

April 9, 2008 Coverage Alert

WASHINGTON COURT OF APPEALS
RULES ATTORNEY FEES SUBJECT TO POLICY LIMITS

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On April 7, 2008, in *Great Am. Ins. Co. v. Assurance Co. of Am.*, No. 58173-2-I (Washington Court of Appeals, Div. I April 7, 2008), Division 1 of the Washington Court of Appeals held that amounts allocated for an underlying claimant's attorneys fees were subject to the primary policy's liability limits and not "costs taxed" under the supplementary payments provision of the policy. The court also held that an excess carrier had no obligation to drop down in the event of a primary insurer's insolvency where the policy specifically provided it would not do so. In addition, the court addressed equitable reapportionment between excess carriers arising from the settlement of an underlying construction defect claim as well as the availability of prejudgment interest and *Olympic Steamship* fees in equitable contribution actions.

Background

This case involved a dispute between three excess insurers over the funding of the settlement of claims against their mutual insured Polygon Northwest Company ("Polygon"). Two of the excess carriers, Assurance Company of America ("Assurance") and Ohio Casualty Insurance Company ("Ohio") sought equitable contribution from the third, Great American Insurance Company ("Great American"). During the period Assurance and Ohio provided excess coverage, Polygon maintained two million dollars in primary coverage. During each of the two years Great American provided excess coverage, Polygon purchased an additional million dollars in primary coverage from United Capital; however, United Capital became insolvent.

Polygon's settlement of the underlying claim included an allocation of \$1,486,000 for the underlying plaintiff's litigation costs, which was paid the primary insurers in addition to policy limits as Supplementary Payments. Assurance, Ohio, and other insurers contributed to the settlement; however, Great America claimed its policy had not been triggered due to the insolvency of the primary insurer.

Excess Policy Triggered, But Insurer Not Required to Drop Down

Great American argued that based upon the language of its insuring agreement, limits of insurance provision, and insolvency provision, its coverage could not be triggered until the amount of the underlying policy limits were actually paid by the insolvent insurer, by Polygon or by Polygon's other carriers. The Court of Appeals noted that the policy provided that in the event an underlying insurer's insolvency, Great American had no obligation to "drop down" to cover the insolvent insurer's obligations. Thus, the Great American excess policy was triggered once the loss exceeded the limits of the underlying

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(insolvent) policy in that year. However, Great American could not be made to contribute in equity for a loss that it did not owe in the first place, and thus it was only jointly and severally liable in each of the years in which it provided excess coverage for the amount in excess of the limits of all the collectible underlying policies plus the limits of the underlying insolvent policy in each year. Thus, for each of the two excess policy periods, Great American was jointly and severally liable for the portion of the settlement exceeding the \$3M even though \$1M was uncollectable. On the other hand, the Assurance and Ohio excess policies were each in excess of all underlying collectible insurance. Thus, Assurance and Ohio were jointly and severally liable for loss in excess of \$2M.

Subrogation and The “Made Whole” Requirement

Next, the court addressed the parties’ subrogation rights. Based upon the requirement that an insured be “made whole” before an insurer can subrogate, the court held Great American would not have subrogation rights until Assurance and Ohio recover a total of \$1M. Thereafter, the insurers would have equal subrogation rights that could be equitably allocated between them. The court’s reasoning for this result was that Assurance and Ohio paid the first million of excess, while Great American did not (due to the underlying insolvency).

“Supplementary Payments” Coverage Does Not Encompass Litigation Costs

Assurance contended that the supplementary payments provision in its policy, which obligated it to pay “[a]ll costs taxed against the insured in the ‘suit,’” had a specific meaning that did not include all legal fees or costs incurred by the insured in a lawsuit and that the plaintiff’s litigation costs were subject to policy limits.

The court reasoned that when the “costs taxed” language was read within the text and context of the policy there was no question that the language was intended to have a legal meaning. The court stressed, “. . . sophisticated business entities, would not have an understanding of a term specifically referring to a legal proceeding that is completely divorced from its standard and well-established legal usage. Further, the items included under the supplementary payments provision of its policy specifically refer to the legal process in one way or another. None arise if the insured is not involved in a lawsuit or other legal proceeding. This being the case, Great American’s attempt to read the individual words “costs” and “taxed” in isolation from the surrounding provisions, giving those words the dictionary definitions most favorable to their case, wrongly ignores the text of the supplementary payments provision itself.” Accordingly, any such “litigation costs” would be considered damages because of “property damage” and thus subject to the policy’s limits of insurance.

Pre-judgment Interest Available on Equitable Portion of an Insurer's Share of a Fixed Underlying Settlement Amount

At issue was whether the subsequent need to equitably apportion a fixed settlement obligation necessarily converted it into an unliquidated sum such that prejudgment interest should not be available. The court found that application of pre-judgment interest was proper because "allocating contribution amounts to an insurance settlement does not involve" a high level of discretion and "the sum at issue here was fixed by the terms of the Polygon settlement." Additionally, how apportionment must occur between insurers is fixed by law, so the court reasoned, "[t]he fact that a claim is disputed does not render the claim unliquidated, so long as it may be determined by reference to an objective source."

Olympic Steamship Fees Unavailable to an Insurer Seeking Equitable Contribution

The court found that because an equitable contribution claim does not involve an assignment of rights from the insured to its insurer, an insurer has no independent standing under *Olympic Steamship* to seek fees. The court reasoned that the "right of equitable contribution belongs to each insurer individually. It is not based on any right of subrogation to the rights of the insured, and is not equivalent to standing in the shoes of the insured[,]" and that the "equitable basis established in *Olympic Steamship* for attorney fee awards is limited to efforts necessary to establish coverage for claims against the insured and is based on the rights of the insured." The court stressed that Polygon's only right under its policies was to full recovery; thus, in the equitable contribution action, Assurance was not asserting Polygon's rights. Therefore an award of *Olympic Steamship* fees would be inappropriate.

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