Determining the true policy limits for a policy-limits demand

A look at the limits of liability under five insurance scenarios demonstrates why it's not always easy to make a true policy-limits demand

BY ALEXANDER F. STUART

There is a famous scene in the movie, Jerry Maguire, where the character played by Cuba Gooding, Jr. demands of his stressed out agent, "Show me the money!" That telling line could have been uttered in the real world of civil litigation, where determining the amount of money available to satisfy a judgment is critical to settlement negotiations. Plaintiff lawyers want to know the limits of coverage applicable to their clients' claims so they can make the all-important "policy limits demand."[1]

In last month's Plaintiff Magazine, my partner Ron Cook advised how to make an effective policy limits demand once an insurer's limits of liability are determined. This article will address limits of liability themselves, employing five examples to demonstrate how determining the amount of coverage can be a complicated and challenging endeavor.

Bodily Injury Claims: One policy; One or more limits

You represent two burn victims who suffered catastrophic injuries when two fire protective suits burst into flame. Your lawsuit names the manufacturer of the suits. The manufacturer produces a copy of its general liability policy providing bodily injury coverage of $1 million per occurrence. You notice that the policy has an aggregate limit of $2 million for "products-completed operations." You want to send the insurer a demand letter for its full limits of coverage. How much do you demand?

The answer can be tricky. If your clients were not wearing the suits and were burned when the fire spread to their location, there probably is only one occurrence, and thus one limit of $1 million for all injuries suffered. Most general liability policies define an "occurrence" as an "accident, including continuous or repeated exposure to the same general harmful conditions." Those same policies typically provide that the limit of liability per occurrence applies to all damages arising from a single occurrence, regardless of the number of persons injured, the number of claims made, the number of claimants seeking damages, or the number of insureds sued. In California, the test is one of simple proximate causation.[2] Was there one, or more than one, proximate cause of injury with respect to conduct of the insured?

Assume for a moment that your clients were both wearing the fire protective suits, and that each was injured separately, although relatively close in time. For example, assume that one of your clients caught fire upon exposure to a flame, and that your other client caught fire while attempting to rescue him. Assume further that your second client would not have caught fire if he had simply chosen to walk away. One occurrence or two occurrences? One policy limit or two?

In a case similar to this one, plaintiffs' counsel concluded that there were two proximate causes of injury – failure of the first suit followed by failure of the second suit during an attempted rescue – and made a demand for $2 million, the full aggregate limit for products-completed operations. The insurer rejected the demand, offering only $1 million under the mistaken, but not unreasonable, belief that there was only one occurrence arising from a single fire. On summary judgment, the United States District Court ruled that there were two occurrences as a matter of law.[3]

The case later settled against the suit manufacturer for $6 million – well in excess of the $2 million aggregate limit for products-completed operations. It was not a defense that the insurer had misconstrued its coverage reasonably. The Supreme Court has held that an insurer gambles with its own money when it rejects a reasonable settlement demand within the limit of its coverage.[4] By failing to accept a reasonable policy limits demand, the insurer becomes responsible for all damages ultimately awarded against its insured.

Bodily Injury Claims: Multiple policies; Multiple limits

Assume that your two burn clients were engaged in a paintball contest, and

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that the premises for the contest were owned by the same corporate entity that manufactured their clothing. Assume further that one of them was riding in a jeep operated by an employee of the premises owner, and that the employee negligently lost control of the Jeep causing it to crash and explode. The accident occurs on the premises – a guest ranch miles from public roadways. The Jeep is used exclusively on those premises and belongs to the premises owner, who has a separate general liability policy covering accidents on the premises with an occurrence limit of $1 million. The employee driver has his own automobile liability policy with an accident limit of $500,000. How much do you demand?

As any careful lawyer might say, it depends. If the second burn victim was injured while attempting to rescue the first victim from the explosion, there should be two occurrences with respect to the manufacturer's liability under the policy covering its manufacturing operations. There also should be an entirely separate occurrence, and additional limit of liability, for the cause of the fire – i.e., negligent operation of the Jeep. While general liability policies, as a rule, exclude coverage for liability arising from the use of an automobile, they often except from the definition of an "auto" any vehicle used exclusively on the insured premises. Barring provisions in the manufacturer's two policies that prohibit the stacking of policy limits, you now have $3 million to demand.

But there is more. The employee driver (who most likely is covered by the manufacturer's premises policy as an insured person) has his own automobile policy, with a separate "accident" limit of $500,000. The policy applies to his owned automobiles and any non-owned automobile (a vehicle neither owned by the employee nor furnished for his regular use) while operated with the owner's permission. Hold on, you might say. The Jeep did not qualify as an "auto" for purposes of an automobile exclusion in the premises liability policy. How can it be a covered "auto" under the employee's automobile liability policy? Welcome to the strange world of insurance law, where language of exclusion is construed quite differently from language of inclusion. Under an automobile liability policy defining "auto" as any vehicle capable of use on a public roadway, your clients could net an additional $500,000 of coverage.

Personal Injury Claims: One policy; multiple limits

While in the hospital, your two burn clients learn that hospital staff has published confidential information about their medical conditions in violation of common law and statutory rights of privacy. As luck would have it, the publication includes confidential records of 2,573 other patients, and you now have a bevy of clients. The hospital has a general liability policy affording "personal injury" coverage in addition to the ordinary bodily injury and property damage protection. Consistent with the norm for personal injury coverage, the term "personal injury" is defined as injury, other than bodily injury, arising out of one or more specifically enumerated "offenses." The offenses include "oral or written publication of material that violates a person's right of privacy." Assume that the hospital's policy has a declarations page stating that the limit of liability for personal injury is $1 million. What do you demand?

Read the policy carefully. Most general liability policies state that the limit for "personal injury" applies to each person injured. A separate limit therefore would apply under most policies for the damages of each person whose rights of privacy were violated. While it is doubtful that any one plaintiff's damages come close to $1 million, the damages of all plaintiffs collectively most likely exceed $1 million. Plaintiff's counsel should be careful not to demand $1 million in hopes of opening a policy limit, risking under-settlement of the case.

Some general liability policies, particularly manuscript policies written for a specific insured, lump all injuries arising from personal injury into one policy limit for any series of related offenses that result in injuries to more than one person. If such a policy were issued here, plaintiff's counsel would want to demand the $1 million limit of coverage, since there would be no additional coverage for any of the claims.

Errors and Omissions Claims: One policy, multiple limits

One of your burn clients dies, leaving his estate to two children. The lawyer who handled his estate planning also handles the estate administration. The estate plan is deficient, exposing the estate to unnecessary taxes, and the lawyer compounds his errors by failing to file the estate's tax return timely. The children ask you to pursue a malpractice claim against the lawyer, who has a professional liability policy providing $1 million of coverage per claim, with an annual aggregate limit of $3 million. The estate planning errors cause more than $3 million of damage. The return filing error causes an additional $1.5 million of penalties and interest. How much do you demand?

Unlike a general liability policy, which provides coverage for occurrences or offenses, a professional liability policy usually provides coverage for "claims." Most professional liability policies, particularly lawyer malpractice policies, confine their limits of coverage for any one claim to all "related claims." Thus, two or more claims arising out of a single act, error or omission, or a series of related acts, errors or omissions, are deemed a single claim for purposes of limits of insurance.

The Supreme Court has held that the term "related" can be broad enough to encompass both logical and causal relationships.[5] For example, in a case involving a lawyer who committed a series of errors handling a collection matter, the court held that all errors were related for purposes of determining the number of

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claims.[6] The errors included failing to serve a stop notice and failing to foreclose on a mechanic's lien. The court held that both errors were related, noting that they arose out of the "same specific transaction, the collection of a single debt."[7] The court observed that the errors arose as to the same client and resulted in the same injury – the loss of the debt.

Contrast the estate planning and estate administration errors. The former harmed both the client and his heirs. The latter harmed only the heirs. The transactions were different. The estate planning errors did not cause the return filing error. If the lawyer had filed the tax returns timely, the only injuries would have been those caused by his deficient estate planning services. In this case, plaintiff's counsel should demand $2 million for two unrelated claims, barring any surprises in the policy.

Not surprisingly, there often are surprises in insurance policies, and professional liability policies are no exception. A policy might provide that coverage is excluded for acts occurring prior to a certain date, ordinarily known as the "retroactive" date. For example, if the lawyer started a new law firm between the time of his estate planning errors and the time of his return filing error, the policy might exclude the estate planning errors. It is not uncommon for lawyer malpractice policies to provide a "retroactive" date that coincides with the inception of a new law firm. If the defendant lawyer failed to procure "tail coverage" for acts occurring prior to the inception of his new law firm, the limit of liability could be $1 million – for the return filing error alone.

Property Damage Claims: Multiple policies; one or more limits

Sometimes the odds are just against you. The surviving burn victim buys one of those condominiums that becomes a timeshare in a lawsuit. The good news is that he comes to you to represent his homeowners association against the builder of the complex. The bad news is that the builder has a series of general liability policies with prior work exclusions, and he is named on only two subcontractor policies as an additional insured. The bad news gets worse. The two subcontractor policies are issued to the same subcontractor, and both have "anti-stacking" provisions stating that the number of policies does not increase the limits of insurance. Each policy provides $1 million of coverage per occurrence, with an aggregate limit of $2 million for "products-completed operations." The cost to repair the condominium complex is $5 million. How much do you demand?

Once again, the correct answer depends. What are the construction defects? How was the project built – at one time, or in phases? If built in phases, was any phase put to its intended use before the other phases were complete? Do the sales contracts have attorney's fees provisions, or is there another basis for obtaining an award of fees? These, and other questions, can determine whether the answer is $1 million, $2 million, more than the $2 million, or perhaps even less than the single $1 million occurrence limit of coverage.

Recall the first bodily injury example above. One fire, two occurrences – two limits of liability. If the project suffers from isolated defects – say roof truss defects and siding defects – and the subcontractor is a framer, then there could be two occurrences.[8] The argument for two occurrences is more compelling if the roof trusses were installed under one contract and the siding under another contract.

Read the builder's own general liability policies. When are the prior work exclusions effective? Does the prior work date stay the same under each policy – e.g., April 1, 2005 – or does it coincide with the inception date of each policy – e.g., April 1, 2005 under the first policy, April 1, 2006 under the next policy? If the builder performed work in phases, and one of those phases was not completed before the prior work date of the second policy, the builder might have coverage under that policy for property damage to the last phase during the policy period.

Look carefully at the sales contracts and other documents describing rights of the condominium owners. Is there any basis for obtaining an award of attorney's fees? General liability policies usually contain "supplementary payments" clauses that provide coverage for costs taxed against the insured in any suit the insurer defends. This coverage includes prevailing party attorney's fees where provided by contract.[9] Until recently, most insurers provided unlimited supplementary payments coverage. The plaintiff's lawyer might want to demand both the applicable limit of property damage coverage and a substantial portion of the lawyer's fees, assuming of course that the clients are entitled to a prevailing party fees award.

The plaintiff's attorney should not overlook the insured's aggregate limits when formulating a demand. If the "products-completed operations" limits of the applicable policies have been reduced by the payment of judgments or settlements in other cases, the remaining limits might be less than a single occurrence limit of $1 million. A demand for that one occurrence limit therefore would not expose the insurer to an opening of its limits, since the demand would exceed the available coverage.

Conclusion

The five examples above demonstrate that determining the amount of applicable coverage can be difficult. It is recommended that the plaintiff's lawyer consider consultation with an expert in insurance policy interpretation to be sure that the amount of applicable coverage is not missed, either by a demand for too little or a demand for too much. An insurance expert can show the plaintiff's lawyer the right amount of money, allow-

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ing the lawyer to make a proper policy limits demand that increases the potential for a successful resolution of the case.

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Endnotes

1 See *Murphy v. Allstate Ins. Co.* (1976) 17 Cal.3d 937, 941 [failure to accept a reasonable policy limits demand – i.e., where there is a substantial likelihood of a judgment exceeding the insurer's applicable limit of coverage – exposes the insurer to liability for all damages awarded against the insured].

2 *Caldo Oil Co. v. State Water Resources Control Bd.* (1996) 44 Cal.App.4th 1821, 1828.

3 See *Evanston Ins. Co. v. Ghillie Suits.com, Inc.,* 2009 WL 734691 [slip opinion not approved for publication].

4 *Johansen v. California State Auto. Assn. Inter-Ins. Bureau* (1975) 15 Cal.3d 9, 16.

5 *Bay Cities Paving & Grading, Inc. v. Lawyers' Mutual Ins. Co.* (1993) 5 Cal.4th 854, 868.

6 *Id.*

7 *Id.* at 873.

8 See *Chu v. Canadian Indemnity Co.* (1990) 224 Cal.App.3d 86, 96-98 [coverage for each set of distinct defects must be analyzed separately].

9 *Prichard v. Liberty Mutual Ins. Co.* (2000) 84 Cal.App.4th 890, 911-912.

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