subcontractor Insurer To Fulfill Its Obligation To The Additional Insured General Contractor/Developer:

- Participate on a pro rata basis with the general contractor's own insurer for subcontractor's anticipated share of liability;
- Participate on a percentage basis based upon the particular subcontractor's anticipated share of liability; or
- Retain separate counsel to defend the additional insured.

c. The Claim Must Be Potentially Covered Under The Policy.

i. Insurance Policies Are Interpreted By Rules of Contract Interpretation.

The court will use contract rules of interpretation to analyze a policy. First, it will look to the mutual intentions of the parties at the time the policy is formed. Montrose Chemical Corp. of Cal. v. Admiral Insurance Co. (1995) 10 Cal.4th 645, 666. “[I]ntent is to be inferred, if possible, solely from the written provisions” of the policy. The court will apply the plain and ordinary meaning of the language in the provisions, unless the parties used the terms in a technical sense or designated special meaning to the provisions. Finally, if there is an ambiguity in the policy, the court will resolve the issue “by interpreting the ambiguous provisions in the sense the promisor (i.e., the insurer) believed the promisee understood them at the time of formation. (*California Civil Code Section 1649*).” In short, if the language of the policy is clear, it will be enforced as is. See Montrose, supra at p. 66; Pardee Construction Co. v. Ins. Co. of the West (2000) 77 Cal. App. 4th 1340; also see Aerojet-General Corp v. Transport Indemnity Co. (1997) 17 Cal. 4th 38, 68.

When language in a policy is ambiguous, meaning capable of two or more constructions, both of which are reasonable, the court has been willing to look beyond the policy to underlying subcontracts. St. Paul Mercury Ins. Co. v. Frontier Pacific Ins. Co. (2003) 111 Cal.App.4th 1234. In St. Paul, a subcontractor entered a lease with a crane rental company. The subcontractor was renting the crane to complete a project for a third party. Pursuant to the lease, the subcontractor added the rental company to its insurance policy as an Additional Insured.

The endorsement stated that the policy provided coverage to the crane rental company only with respect to liability “arising out of” the subcontractor’s operations “performed for” the rental company. There was, however, no contemplated work to be done for the rental company. The California Court of Appeal, Fourth Appellate District determined that the 2010 Endorsement issued was ambiguous. Therefore, the court looked to the underlying lease and the context of the situation to clarify the ambiguity, rather than simply interpreting ambiguities to provide coverage. St. Paul Mercury Ins. Co. v. Frontier Pacific Ins. Co. (2003) 111 Cal.App.4th 1234.

ii. Additional Insured Endorsements Include The Duty To Defend.

In Maryland Casualty Co. v. Nationwide Insurance Co. (1998) 65 Cal.App.4th 21 (Maryland I), the Court of Appeal held that an Additional Insured Endorsement entails an obligation to defend, even though not expressly stated on the endorsement.

The policy in Maryland I provided for indemnity and defense to “insureds.” “Insured” was defined as “. . . any person or organization qualifying as such under Who Is an Insured (Section II).” Maryland I, supra at p. 27-28. The Additional Insured was not listed in Section II. It was, however, named on the Additional Insured Endorsement. The endorsement language modified the policy so that Section II included the name on the Additional Insured Endorsement as an insured. Since the endorsement did not expressly or implicitly limit the defense obligation, the California Court of Appeal, Fourth Appellate District concluded that the insurer had a duty to defend.

The court also rejected the insurer’s argument that there was no duty to defend, because if the duty did exist, it existed “only to the extent” the general contractor was

“held liable” for the acts of the Named Insured. On the contrary, the court decided that “since a defense duty is broader than an indemnification obligation, the limitation on the scope of coverage does not eliminate the defense duty, but instead merely forms the parameters for that duty.” Further, the court said that it would arrive at the same conclusion whether the endorsement language was “held liable,” or “arising out of.” Maryland Casualty Co. v. Nationwide Insurance Co. (1998) 65 Cal.App.4th 21, 27-28.

Following the Maryland I decision, the California Court of Appeal, Fourth Appellate District decided Presley Homes, Inc. v. American States Ins. Co. (2001) 90 Cal.App.4th 571. The court held:

It is settled that where an insurer has a duty to defend, the obligation generally applies to the entire action, even though the suit involves both covered and uncovered claims, or a single claim, only partially covered by the policy. [Citation omitted] The Additional Insured Endorsements amended the policies’ definition of the term “insured” to include plaintiff. Defendant assumed a duty to defend an action seeking damages for injury to property. While the endorsements limited the coverage for plaintiff to “liability” arising from Link’s and Sunrise’s work, nothing in either the policies or the endorsements limited defendant’s obligation to provide plaintiff with a defense. (p. 575.)

Emboldened by the language of the Presley case, many developers chose to present “Presley tenders” directly to one additional insuring carrier. As a consequence, that carrier receiving the tender must assume the full and complete defense of the Additional Insured.

iii. **There Must Be A Potential For Indemnity Under The Policy:**
Interpretation Of “Arising Out Of”

These three simple words, “arising out of,” have engendered a series of cases. The scope of “arising out of” has been very broadly defined, and now appears subject to greater limitations than was initially conceived.

d. The Damage Claimed Must Have Occurred During the Policy Period.

For a duty to defend to exist, coverage must be triggered, i.e., the damage claimed must potentially have occurred during the policy period. The trigger of coverage is “that which, under the specific terms of an insurance policy, must happen in the policy period in order for the *potential* of coverage to arise.” Montrose Chemical Corp. of Cal. v. Admiral Insurance Co. (1995) 10 Cal.4th 645, 655 fn.1. In other words, there is a timing issue to be resolved before the duty to defend arises.

In Montrose, the Supreme Court of California adopted the “continuous injury” trigger of coverage for third party liability insurance lawsuits involving continuous or progressively deteriorating losses. The “continuous injury” trigger of coverage means that “bodily injuries and property damage that are continuous or progressively deteriorating throughout successive policy periods is potentially covered by all policies in effect during those periods.” Montrose, supra at 655. In other words, the timing of the accident and the date of discovery are largely immaterial.

While Montrose is technically a defense case, the continuous injury trigger of coverage applies in many contexts. It has been extended to construction defect litigation, see Pepperell v. Scottsdale Insurance Co. (1998) 62 Cal.App.4th 1045, and inter carrier contribution actions involving construction defect, see Ins. Co. of North America v.

National American Ins. Co. (1995) 37 Cal.App.4th 195. The continuous injury trigger of coverage also applies to indemnity, as well as defense. See Stonewall Ins. Co. v. City of Palos Verdes Estates (1996) 46 Cal.App.4th 1910.

2. If The Policy Indicates That There Is A Duty To Defend, What Is The Extent Of The Obligation?

Once an insurer has determined that there is a duty to defend based on the terms of the policy, its obligation is to defend entirely. The insurer will have a right to reimbursement for defending claims that are not potentially covered under the policy. Furthermore, the defense costs are subject to equitable allocation whenever multiple insurers have a duty to defend a single Additional Insured.

a. Each Insurer Has A Duty to Defend Entirely.

In Buss v. Superior Court of Los Angeles County (1997) 16 Cal.4th 35, the Supreme Court of California held that an insurer has a duty to defend entirely, even in a “mixed” action. A “mixed” action is one where some of the claims are at least potentially covered and other claims are not. Consequently, the insurer has a right to reimbursement. It can “recover those defense expenses which can be fairly and reasonably allocated *solely* to noncovered claims for which there never was any potential for coverage. [Citation].” Buss v. Superior Court of Los Angeles County (1997) 16 Cal.4th 35, 53 n.15.

To seek reimbursement for defense costs, the insurer must reserve its right at the outset. It may do so unilaterally. Further, the insurer must carry the burden of proof. That burden is by a preponderance of the evidence. Thus, in a reimbursement action there will be triable issues of material fact.

The Buss rule applies even in the context of a “Presley tender” (see Section I (c)(ii) above). In other words, even when an Additional Insured carrier is targeted with the initial tender and there are several other carriers with a duty to defend, the carrier receiving the tender is obligated to defend entirely. Consequently, that carrier is responsible for the initial defense and the coordination of Additional Insured coverage. After acceptance, the rights and obligations between co-carriers are governed by claims for contribution in equity. See, e.g. Maryland Casualty Co. v. Nationwide Mutual Ins. Co. (2000) 81 Cal.App.4th 1082, 1089 (Maryland II).

**b. An Insurer Can Seek Contribution From Other Carriers
Based On An Equitable Allocation of Defense Costs.**

Once a carrier has made payments to fulfill its duty to defend, it has a right to seek contributions from other carriers that were equally obligated to defend the Additional Insured. See supra, Maryland II at 1089. Costs are reallocated based on principles of equity, thus within the trial court’s broad discretion. Maryland Casualty Co. v. Nationwide Mutual Ins. Co. (2000) 81 Cal.App.4th 1082, 1089.

There are two different methods of reallocation: (1) equitable subrogation and (2) equitable contribution. Subrogation allows a carrier to recover the total amount spent from a single carrier that is primarily liable for the loss. See supra, Maryland II at 1088. Contribution, on the other hand, apportions costs among insurers that share the same level of liability on the same risk as to the same insured. See supra, Maryland II at 1089. Usually this doctrine is implicated when multiple insurers are obligated to indemnify or defend the same claim and one insurer has paid more than its fair share of the loss.

Typically, equitable contribution applies to reallocate costs in the Additional Insured context. Subrogation does not apply, because there is no single carrier that is primarily liable for the loss, rather there are multiple carriers that are equally liable.

The law allows multiple insurers, who have an obligation to pay under an indemnity contract, to apportion costs based on equitable contribution, as it would if dealing with an insurance agreement. In Golden Eagle Insurance Company v. Insurance Company of the West (2002) 99 Cal.App.4th 837, the court held that defense costs are sums insured is legally obligated to pay because of “property damage,” as stated in the indemnity contract. Therefore, multiple insurers are on the risk assumed by an indemnitor (e.g., a subcontractor) and there is no equitable basis for shifting the entire burden to the indemnitee’s insurer.

c. “Other Insurance” Clause

In Travelers Casualty and Surety Company v. Century Surety Company (2004) 118 Cal.App.4th 1156, the court noted that the general rule was to pro rate according to the policy limits when multiple policies shared the same risk but had inconsistent “other insurance” clauses. Between July 1988 and 1993, plaintiff issued CGL policies covering Standard Wood Structures, Inc. (“Standard”), a framing contractor. Defendant issued a primary CGL policy to Standard covering it between September 1996 and September 1997. Between 1987 and 1990, Standard performed carpentry and framing work on Canyon Estates, a residential development. In 1998, homeowners in Canyon Estates filed a lawsuit, in part alleging continuing damage to their properties caused by defect construction work. Standard was named as a defendant. Standard tendered the defense of the action to plaintiff, defendant and CNA, its primary liability insurance carriers.

Initially, all three insurers agreed to provide Standard with a defense. Defendant later withdrew its tender, citing its policy's "other insurance" clause. Plaintiff and CNA ultimately settled the claim and then sued defendant for declaratory relief and equitable contribution. Defendant's policy declared that it was excess to other valid and collectible insurance. Since plaintiff's policy contained a "pro-rata" other insurance clause, defendant asserted that plaintiff needed to exhaust the limits of its policy in defending and indemnifying the insured before defendant's duty to do so arose. Given effect to defendant's "other insurance" provision, which was in the nature of an escape clause, would have resulted and imposing on plaintiff the burden of shouldering that portion of the continuous loss attributable to the time when defendant was the only liability insurer covering the insured. Travelers Casualty and Surety Company v. Century Surety Company (2004) 118 Cal.App.4th 1156.

In Travelers Casualty & Surety Co. v. Transcontinental Ins. Co., (2004) 122 Cal.App.4th 949, Federal Insurance Company (Federal) issued an "excess" insurance policy to a real estate developer. The policy provided for a defense to the developer upon the exhaustion of a specific policy, which the parties agreed had been exhausted. The developer was also named as an "additional insured" on insurance policies issued to subcontractors working on the developer's project. The developer was sued for construction defects on the project. After paying a portion of the cost to defend the developer, Federal sought a judicial declaration that it did not have a duty to defend because the subcontractors' insurance was unexhausted "primary" insurance. See Travelers Casualty & Surety Co. v. Transcontinental Ins. Co., (2004) 122 Cal.App.4th 949.

Defendant argued that Federal's duty to defend under the excess policy was triggered because the specific primary policy referenced in the excess policy had been exhausted. The court agreed. Under the plain language of the excess policy, Federal had a duty to defend the developer against claims when the limit of the underlying insurance had been exhausted. The defense obligation was not dependent upon the exhaustion of any insurance other than "underlying insurance," which was defined as specific policies listed in a schedule. The only listed underlying insurance policy was Federal's primary policy, which had been exhausted. Because the excess policy stated that it was excess over a specifically described policy and would cover a claim when that specific primary policy was exhausted, the language was sufficiently clear to overcome the usual presumption that all primary coverage had been exhausted. The "other insurance" provision constituted a condition to payment of claims, but did not constitute a condition to coverage or the duty to defend. The developer had coverage under the excess policy upon the exhaustion of the primary policy, which obligated Federal to defend. See Travelers Casualty & Surety Co. v. Transcontinental Ins. Co., (2004) 122 Cal.App.4th 949.

3. Is An Agreement For Indemnity The Same As An Insurance Agreement?

a. Indemnity Agreements and Insurance Contracts Are Not The Same.

Indemnity is "the obligation resting on one party to make good a loss or damage another party has incurred." Rossmoor Sanitation, Inc. v. Pylon, Inc. (1975) 13 Cal. 3d 622. An indemnity agreement (e.g., a subcontract) is not an insurance policy, because the duty to indemnify only arises after liability has been established. There is also a broad

duty to defend under an insurance contract, which is not the same under an indemnity agreement. Regan Roofing Co., Inc. v. The Superior Court of San Diego County (1994) 24 Cal.App.4th 425, 436. With an indemnity contract, the burden is to prove that there is entitlement to recover damages. Whereas, with an insurance policy, the burden is to prove that there is potential coverage to trigger the affirmative defense duty.

b. Indemnity and Insurance Contracts Are Interpreted The Same.

Although different in nature, indemnity contracts and insurance policies are both interpreted with ordinary rules of contractual interpretation. The court will focus on the contract language and try to give effect to the mutual intentions of the parties.

Continental Heller Corp. v. Amtech Mechanical Services, Inc. (1997) 53 Cal.App.4th 500; Heppler v. J.M. Peters Co., Inc. (1999) 73 Cal.App.4th 1265

c. Contractual Indemnity

“Indemnity is a contract by which one engages to save another from a legal consequence of the conduct of one of the parties, or of some other person. (Civ. Code §2772). ‘A collection of rules, developed primarily in insurance and construction cases, governs actions to enforce indemnity agreements. Paramount is the rule that where the parties have expressly contracted with respect to the duty to indemnify, the extent of that duty must be determined from the contract and not by reliance on the independent doctrine of equitable indemnity.’” See Mel Clayton Ford v. Ford Motor Co. (2002) 104 Cal.App.4th 46, 54 [citations omitted].

This coverage is important in cases involving contractual indemnity issues. The CGL policy form contains a contractual liability exclusion. This exclusion provides that

the insurance does not apply to liability assumed by the insured under any contract or agreement except an “incidental contract.” “Incidental contract” generally has a narrow and impractical definition. For an additional premium, the insured can get contractual liability coverage. This coverage increases the scope of the term “incidental contract” to include any oral or written contract or agreement relating to the conduct of the named insured’s business.

Thus, if the insured purchases contractual liability coverage, the insured will receive protection when it is sued, for example, in a cross-complaint for express contractual indemnity.

d. There Is No Joint And Several Liability For Indemnity

Judgments.

In Expressions at Rancho Niguel Assoc. v. Ahmanson Developments Inc. (2001) 86 Cal.App.4th 1135, the Court of Appeal of California, Fourth Appellate District held that “joint and several liability principles do not apply in apportioning losses from an indivisible injury among joint tortfeasors.” Page 1137. Expressions is a construction defect case where the developer and the owner were strictly liable for plaintiff’s injuries. After settling with plaintiff, the owner and the developer brought an indemnity claim against a subcontractor seeking the full amount of the settlement proceeds based on joint and several liability. The court refused to apply joint and several liability in that context and instead applied equitable indemnity principles.

Therefore, multiple insurers are on the risk assumed by an indemnitor (e.g., a subcontractor) and there is no equitable basis for shifting the entire burden to the indemnitee’s insurer.