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**WASHINGTON COURT OF APPEALS UPHOLDS
INSOLVENCY PROVISIONS IN EXCESS POLICY
Also Rules Attorney's Fees Are Not Recoverable
In An Equitable Contribution Action**

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In *Polygon Northwest Co. v. American Nat. Fire Ins. Co.*, --- P.3d ----, 2008 WL 921390 (April 7, 2008), the Washington Court of Appeals, Division I, held that: (1) an excess insurer's indemnity obligation does not commence until the insured's liability exceeds the limits of all underlying insurance, including the limits of an insolvent primary insurer's policy; (2) attorney's fees do not constitute "costs taxed against the insured," within the meaning of a "supplemental payments" provision; (3) prejudgment interest may be awarded against insurers failing to pay their equitable share in funding a settlement; and, (4) an insurer may not recover attorney's fees in an equitable subrogation action.

In *Polygon*, Assurance Company of America ("Assurance") and Ohio Casualty Insurance Company ("Ohio") brought claims against Great American Insurance Company ("Great American") for equitable contribution to a settlement funded by Assurance and Ohio on behalf of their mutual insured, Polygon. The lawsuit giving rise to the settlement was brought by the homeowners association of a condominium project known as Sammamish Pointe against Polygon, the builder. The homeowners association alleged the existence of various serious construction defects arising prior to 1996 and continuing through 2000.

Polygon tendered defense of the Sammamish Pointe action to its liability insurers, including Assurance, Ohio, United Capitol, Great American, and Commercial Underwriters Insurance Company (CUIC). Polygon had primary and excess insurance for the years 1996 – 2000, as follows: for the year 1996-1997, Polygon had a \$1 Million primary policy with Assurance and a \$10 Million excess policy with Assurance; for the year 1997-1998, Polygon had a \$1 Million primary policy with CUIC and a \$10 Million excess policy with Ohio; for

the years 1998-1999 and 1999-2000, Polygon had a \$1 Million primary policy with United Capitol and a \$50 Million excess umbrella policy with Great American. However, United Capitol became insolvent in November of 2000. As such, the total primary insurance available to Polygon for the relevant years (i.e., 1996 – 2000) was \$2 million.

Assurance, along with CUIC, United Capitol (before its insolvency), and two other insurers that provided additional insured coverage, Valley Insurance Company (Valley) and Truck Insurance Exchange (Truck), funded Polygon's defense." Following mediation, Polygon reached a \$7.8 million settlement with the homeowners, of which \$6,314,000 was for payment of the claims and \$1,486,000 was for the homeowners' "litigation costs." Great American did not fund any part of the settlement because it claimed that its excess insurance had not been triggered because of United Capitol's failure to pay its underlying limits, due to insolvency. The participating insurers paid into the settlement as follows:

Assurance	\$ 5,413,666.67
CUIC	\$ 1,743,000.00
Ohio	\$ 483,333.33
Valley	\$ 100,000.00
Truck	\$ 60,000.00
TOTAL	\$ 7,800,000.00

To facilitate the settlement, CUIC and Assurance each paid half (i.e., \$743,000) of the homeowner's litigation costs (\$1,486,000), meaning that each paid \$743,000 more than their \$1 Million primary limits. The settlement agreement also allowed Polygon, Assurance, and Ohio to jointly pursue claims against the implicated subcontractors, and to share in any recovery.

The trial court ruled that because Polygon's legal liability clearly exceeded the \$1 million limit of each of United Capitol's underlying policies, Great American was required to contribute to the settlement. The trial court subsequently characterized the \$2 million not paid by United Capitol because of its insolvency as a "gap" in primary coverage that equity required to be apportioned equally among the three excess insurers for all four policy years. The trial court also ruled that the \$1,486,000 of the homeowners' "litigation costs," split between Assurance and CUIC as the solvent primary insurers, were "costs taxed against the insured" in the lawsuit and, as such, had been correctly characterized as the responsibility of Assurance and CUIC pursuant to the "supplementary payments" provisions of their primary insurance policies. The trial court further concluded that the underlying settlement amount was a liquidated sum and awarded prejudgment interest from the date of settlement to Assurance from both Great American and Ohio. Finally, the trial court concluded that Assurance and Ohio were Polygon's assignees with respect to the contribution action and awarded attorney fees with respect to the coverage dispute.

On appeal, Great American argued that its excess coverage never took effect because there were no "losses paid" by United Capitol, nor "exhaustion" of United Capitol's policy limits, per the limits of insurance provisions. Great American also argued that to find that coverage was triggered would be to force it to replace its underlying insurance, in violation of its insolvency provisions. The Washington Court of

Appeals held that Great American's excess obligation was triggered because the insured's liability exceeded the \$3 Million of primary insurance (\$1 Million Assurance, \$1 Million Ohio, and \$1 Million Capitol), including the primary insurance of the insolvent insurer (Capitol). As such, the Court of Appeals held that Great American was not required to pay "first dollar" indemnity, nor fill the "gap" created by Capitol's insolvency, in keeping with the policy's insolvency provision. Rather, Great American was found to be jointly and severally liable, as to each of the two policy periods it insured, for sums in excess of \$3 million (the total limits of primary insurance) up to the full settlement amount of \$7.8 million. While the insolvency provision did not relieve Great American of its excess obligation, Great American was not required to "drop down" to fill the insolvent insurer's liability.

With regard to Assurance and Ohio's payments of \$743,000 each for the homeowner's attorney's fees, which were made in excess of policy limits under the supplemental payments provisions, the Court of Appeals held that the payments were not properly considered "costs taxed against the insured," and therefore should not have been considered supplemental payments. Rather, the Court of Appeals found that "taxable costs" only included statutory costs as defined in RCW 4.84.010, and not reasonable attorneys fees. Accordingly, the homeowners association's attorney's fees were considered part of the loss to be apportioned among the insurers.

With regard to prejudgment interest, the Court of Appeals remanded to the trial court to calculate the prejudgment interest to be assessed against Great American and Ohio based on the amount of the settlement liability that it decides to equitably allocate to those insurers. Finally, the Court of Appeals held that Assurance's claims for equitable contribution against the jointly liable co-insurers did not arise from the rights of the insured, but rather from its own rights as an overpaying insurer. Accordingly, Assurance, as the overpaying insurer, was not entitled to attorney's fees under the Washington law allowing insureds or their assignees to recover attorneys fees when they are forced to engage in litigation to receive the full benefit of the insurance contract.

Any party can request that the state supreme court review this decision. William Knowles and Tylor Laney will issue a supplemental Alert if review is requested and granted. Cozen O'Connor is a nationally recognized leader in representing the insurance industry in all coverage areas.