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An Exhausting Question for Insurers

Courts consider when excess carrier's duty to defend kicks in

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Excess insurance policies are typically written so that excess coverage is triggered only by "exhaustion" of specified underlying insurance. The questions of how and when an underlying policy is "exhausted," thereby triggering an excess carrier's duty to defend, are commonly litigated issues. One particular issue that parties routinely dispute is whether a primary carrier's tender of its policy limits through an offer of settlement before the claim against the insured is settled or judgment has been entered constitutes "exhaustion" of the underlying policy.

This very question was posed as a matter of first impression before a Connecticut federal court in *Cambridge Mutual Fire Insurance v. Ketchum*, No. 3:11-CV-00743 VLB, 2012 WL 3544885 (D. Conn. Aug. 16, 2012). However, that court decided not to answer it. Instead, Cambridge, adopting a minority view, found that there was exhaustion of the primary policy where the claim for damages in the underlying action exceeded the primary carrier's liability limits, thereby triggering the excess carrier's duty to defend, regardless of whether the primary carrier tendered its policy limits.

While it is tempting to construe *Cambridge* as effectively converting an excess carrier into a "co-primary insurer" with a concurrent duty to defend, it appears that courts in Connecticut instead will look to policy language and consider the "total policy insuring intent" in determining the order of coverage as between insurers, even when both carriers' duties to defend have been triggered.

Cambridge involved a coverage dispute under a homeowner's umbrella policy. The claim related to a personal injury lawsuit arising out of a motorcycle accident, seeking damages between $400,000 and $500,000. The umbrella policy provided that the excess carrier "agree[d] to pay on behalf of the Insured the ultimate net loss which: 1) The insured becomes legally obligated to pay because of personal injury or property damage; and 2) is in excess of the retained limit." The policy further provided that the excess carrier shall provide "additional coverage" for an occurrence which is covered under the policy and "is either: 1) not covered by any primary insurance shown in the schedule or any other insurance which applies; or 2) covered by a primary policy under which one of these additional coverages has been exhausted."

At the time of the accident, the insured had primary coverage through an automobile liability policy with liability limits of $250,000. Although the primary carrier offered to partially settle the underlying claim for its policy limits, the claimant argued that the settlement offer could not practically be effected until the excess carrier agreed to assume the defense of the insured for the balance of the claim or participated in an overall settlement. The excess carrier refused to assume the defense, arguing that its duty to defend was never triggered because an offer of settlement up to the policy limits did not constitute an exhaustion of the automobile policy.

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In considering whether the automobile policy had been exhausted, *Cambridge* acknowledged that "a majority of states to have addressed this issue have held that the excess carrier's duty to defend is not triggered until the policy limit of the primary carrier is exhausted by settlement or tender of payment, even if the claim for damages in the underlying action exceeds the primary carrier's limit and the excess carrier's policy will necessarily be implicated in the action." According to the majority view, this is so because the terms of the contract should be enforced as written, and it would be inappropriate for courts to alter the parties' respective obligations and economic expectations.

In contrast to the majority view, the court wrote that a "minority of states have found that the excess carrier's duty to defend is triggered once the excess carrier becomes aware that the claim for damages in the underlying action will exceed the primary carrier's policy limit." As *Cambridge* acknowledged, no Connecticut court had squarely addressed the issue and therefore it was a matter of first impression. *Cambridge* ultimately found the rationale of the minority view more persuasive and concluded that an "excess carrier has a duty to defend where there is a reasonable possibility that a defendant's excess coverage may be reached despite the fact that a primary insurer has undertaken the defense as well."

To date, the decision is the only case to directly consider this issue in Connecticut. By contrast, a recent Superior Court decision disagreed with *Cambridge*, albeit in dicta, finding the "majority position more persuasive and more consistent with our well-established standards of insurance policy interpretation." *R.T. Vanderbilt v. Hartford Accident & Indemnity*, No. X02UWYCV075016321, 2014 WL 1647133, at *3 (Conn. Super. Ct. March 28, 2014) (J. Shaban) (appeal pending). R.T. Vanderbilt's disagreement with Cambridge portends that a split of authority may develop in Connecticut on this issue.

If Connecticut courts adhere to the minority view adopted in *Cambridge*, an excess carrier's duty to defend would in theory be triggered on the initiation of any action where the damages sought exceed the primary policy's limits. As a consequence, *Cambridge* can be interpreted to transform an excess carrier into a co-primary insurer with a co-extensive duty to defend. However, in Connecticut, the mere existence of the duty to defend on the part of an excess carrier does not necessarily mean that an excess carrier will be required to concurrently contribute to a loss on a pro rata basis with a primary carrier. In determining the order of coverage between insurers, Connecticut courts will consider the language of the triggered policies, including competing "other insurance" clauses, as well as the "total policy insuring intent" of those policies.

The Connecticut Supreme Court has recognized that "other insurance' clauses are valid for the purpose of establishing the order of coverage between insurers, as long as their enforcement does not compromise coverage for the insured." *Aetna Casualty & Surety v. CNA Insurance*, 221 Conn. 779, 783, 606 A.2d 990, 992 (1992). It is not uncommon for "other insurance" clauses between responding policies to compete and conflict with each other. In interpreting competing "other insurance clauses," the Connecticut Supreme Court has instructed courts to carefully read the language of policies in their entirety to reconcile any conflict or ambiguity that "may arise when identical or similar 'other insurance' clauses exist and if enforcement of clauses would not produce adverse consequences for the insured, clauses should be enforced as written to establish order of coverage between insurers."

However, where two "other insurance" clauses are truly "mutually repugnant" and incapable of being reconciled, courts should look to the "total policy insuring intent" test wherein the "function and intent of the various policies are examined to determine whether logic dictates that they be ranked in a particular order." *Scottsdale Ins. v. Underwriters at Lloyd's London*, No. CV064022710S, 2009 WL 3284231, at *7 (Conn. Super. Ct. Sept. 8, 2009). The court in Scottsdale added: "Under the 'total policy insuring intent' test, a policy designed to cover the risk in question takes precedence over a policy which only incidentally covers that risk."

In instances where both the "other insurance" clauses are mutually repugnant and the "total policy insuring intent" is the same between policies, courts often require both policies to jointly contribute their pro rata share based on the total limits of insurance. Indeed, the U.S. Court of Appeals for the Second Circuit, interpreting Connecticut law, has found that where two policies contemplate the same risk equally, such as where two policies both purport to be true excess policies, the policies will be found to provide concurrent coverage. *Continental Casualty v. Aetna Casualty & Surety*, 823 F.2d 708, 712 (2d Cir. 1987).

However, true excess policies seldom have the same insuring intent as a primary policy, as those policies do not contemplate the same risk equally. Under this analysis and reasoning, an excess carrier will likely not be required to contribute pro rata to a loss concurrently with a primary carrier, but may be required to respond to a loss concurrently with other excess carriers.

While *Cambridge* may not always convert an excess carrier into a co-primary insurer, one potential outcome of the decision is to encourage early settlement of claims by ensuring that all potentially responding carriers—both primary and excess—are actively involved from the inception of the claim.