Imprecise Policy Language Results in Umbrella Policy Becoming Primary for Duty to Defend Purposes

Posted on June 25, 2010 by Larry Golub

On June 11, 2010, the California Court of Appeal for the Second Appellate District reissued its decision (following rehearing) in *Legacy Vulcan v. Superior Court (Transport Insurance Company)*, and held that an umbrella insurer became a "primary umbrella" insurer and was obligated to defend its insured since no scheduled underlying insurance applied, and the $100,000 self-insured retention under the umbrella policy was applicable only to the insurer's indemnity obligation.

The decision, while providing a detailed analysis of the umbrella/excess policy issued by Transport, presents more of an isolated instance of an insurer not carefully limiting the scope of its defense obligation under a policy issued nearly 30 years ago, rather than an opinion providing any broad pronouncement that umbrella insurers are to provide a duty to defend from dollar one.

Vulcan was named in multiple lawsuits claiming environmental contamination and alleging damages occurring over a number of years, including when Transport's Excess Catastrophe Liability Policy was in effect. Vulcan tendered the defense of the actions to several insurers, including Transport, but none of the insurers offered a defense. Vulcan paid for its own defense and settled the lawsuits. Transport filed a declaratory relief action against Vulcan to determine its rights and obligations under the policy.

The coverage action proceeded with the parties stipulating to resolve certain legal issues before trial, and many of the facts of the dispute (including the reasons why the underlying insurers did not provide a defense to Vulcan) did not make their way into the Court of Appeal's decision. The trial court found that Transport had no duty to defend Vulcan until it established that the applicable underlying insurance had been exhausted and upon a showing that the claims were actually covered.

In analyzing coverage under the Transport policy, the appellate court went into great detail examining the language used by Transport in its insuring agreements, limits of liability section, definitions, and conditions. The court held that the Transport policy provided both excess and umbrella coverage. With respect to the umbrella coverage portion, and based on the ambiguity of the policy's use of the unqualified term "underlying insurance" in the insuring agreement, the court held that, under the facts of this case (where no primary or underlying insurer defended Vulcan), Transport's umbrella coverage was *primary* umbrella defense coverage.

Finding the umbrella coverage to be primary, the ordinary rules regarding a primary insurer's duty to defend applied. As such, Transport was obligated to defend Vulcan regardless of the exhaustion of any underlying insurance and regardless of the provision for a $100,000 retained limit (which, in this case, was found to only apply to the duty to indemnify). Moreover, Vulcan did not need to establish that the claims were actually covered under the Transport policy to trigger the duty to defend, but merely show a potential for coverage.

In its analysis, the court made clear that the result here was based on the policy language at issue. For example, the court observed that "the impact of a policy reference to a 'self-insured retention' or 'retained limit' on the duty to defend will depend on the language of a particular policy," and it referenced cases where policy language expressly stated there was no duty to defend unless the retained limit was exhausted.

This case therefore stands as another warning to insurers to be careful in drafting policy language, and this is especially true when it come to the duty to defend.