

April 27, 2023

Related Professionals

Rebecca S. Hummel

Related Practice Groups

Construction

Insurance Litigation & Coverage

Litigation

New “No Voluntary Payments” Decision in California in Favor of Insurer

On March 30, 2023, the California Court of Appeal issued a new published decision, affirming orders granting summary adjudication and summary judgment in favor of an insurer on the “no voluntary payments” issue.

In *Santa Clara Valley Water District v. Century Indemnity Company*, the District brought an action against Century alleging that Century breached its contract and committed bad faith when it refused to indemnify and reimburse the District for approximately \$8.4 million in costs the District incurred in complying with a Consent Decree it entered into with the Fish & Wildlife and other entities (collectively, “the Trustees”) to resolve a natural resources damages claim (“NRD”) brought against it.

The Court of Appeal for the Sixth Appellate District issued its published opinion upholding the trial court’s orders granting Century’s summary judgment motion on the grounds that the no voluntary payments provisions contained in primary and excess policies barred the District from seeking indemnification for expenses it incurred as a result of its entry into a Consent Decree to settle a lawsuit without notice to Century of the lawsuit or the entry into the Consent Decree.

In August of 2000, the District notified Century of potential NRD claims against it. Century issued a response on May 31, 2001 stating it had no duty to defend the claims because the NRD was not a “suit” as defined by the primary policies. Century also advised the District that no coverage was afforded under the excess policies unless and until the underlying policies were exhausted, and reserved its rights under the policies. On June 4, 2002, the District advised it had retained coverage counsel, but did not otherwise provide Century any further information on the status of the underlying NRD claim. There was no further communication from the District to Century concerning the claim until April 22, 2008.

In the interim period, on May 11, 2005, the District signed a proposed Consent Decree. On July 28, 2005, the United States filed a lawsuit against the District and, on that same day, the fully executed Consent Decree was filed in the federal action. Pursuant to this Consent Decree, the District agreed to fund, commence and complete remediation work required by the Trustees.

Nearly three years after the entry of the Consent Decree, on April 22, 2008, the District wrote to Century seeking indemnity under the primary and excess policies for the federal action, advising Century that it had incurred approximately \$4 million dollars in completing work outlined in the Consent Decree, with approximately 60% more work to be done. On July 3, 2008, Century responded, advising that it reserved its rights under the policies, and alluding to the policies’ no voluntary payments (NVP) provisions. Approximately six years later, the District advised Century that it had effectively completed the work under the Consent Decree, and included detailed documents concerning the work performed and associated costs. On January 14, 2015, Century advised the District of the coverage issues, including the NVP provisions as a potential bar to coverage.

MusickPeeler

On October 5, 2015, the District initiated the lawsuit against Century alleging that it was entitled to indemnity under the primary and excess policies issued by Century. Century filed, and the trial court granted, two separate motions, one for summary adjudication and another for summary judgment, on the grounds that coverage for the underlying claim was barred because the District failed to comply with the NVP provisions, thus precluding coverage under all of the primary and excess policies issued to the District. On appeal, the Court upheld the trial court's orders.

The Court of Appeal acknowledged that the wrongful denial of a defense or coverage constitutes breach of contract, and in such instance, allows the insured to seek indemnity for a reasonable settlement with third parties without the insurer's consent. However, the Court concluded that the principle did not apply because Century's initial response to the tender of the NRD claim properly set forth Century's then-existing obligations under both the primary and excess policies, and was not a declination of coverage. As of May 31, 2001, when Century issued its coverage position, Century's primary policies were not yet implicated as no lawsuit had been filed against the insured, and no obligation existed under its excess policies because the underlying policies had not yet been exhausted. Thus, Century had not denied coverage, but had reserved its rights.

The Court concluded that the August 2000 notice to Century was only of a potential claim, and such notice did not relieve the District of its obligation to notify Century in the event that the potential claim had ripened into a lawsuit, or if the insured later learned of information that indicated the likelihood that the underlying policy's liability would be exhausted thus triggering the excess policies' indemnification obligations.

The Court dismissed the District's argument that its payment was involuntary. While the Court conceded that an insured can prevent the application of the NVP provision if its payment is involuntary, the circumstances which constitute an involuntary payment (*i.e.*, when an insured is unaware of the identity of the insurer or contents of the policy, or is faced with a situation requiring immediate response to protect its legal interests) did not exist here. The District knew Century's identity, and there was nothing that required the District to enter into the Consent Decree immediately and without prior notification to and approval from Century.

Most importantly, the Court also rejected the District's argument that the NVP provisions are exclusionary clauses that are subject to strict construction against the insurer. The Court held: "[a]n NVP provision, both generally and in this instance, is a term and condition prohibiting the insured from making a voluntary payment or a voluntary undertaking of liability, rather than an exclusion that removes from coverage certain risks under the policy." This reasoning was repeated in the Court's rejection of the District's equitable estoppel and waiver arguments: "[f]urther, although the NVP provisions were conditions, not exclusions, waiver cannot be based upon Century's failure to specifically mention them in the May 31, 2001 letter." The principles of waiver and estoppel did not apply because the Court agreed that the May 31, 2001 letter issued by Century did not constitute a declination letter, but instead reflected the then accurate coverage positions regarding Century's obligations under its primary and excess policies.

The Court upheld Century's reliance on the NVP provisions because the District had remained silent for years, and had failed to notify Century of the federal lawsuit filed against the District and its entry into the Consent Decree for more than three years. Therefore, Century was not obligated to reimburse the District for any portion of the \$8.4 million the District incurred under the Consent Decree.

The decision is a favorable development for insurers in California – even if the facts of the case are somewhat unique. It is a reminder to policyholders of their duties to cooperate and not undertake payment without the consent of their

MusickPeeler

carrier. Likewise, it is a reminder for insurers to carefully consider the NVP and no action clauses when interacting with the policyholder or issuing coverage position letters.