The War Between Primary and Excess Carriers

The current dynamic between primary and excess liability insurance carriers.
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American Alternative Insurance Corp. v. Hudson Specialty Insurance Co. 938 F.Supp.2d 908 (C.D. Ca. 2013) addressed this question. In this case, the court dealt with a dispute between the primary insurer and the excess insurer regarding their responsibilities to settle the underlying action. Two issues addressed by the court included:

1. Whether a primary insurer can state a claim against the excess carrier for equitable subrogation;

   AND

2. Whether a primary insurer can state a claim against the excess carrier for equitable indemnity.

The Underlying Action
The accident occurred when Minuteman provided valet parking services for The Fantasy Springs Casino in Riverside County, California. In October 2008, a Minuteman employee struck Tory Fretz in the Casino’s parking lot. Ms. Fretz was treated in the hospital for 4 days. She also required follow up visits with several other surgeons. Ms. Fretz sued Minuteman in Riverside Superior Court.

Hudson insured Minuteman under a primary insurance policy. The policy provided liability coverage up to $1 million. American Alternative Insurance Corporation (“AAIC”) insured Minuteman under an excess insurance policy with available coverage of $4 million after exhaustion of the $1 million Hudson primary policy. The excess policy stated AAIC would “assume charge of the settlement...of any claim or suit against the insured when the aggregate Limit of Liability of the primary policy was exhausted by payment of claim.”

Defense counsel formulated an evaluation report based on Ms. Fretz’s injuries and gave a recommended settlement range of $500,000 to $700,000. Ms. Fretz offered to settle the action for $1 million, which Hudson rejected. After her neuropsychologist testified she suffered significant psychological impairment, Ms. Fretz’s settlement demand increased to $3 million. Hudson made its policy limits available to settle, and Hudson and AAIC countered with a $1.25 million offer. Ms. Fretz increased her demand to $5 million. AAIC authorized up to $5 million to settle the case but did not offer this amount. At trial, the jury found in Ms. Fretz’s favor for close to $7.2 million. Hudson paid the $1 million policy limits and AAIC funded the remainder.

AAIC sued Hudson, alleging Hudson was obligated to pay the entire judgment against Minuteman plus prejudgment costs and interest. Hudson counterclaimed alleging AAIC unreasonably failed to settle the underlying action. Hudson claimed AAIC was responsible for defense costs after AAIC failed to settle, plus costs and interest paid as part of the final judgment.

Equitable Indemnity, Equitable Subrogation, or Both?
Simply stated, Hudson can bring a claim for equitable subrogation, which permits the insurer to assume its insured’s rights and assert all claims against another insurer. The court held under a theory of equitable subrogation, an excess insurer has a good faith obligation to a primary insurer to reasonably settle a case. In Diamond Heights Homeowners Assn. v. Nat’l Am. Ins. Co. (1991), 227 Cal.App.3d 563, 578, the court held that “any insurer, whether excess or primary, in conducting settlement negotiations, is subject to an implied duty of good faith and fair dealing which requires it to consider the interests of the insured equally with its own and evaluate settlement proposals as though it alone carried the entire risk of loss.” Both excess and
primary insurers may bring a claim under the theory of equitable subrogation. Other California courts have found a contrary rule would “imperil the public and judicial interests in fair and reasonable settlements of lawsuits.”

However, in answer to the second question, Hudson cannot bring a claim for equitable indemnity against AAIC. The right to indemnify is based upon a legal relationship between the parties. The court held because there is no underlying contractual relationship between Hudson and AAIC, a primary insurer owes no independent duty of good faith and fair dealing to an excess insurer.

**What Do We Learn?**
Both primary and excess carriers in California should acknowledge their good faith obligations to one another. This obligation exists, even for the excess carrier, as soon as the action commences. The excess carrier’s obligation can still arise well before the primary policy has been exhausted. Thus primary and excess carriers need to coordinate not only reasonable but timely settlements.

**ABOUT THE AUTHOR**
Kelly Denham graduated from Loyola Law School in 2012. Ms. Denham’s primary focus at Tyson & Mendes is construction defect litigation.