



LEXSEE 2009 U.S. DIST LEXIS 77222

**LLOYD CHARTRAND, Plaintiff, v. ILLINOIS UNION INSURANCE COMPANY
and DOES 1-50, inclusive, Defendants.**

No. C 08-05805 JSW

**UNITED STATES DISTRICT COURT FOR THE NORTHERN DISTRICT OF
CALIFORNIA**

2009 U.S. Dist. LEXIS 77222

August 28, 2009, Decided

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For Illinois Union Insurance Company, a corporation , Defendant: Darren Burke Le Montree, LEAD ATTORNEY, Wilson, Elser, Moskowitz, Edelman & Dicker LLP, Los Angeles, CA; James Anthony Stankowski, Wilson Elser et al LLP, Los Angeles, CA.

JUDGES: JEFFREY S. WHITE, UNITED STATES DISTRICT JUDGE.

OPINION BY: JEFFREY S. WHITE

OPINION

ORDER DENYING DEFENDANT'S MOTION FOR SUMMARY JUDGMENT AND GRANTING PLAINTIFF'S CROSS-MOTION FOR SUMMARY JUDGMENT

Now before the Court are the cross motions for summary judgment filed by Plaintiff Lloyd Chartrand ("Chartrand") and Defendant Illinois Union Insurance Company ("Illinois Union") on the issue of insurance coverage. The Court finds the motions appropriate for decision without oral argument. N.D. Civ. L.R. 7-1(b).

Accordingly, the hearing date of September 4, 2009 is HEREBY VACATED. Having carefully reviewed the parties' papers, considered their arguments and the relevant legal authority, the Court hereby DENIES Illinois Union's motion for summary judgment and GRANTS Chartrand's cross-motion [*2] for summary judgment.

BACKGROUND

This is an insurance coverage dispute between Chartrand and Illinois Union arising out of Plaintiff's demand for a defense and indemnity for claims asserted against him under a commercial liability insurance policy. Chartrand, the insured, contends that the defense costs incurred in the underlying lawsuit are covered under the Directors and Officers ("D&O") liability policy issued by Illinois Union. Illinois Union claims the defense costs are excluded by virtue of the Insured v. Insured Exclusion in the policy barring coverage for a claim asserted by an insured. By way of its motion for summary judgment, Illinois Union seeks to have the Court find that it had no duty to defend or indemnify Chartrand in the underlying tendered action and that given the absence of coverage, Illinois Union is not liable for breach of contract and breach of the covenant of good faith and fair dealing. By his cross-motion, Chartrand seeks reimbursement of attorneys' fees and costs reasonably incurred in his defense in a lawsuit currently pending in Sonoma County Superior Court, *Carl B. Johnston Revocable Trust v. Mentura, Inc.*, SCV 240480

("JRT Action").

Illinois Union issued [*3] to Mentura, Inc. ("Mentura") a D&O policy, effective November 25, 2005 to November 25, 2006 ("the Policy"). The insuring clause of the Policy provides, in pertinent part:

The Insurer shall pay the Loss of the Directors and Officers for which the Directors and Officers are not indemnified by the Company and which the Directors and Officers have become legally obligated to pay by reason of a Claim first made against the Directors and Officers during the Policy Period, or, if elected, the Extended Period, and reported to the Insurer pursuant to subsection E.1. herein, for any Wrongful Act taking place prior to the end of the Policy Period.

(See Stipulation, Ex. 1 at 16.)

The term "Claim" is defined in the Policy as: "a written demand against any Insured for monetary damages or non-monetary or injunctive relief [or] a civil proceeding against any Insured seeking monetary damages or non-monetary or injunctive relief, commenced by the service of a complaint or similar pleading." (*Id.*)

Exclusion C.1(e), known as the Insured v. Insured Exclusion of the Policy provides:

Insurer shall not be liable for Loss under this Coverage Section on account of any Claim:

e) brought or maintained by, on behalf [*4] of, or at the direction of any Insured in any capacity, any Outside Entity or any person or entity that is an owner of or joint venture participant in any Subsidiary in any respect and whether or not collusive,....¹

(*Id.* at 19.)

¹ Chartrand contends that the Insured v. Insured Exclusion from the D&O policy from 2004-2005 should apply. The earlier policy provides merely that the "Insurer shall not be liable to make

payments under this Coverage Section in connection with any Claim ... by, on behalf of, or at the direction of any of the Insureds." (See Stipulation, Ex. 2 at 42.) Illinois Union concedes that "the language of the Insured v. Insured Exclusion [from the operative, later policy] was not materially in variance with the prior policy's Insured v. Insured Exclusion. (Opp. Br. at 6.) The Court similarly does not find the difference in policy language dispositive.

On November 21, 2005, Carl B. Johnston submitted a claim letter, indicating that various named claimants had made claims against Mentura for failure to disclose "material facts concerning the Company's licenses, trademarks, patents and freedom from trademark and patent infringement." (*Id.* at Ex. 7.) Claimants indicated that had [*5] they had such information, they would not have made investments in Mentura. (*Id.*) By letter from Jonathan Yee of Mentura dated November 22, 2006, tender was made to Illinois Union three days before expiration of the Policy. By letter dated February 23, 2007, Illinois Union declined coverage for the claim on the basis of the Insured v. Insured Exclusion, contending that because Mentura's Chairman of the Board, Yee, was also a claimant, the claim fell within the exclusion. Following the initial claim letter, additional claimants filed three separate, although related and remarkably similar, lawsuits against Mentura and its officers and directors in the Superior Court of California in the County of Sonoma ("the Underlying Actions").

There is no significant dispute of material fact presented to this Court. The legal question is whether the Insured v. Insured Exclusion applies to preclude coverage where there are claims asserted by both insureds and parties who are not insureds. There is no binding authority on the issue, so the Court must review persuasive authorities from other jurisdictions.

The Court shall address additional facts as necessary to its analysis in the remainder of this [*6] Order.

ANALYSIS

A. Legal Standard on Motion for Summary Judgment.

A court may grant summary judgment as to all or a part of a party's claims. *Fed. R. Civ. P. 56(a)*. Summary judgment is proper when the "pleadings, depositions,

answers to interrogatories, and admissions on file, together with the affidavits, if any, show that there is no genuine issue as to any material fact and that the moving party is entitled to judgment as a matter of law." *Fed. R. Civ. P. 56(c)*. An issue is "genuine" only if there is sufficient evidence for a reasonable fact finder to find for the non-moving party. *Anderson v. Liberty Lobby, Inc.*, 477 U.S. 242, 248-49, 106 S. Ct. 2505, 91 L. Ed. 2d 202 (1986). A fact is "material" if the fact may affect the outcome of the case. *Id.* at 248. "In considering a motion for summary judgment, the court may not weigh the evidence or make credibility determinations, and is required to draw all inferences in a light most favorable to the non-moving party." *Freeman v. Arpaio*, 125 F.3d 732, 735 (9th Cir. 1997).

A principal purpose of the summary judgment procedure is to identify and dispose of factually unsupported claims. *Celotex Corp. v. Catrett*, 477 U.S. 317, 323-24, 106 S. Ct. 2548, 91 L. Ed. 2d 265 (1986). The party moving for summary judgment [*7] bears the initial burden of identifying those portions of the pleadings, discovery, and affidavits which demonstrate the absence of a genuine issue of material fact. *Id.* at 323. Where the moving party will have the burden of proof on an issue at trial, it must affirmatively demonstrate that no reasonable trier of fact could find other than for the moving party. *Id.* Once the moving party meets this initial burden, the non-moving party must go beyond the pleadings and by its own evidence "set forth specific facts showing that there is a genuine issue for trial." *Fed. R. Civ. P. 56(e)*. The non-moving party must "identify with reasonable particularity the evidence that precludes summary judgment." *Keenan v. Allan*, 91 F.3d 1275, 1279 (9th Cir. 1996) (quoting *Richards v. Combined Ins. Co.*, 55 F.3d 247, 251 (7th Cir. 1995)) (stating that it is not a district court's task to "scour the record in search of a genuine issue of triable fact"). If the non-moving party fails to make this showing, the moving party is entitled to judgment as a matter of law. *Celotex*, 477 U.S. at 323.

B. Governing Insurance Coverage Principles.

A liability insurer owes a duty to defend whenever there is a potential for [*8] indemnity coverage under the insurance policy. *See, e.g., Montrose Chem. Corp. v. Superior Court*, 6 Cal. 4th 287, 299-300, 24 Cal. Rptr. 2d 467, 861 P.2d 1153 (1993). Where any allegation demonstrates a potential for coverage, the insurer must mount and fund the defense of the entire action, including

claims for which there is no potential for coverage. *Buss v. Superior Court*, 16 Cal. 4th 35, 48, 65 Cal. Rptr. 2d 366, 939 P.2d 766 (1997). In order to determine whether an insured has made a claim for covered damages, the court must compare the underlying complaints with the terms of the policy. *Waller v. Truck Ins. Exch.*, 11 Cal. 4th 1, 18, 44 Cal. Rptr. 2d 370, 900 P.2d 619 (1995). If the underlying complaints and any relevant extrinsic evidence submitted by the insured do not demonstrate that the underlying claims seek damages that are potentially covered under the policy, the insurance company has no duty to defend. *Id.* at 19.

To interpret the meaning of the policy language, courts must first look at the written provisions of the policy. "If the policy language is clear and explicit, it governs. ... When interpreting a policy provision, we must give its terms their ordinary and popular sense, unless used by the parties in a technical sense or a special meaning is given to them by usage." *Palmer v. Truck Ins. Exch.*, 21 Cal. 4th 1109, 1115, 90 Cal. Rptr. 2d 647, 988 P.2d 568 (1999) [*9] (citations omitted). In undertaking this analysis, courts must read limitations on coverage narrowly and insuring agreements "broadly so as to afford the greatest possible protection to the insured." *MacKinnon v. Truck Ins. Exch.*, 31 Cal. 4th 635, 648, 3 Cal. Rptr. 3d 228, 73 P.3d 1205 (2003) (quoting *White v. Western Title Ins. Co.*, 40 Cal. 3d 870, 881, 221 Cal. Rptr. 509, 710 P.2d 309 (1985)).

Policy exclusions are strictly construed, while exceptions to exclusions are broadly construed in favor of the insured. *MacKinnon*, 31 Cal. 4th at 648; *Aydin Corp. v. First State Ins. Co.*, 18 Cal. 4th 1183, 1192, 77 Cal. Rptr. 2d 537, 959 P.2d 1213 (1998). An insurer cannot escape its basic duty to insure by means of an exclusionary clause that is unclear. Any exception to the performance of the basic underlying obligation must be so stated as clearly to apprise the insured of its effect. *MacKinnon*, 31 Cal. 4th at 648.

A policy provision is ambiguous if it is susceptible to two or more reasonable constructions. *E.M.M.I., Inc. v. Zurich American Ins. Co.*, 32 Cal. 4th 465, 470, 9 Cal. Rptr. 3d 701, 84 P.3d 385 (2004). Any ambiguous terms are interpreted in favor of finding coverage, consistent with the insured's reasonable expectations. *Id.* Policy language must be interpreted as a reasonable lay person would read it, not as it might [*10] be analyzed by an attorney or insurance professional. *Id.*; *see also Crane v.*

State Farm Fire & Casualty Co., 5 Cal. 3d 112, 115, 95 Cal. Rptr. 513, 485 P.2d 1129 (1971). "[W]ords ... are to be understood in their ordinary and popular sense, rather than according to their strict legal meaning" unless used by the parties in that sense. Cal. Civ. Code § 1644.

Chartrand has the initial burden of demonstrating that, interpreting the facts and allegations most favorably to himself, construing any ambiguities in the Policy in favor of the insured and construing exclusions strictly against Illinois Union, it is possible that the Policy could potentially cover some damages alleged in any part of the tendered Underlying Actions. See *Montrose*, 6 Cal. 4th at 300. It is then Illinois Union's burden to demonstrate, again construing all ambiguities and restraints on coverage in favor of Chartrand, that there was no possibility of coverage for any claim made in the Underlying Actions. See *id.*

C. The D&O Coverage May Cover the Underlying Actions.

Because Chartrand has met his initial burden to show some coverage for the Underlying Actions and Illinois Union cannot meet its burden to demonstrate that, at the time it denied coverage, it had [*11] facts and information conclusively demonstrating that there was no potential for coverage under the D&O provision, the Court finds that Illinois Union had a duty to defend under the Policy. See *Montrose Chem.*, 6 Cal. 4th at 299-300.

The Court accepts as true the undisputed fact that the Underlying Actions include both insureds and claimants who were not insureds under the Policy. Under California law, policy exclusions are strictly construed, while exceptions to exclusions are broadly construed in favor of the insured. *MacKinnon*, 31 Cal. 4th at 648. The Insured v. Insured Exclusion is applicable when the insurer demonstrates that the "allegations of the complaint place the claims squarely within the language of the exclusion." *Bodewes v. Ulico Casualty Co.*, 336 F. Supp. 2d 263, 273 (W.D.N.Y. 2004). Under California law which construes exclusions narrowly, the Court finds that the operative exclusionary clause does not limit coverage for defense costs associated with the claims made by parties who do not qualify as insureds. Further, under California law, all insurance policies incorporate principles of allocation, whether or not the policy contains an explicit allocation clause. See [*12] *Buss*, 16 Cal. 4th at 50 ("As to the claims that are not even potentially covered, however, the insurer may indeed seek reimbursement for defense

costs.")

Because the allegations in the Underlying Actions include complaints by uninsured plaintiffs, the duty to defend was triggered. See, e.g., *Megavail v. Illinois Union Ins. Co.*, 2006 U.S. Dist. LEXIS 53658, 2006 WL 2045862, *2-3 (D. Or. July 19, 2006) (holding that the exclusionary clause was not a complete bar to defendant's obligation to defend the underlying lawsuit where duty is triggered by the presence of uninsured plaintiffs in the underlying lawsuit); see also *Level 3 Communications, Inc. v. Federal Insurance Co.*, 168 F.3d 956, 960 (7th Cir. 1999) (holding that the presence of an insured party "could conceivably contaminate the entire litigation," but found that the allocation clause of the contract dealt "with this problem in another way, by requiring allocation of covered and uncovered losses"); see also *Home Federal Savings and Loan Ass'n of Niles v. Federal Insurance Co.*, 2007 U.S. Dist. LEXIS 68558, *12-13 (N.D. Ohio Sept. 4, 2007) (holding that because the policy did not clearly exclude the claims brought by non-insureds, the insurance company had [*13] obligation to defend the underlying litigation, subject to the allocation); but see *Sphinx International, Inc. v. National Union Fire Ins. Co. of Pittsburgh*, 226 F. Supp. 2d 1326, 1336-37 (M.D. Fla. 2002) (holding that, under Florida law and in the absence of an express allocation clause or implied principle, if even a single plaintiff in the underlying case is an insured, the Insured v. Insured Exclusion bars any defense or indemnity obligation).

Because under California law, all insurance policies incorporate principles of allocation, the Court finds persuasive the reasoning of the out-of-circuit cases finding the Insured v. Insured Exclusion not to preclude coverage for all underlying suits where instituted by both insured and non-insured claimants where the court can allocate the costs of defense. See, e.g., *Federal Insurance Co. v. Infoglide Corp.*, 2006 U.S. Dist. LEXIS 53734, 2006 WL 2050694, *5-6 (W.D. Tex. July 18, 2006) (holding that the existence of an allocation clause clearly contemplated cases in which covered claims could be combined with non-covered claims and the inclusion of an insured as a plaintiff does not bar coverage for the entire claim). Therefore, the Court finds that Illinois Union's duty [*14] to defend was triggered as there was a potential for indemnity coverage under the Policy. See *Montrose Chem.*, 6 Cal. 4th at 299-300.

CONCLUSION

For the foregoing reasons, the Court DENIES Illinois Union's motion for summary judgment and GRANTS Chartrand's cross-motion for summary judgment. The parties shall submit a joint case management statement by no later than September 25, 2009 and shall appear for a status conference on October 2, 2009 at 1:30 p.m.

IT IS SO ORDERED.

Dated: August 28, 2009

/s/ Jeffrey S. White

JEFFREY S. WHITE

UNITED STATES DISTRICT JUDGE