An Insurer Is Not Obligated to Pay for Loss of Property Value When It Pays to Restore Property to Its Pre-Loss Condition.

Baldwin v. AAA Northern California, Nevada & Utah Ins. Exchange, 1 Cal. App. 5th 545 (2016)

The California Appellate Court recently ruled that an insurer's obligation to repair damaged property only required that the repair substantially restore the property to its pre-loss condition and did not also require the insurer pay for a loss of value. To require otherwise, the court reasoned, would obligate the insurer to insure the property's diminution in value and would extinguish the insurer's policy right to only pay for the repair of property.

In *Baldwin v. AAA Northern California, Nevada & Utah Ins. Exchange*, 1 Cal. App. 4th 545 (2016), the insured was the owner of a pick-up truck that was damaged in an accident. AAA insured the truck and covered the loss. The vehicle was virtually new at the time of the accident. The insurance policy stated that AAA, "may pay the loss in money or repair . . . the damaged . . . property." AAA opted to pay to repair the vehicle at a cost of $8,196. The vehicle's resale value, however, declined by $17,100 after it was repaired. The insured argued that since the repair could not restore the vehicle to its pre-loss value, the vehicle could not be repaired and AAA, therefore, was required to pay him the vehicle's diminution from the pre-loss value. The insured's position was consistent with a minority of jurisdictions that have held if an attempted repair does not result in the complete restoration of a vehicle's pre-loss condition, the vehicle is not repaired, and the resulting diminution of value of the vehicle was a loss the insurer was liable for under the insurance policy. See *Gonzales v. Farmers Ins. Co. of Oregon*, 345 Or. 382, 196 P.3d 1 (2008); *State Farm Mut. Auto. Ins. Co. v. Mabry*, 274 Ga. 498, 556 S.E.2d 114 (2001).

The Appellate Court rejected the insured's argument and the minority position. The court acknowledged that the insurance policy allowed AAA to choose to either repair the property or to pay for the vehicle's value. However, the insured and minority position eliminated this option. Implicit in the court's decision was a recognition that a damaged vehicle's resale value is never fully restored to its pre-loss value after an accident and the ensuing repairs. As a result, any time an insurer opts to exercise its right under a policy to repair a vehicle, it would be virtually impossible for the insurer to meet the standard of bringing the property's post-loss value back to its pre-accident value. Thus, the insurer would always be forced to also pay for the vehicle's diminution from the pre-loss value. Such a holding would fundamentally

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change the policy to strictly provide coverage for damaged property's diminution in value. Requiring an insurer to pay to return the vehicle to its pre-loss condition would essentially rewrite the policy to eliminate the provision allowing an insurer's election to pay for repairs.

Accordingly, the court held that an insurer's option to pay for repair only required the insurer to pay to substantially return the vehicle to its pre-loss condition. This follows the holdings of the majority of jurisdictions that do not require that the insurer also pay for the diminution in value when it pays to repair the damaged property's physical condition. *See O'Brien v. Progressive Northern Ins. Co.*, 785 A.2d 281 (Del. 2001); *Camden v. State Farm Mut. Auto. Ins. Co.*, 66 S.W.3d 78 (Mo. App. 2001); *Smith v. Superior Ins. Co.*, 802 So. 2d 424 (Fla. Ct. App. 2d 2001); *Townsend v. State Farm Mut. Auto. Ins. Co.*, 793 So. 2d 473 (La. App. Cir. 2001); *Hall v. Acadia Ins. Co.*, 801 A.2d 993 (Me. 2002); *Bailey v. Progressive County Mut. Ins. Co.*, 78 S.W.3d 708 (Tex. App. 2002); *Schulmeyer v. State Farm Fire and Cas. Co.*, 353 S.C. 491 (2003); *Given v. Commerce Ins. Co.*, 440 Mass. 207 (2003).

An Insured's Parent Company Does Not Have a Sufficient Interest in Its Subsidiary's Insurance Policy to Assert a Cause of Action Against Its Subsidiary's Insurer.

D. Cummins Corporation v. United States Fidelity and Guaranty Co., 246 Cal. App. 4th 1484 (2016)

The California appellate court recently ruled that an insured's parent company, if not an insured under the policy, has no standing to sue its subsidiary's insurer. In this matter, Cummins Corp. was insured under a liability policy issued by U.S. Fidelity. Cummins Corp.'s parent company was the aptly named Holding Co. Both Cummins Corp. and Holding Co. filed a complaint for declaratory relief against U.S. Fidelity concerning coverage for lawsuits against Cummins Corp. Holding Co. alleged that it could assert a claim for a declaratory relief because California law allowed "any person interested under a written instrument . . . or contract" to bring a claim for declaratory relief. The trial court disagreed and dismissed Holding Co. on the basis that it was not an insured under the U.S. Fidelity policy.

Holding Co. admitted it was not an insured under the U.S. Fidelity policy. Nonetheless, it argued it was an interested party to its subsidiary's policy because Holding Co. had a practical interest in the proper interpretation of the policy. Holding Co. was

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the sole entity responsible for managing the affairs of Cummins Corp. and its responsibilities included making decisions as to litigation strategy, resolution and settlement. It therefore reasoned that given its relationship and central role in pursing Cummins Corp's defense and indemnity with U.S. Fidelity's insurance assets, it was an interested party to the policy.

The appellate court agreed with U.S. Fidelity and the trial court. Accordingly, it ruled only the insured, Cummins Corp. had a direct interest in the policy and since Holding Co. was not an insured, it could not be an "interested party." The court further explained why Holding Co.'s argument, concerning its management of Cummins, Corp. was not persuasive. The court reasoned that despite Holding Co.'s argument that its involvement in the claim was necessary, Cummins Corp.'s law suit for coverage would go on despite Holding Corp.'s dismissal, demonstrating that Holding Corp. merely had an indirect interest in the law suit. Thus, any indirect interest, no matter how enthusiastic it may be, does not transfer to a legally cognizable claim for declaratory relief. The court further noted its ruling that a parent company who is not an insured and who has no interest in its subsidiary's insurance policy, is no different from California's long held principal that shareholders have no standing to sue a corporation's insurer.

Insuring Agreement Provision Stating There is No Duty to Defend If Another Insurer is Providing a Defense Found to Be Unenforceable.

Certain Underwriters at Lloyds, London v. Arch Specialty Ins. Co., 246 Cal.App.4th 418 (2016)

A provision in a general liability policy stating there is no duty to defend if another insurer is already providing a defense was found to be unenforceable. The provision was at issue in a law suit between Certain Underwriters at Lloyds, London and Arch Specialty Insurance Company.

Both Lloyd's and Arch issued a commercial general liability policy to the same insured, Framecon. The policies, however, covered different policy years and were not overlapping. Framecon was sued for ongoing and continuous injuries that occurred during two of Lloyd's policy periods and one of Arch's policy periods. Framecon tendered its defense to both insurers. Lloyd's accepted the tender. Arch rejected the tender on the basis it had no duty to defend due to a unique insuring agreement in the policy. The insuring agreement stated, "we have the right and duty to defend you . . against any suit . . . provided that no other insurance affording a defense

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against such a suit is available to you." The claims against Framecon were settled by Lloyd's and Arch. Each insurer agreed to share in the settlement payment, but Arch refused to contribute any defense costs. Lloyd's sued Arch seeking contribution for the amounts it incurred defending Framecon.

Lloyd's argued that Arch's policy term – excusing it from a duty to defend when another insurer has a duty to defend – was an unenforceable "escape clause" against public policy. Arch admitted its policy afforded coverage for the risk and that it had a duty defend. However, Arch maintained that the policy did not afford coverage for defense costs for the claims against Framecon because the "other insurance" provision was placed in the coverage agreement section of the policy, thereby limiting the scope of the coverage for Framecon's defense because of Lloyd's prior defense acceptance.

The court concluded that Lloyd's had a better argument. It noted that public policy disfavors escape clauses, whereby coverage purports to evaporate in the presence of other insurance. The court specifically pointed to, as an example, law prohibiting the enforcement of an "other insurance" clause in a policy's conditions when such a clause is used to shift the burden away from one primary insurer to another insurer. It was also noted that Arch's policy specifically set forth a duty to defend suits against its insured and it would be unfair to force Lloyd's to shoulder Framecon's entire defense, including for the year when Arch was the only insurer. The court further found that locating the clause in the insuring agreement was not sufficient to limit Arch's defense duty because that would encourage insurers to jockey for the best positon of where to locate "other insurance" provisions, needlessly complicating the drafting of policies, inducing wasteful litigation among insurers and delaying settlements, all to the detriment of the insurance buying public.

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