California Court Addresses Payment of Self-Insured Retention

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In its recent decision in *National Fire Ins. Co. of Hartford v. Federal Ins. Co.*, 2012 U.S. Dist. LEXIS 641 (N.D. Cal. Jan. 4, 2012), the United States District Court for the Northern District of California had occasion to consider the issue of whether an insured was required to satisfy a self-insured retention with its own funds, or whether the retention could be paid by other insurance.

The insured in *National* was a restaurant located within a hotel. The restaurant hosted a graduation party at which a three-year old girl fell to her death from a balcony. The girl's family brought a wrongful death suit, initially against the hotel only, which was insured by Federal Insurance Company. The hotel tendered its defense to National, the primary insurer for the restaurant, on the basis that the hotel qualified as an additional insured under the restaurant's policy. While National initially denied coverage to the hotel, it later paid its policy limit to plaintiffs in order to secure a settlement on behalf of the restaurant and the hotel. National then brought a contribution claim against Federal.

After finding that the hotel was, in fact, entitled to additional insured coverage under the policy National issued to the restaurant, the court addressed the issue of priority of coverage as between the National and Federal policies, and the related issue of whether payments made by National on behalf of the hotel satisfied the Federal policy's self-insured retention. The Federal policy had a $250,000 self-insured retention and the policy provision concerning payment of the retention stated that "[w]e have no obligation or liability under such Coverages unless and until the applicable Self-Insured Retentions … are exhausted by payments you make … You must pay all self-insured retention expenses." Thus, from the face of this provision, only the insured could pay the retention.

Citing to the 2010 California state court decision in *Forecast Homes, Inc. v. Steadfast Ins. Co.*, 181 Cal. App. 4th 1466 (Cal. App. 2010), Federal argued that this policy language required the hotel to pay the retention with its own funds, and that the retention could not be insured. The court rejected this argument, however, noting that in *Forecast Homes*, the provision concerning payment of the self-insured retention expressly stated that "Payment by others, including but not limited to additional insureds or insurers, do not serve to satisfy the self-insured retention." By contrast, the Federal policy contained a "Bankruptcy Within the Self-Insured Retention" provision stating that the bankruptcy of any insurer, or any other person, would not relieve the hotel of its obligation to satisfy the retention. This language, explained the court, implied that the retention could be paid by other insurers, or other persons, and at the very least, did not "clearly require the hotel to satisfy the SIR out of its own pocket." In other words, the bankruptcy provision negated the otherwise clear policy provision stating that the retention must be paid by "you."

This aspect of the *National Fire* decision adds to the body of California case law dating back to *General Star Nat. Ins. Corp. v. World Oil Co.*, 973 F. Supp. 943 (C.D. Cal. 1997) and *Vons Cos. v. United States Fire Ins. Co.*, 78 Cal. App. 4th 52 (Cal. App. 2000), and more recently in cases such as *Forecast Homes*, *Mt. McKinley Ins. Co. v. Swiss Reinsurance Am. Corp.*, 757 F. Supp. 2d 952 (N.D. Cal. 2010); *Travelers Indem. Co. v. Arena Group 2000*, L.P., 2007 U.S. Dist. LEXIS 17931 (S.D. Cal. 2007). These cases establish the general rule that absent express and unambiguous language restricting payment of a retention to the insured, California courts will allow retentions to be satisfied by secondary sources, including other insurance.