Case No. S236765

IN THE SUPREME COURT OF THE

STATE OF CALIFORNIA

LIBERTY SURPLUS INSURANCE CORPORATION, *et al.*,

Plaintiffs and Respondents,

v.

LEDESMA AND MEYER CONSTRUCTION COMPANY, INC., *et al.*,

Defendants and Appellants.

After Order Certifying Question by the U.S. Court of Appeals for the Ninth Circuit

# APPLICATION FOR PERMISSION TO FILE AN AMICUS CURIAE BRIEF AND PROPOSED BRIEF OF AMICI CURIAE COMPLEX INSURANCE CLAIMS LITIGATION ASSOCIATION AND AMERICAN INSURANCE ASSOCIATION IN SUPPORT OF LIBERTY SURPLUS INSURANCE CORPORATION

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## APPLICATION FOR LEAVE TO FILE AMICUS CURIAE BRIEF

## TO THE SUPREME COURT OF CALIFORNIA:

The Complex Insurance Claims Litigation Association ("CICLA") and the American Insurance Association ("AIA") (together, "amici") respectfully request permission of this Court to file the accompanying *amicus curiae* brief.

CICLA and AIA are leading trade associations of major property and casualty insurance companies. The members of CICLA and AIA write a substantial amount of insurance both in California and nationwide. CICLA and AIA member companies offer all types of property-casualty insurance, including personal and commercial auto insurance, commercial property and liability coverage for small business, workers' compensation, homeowners' insurance, medical malpractice coverage, and product liability insurance.

Amici seek to advise courts in understanding and resolving issues of importance to the insurance system. Amici have participated in numerous insurance cases throughout the country, including important cases before this Court.[1] Amici have a national perspective and in-depth knowledge of the important issues presented in this case, which will substantially impact

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[1] *See, e.g., Fluor Corp. v. Superior Court of Orange Cnty.* (2015) 61 Cal.4th 1175; *Hartford Cas. Ins. Co. v. J.R. Marketing L.L.C.* (2015) 61 Cal.4th 988; *State v. Cont'l Cas. Co.* (2012) 55 Cal.4th 186.

insurers and policyholders throughout the State. Amici respectfully submit that their unique perspective will assist the Court in deciding this case and the important principles at stake.

Amici are familiar with the issues before this Court and the scope of their presentation and believe that further briefing is necessary to address matters not fully addressed by the parties' briefs, including broader policy considerations. Amici can provide an important perspective to this Court and therefore respectfully requests that their *amicus curiae* brief be filed and considered by this Court.

Pursuant to Rule 8.200(c)(3), no party or any counsel for a party in the pending appeal authored the proposed *amicus curiae* brief, in whole or in part, or made a monetary contribution intended to fund the preparation or submission of the brief. The brief is funded by the amici.

Dated: April 24, 2017

CROWELL & MORING LLP

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## AMICUS CURIAE BRIEF

## I. STATEMENT OF THE CASE

Amici incorporate by reference the Statement of the Case and Procedural History of This Coverage Action sections set forth in Respondent Liberty Surplus Insurance Corporation's Answering Brief on the Merits. (Respondent's Answering Brief on the Merits at pp. 3-16).

Briefly, Amici understand that this case stems from sexual assault committed by an employee of Appellant Ledesma & Meyer, Darold Hecht. Hecht was a supervisor on a construction project involving the San Bernardino County Unified School District prior to the beginning of the 2006-2007 school year. Allegedly, Hecht was a registered sex offender in California prior to his employment, and sexually abused a student in October and November 2006, during which time he was working for Ledesma. Ledesma was sued in connection with the allegations against Hecht and tendered the claim to its insurer, Liberty.

Liberty issued a Commercial General Liability policy and Commercial Umbrella policy to Ledesma, both effective June 1, 2006 to June 1, 2007. Liberty's primary policy was an occurrence based policy and contained the following insuring agreement.

> a. We will pay those sums that the insured becomes legally obligated to pay as damages because of "bodily injury" . . . to which this insurance applies. We will have the right and duty to defend the insured against any "suit" seeking those damages. However, we will have no duty to defend the insured against any

"suit" seeking damage for "bodily injury" . . . to which this insurance does not apply . . . .

b. This insurance applies to "bodily injury" . . . only if:
(1) The "bodily injury" . . . is caused by an "occurrence" . . . .

The policy defined an "occurrence" as "an accident, including continuous or repeated exposure to substantially the same general harmful conditions." The umbrella policy also required bodily injury to be caused by an "occurrence," which was defined the same way as in the primary policy.

Liberty filed a coverage action against Ledesma. A California District Court held in Liberty's favor that there was no occurrence under its policy. Ledesma appealed to the Ninth Circuit, which certified a question for review to this Court.

## II. SUMMARY OF ARGUMENT

The Ninth Circuit certified the following question to this Court:

> Whether there is an "occurrence" under an employer's commercial general liability policy when an injured third party brings claims against the employer for the negligent, hiring, retention, and supervision of the employee who intentionally injured the third party.

The answer to the question is no.

As explained below, Appellants improperly attempt to sidestep the question by asking the Court to focus on policy exclusions rather than the insuring clause. That is contrary to California law. The initial step in any coverage determination is to determine whether the claim comes within the

policy's insuring clause. Only if the claimant can meet that burden are policy exclusions considered. In this case, the certified question should be determined by focusing on the policies' insuring clauses.

Based on case law and the insuring clause language, the relevant conduct in determining whether there is an occurrence and thus, the possibility of coverage, is the act that directly caused the alleged injury. It follows that an employer's liability for an employee's intentional conduct such as sexual assault is not covered, because the alleged harm is directly caused by the employee's intentional act, notwithstanding any act or failure to act by the employer. The employer's negligence at most creates the possibility of future injury and is not the proper focus. What is more, the State's public policy against insuring intentional conduct supports a finding that employers are not entitled to coverage for their employees' intentional torts such as sexual assault.

## III. ARGUMENT

### A. To determine the certified question, the Court must focus on the insuring clause, not exclusions

The rules regarding interpretation of insurance policies are well-settled. The first step in deciding whether any claim is covered is to determine if it comes within the applicable insurance policy's insuring clause. Appellants' argument that coverage can be decided by reference to policy exclusions "without first having to decide whether the conduct was

accidental in the first instance" is contrary to (i) how insurance policies are interpreted, and (ii) established burdens of proof in the insurance context.

Like any contract, interpretation of an insurance policy is governed by the mutual intent of the parties at the time of contracting. (*Shell Oil Co. v. Winterthur Swiss Ins. Co.* (1993) 12 Cal.App.4th 715, 736-37). Judicial interpretation is controlled by "'the clear and explicit' meaning of these provisions, interpreted in their 'ordinary and popular sense,' unless 'used by the parties in a technical sense or a special meaning is given to their usage." (*Id.* at 737, citations omitted).

Contrary to Appellants' assertion, it is a fundamental principle in insurance law that the "insuring clause is the foundation of the agreement and forms the basis of all obligations owed to the insured." (*Dominguez v. Financial Indem. Co.* (2010) 183 Cal.App.4th 388, 400). The insuring clause identifies the risks covered by the policy, while exclusions remove coverage for risks that would otherwise be covered. (*Id.*).

Accordingly, coverage is first determined by looking to the insuring clause rather than the exclusions. (*Collin v. American Empire Ins. Co.* (1994) 21 Cal.App.4th 787, 803). The insuring clause and its occurrence requirement is not a "vague multipurpose exclusion," but rather sets forth the coverage afforded by the policy that an insurer has agreed to provide. (*Fidelity & Deposit Co. v. Charter Oak Fire Ins. Co.* (1998) 66 Cal.App.4th 1080, 1086). "[I]f the insuring clause does not cover a claimed loss, then

there is no coverage [and] . . . no need to consider policy exclusions because exclusions serve to limit coverage granted by an insuring clause and thus apply only to hazards *covered* by the insuring clause." (*Old Republic v. Superior Court* (1998) 66 Cal.App.4th 128, 144 *rev'd on other grounds Vandenberg v. Superior Court* (1999) 21 Cal.4th 815 (emphasis in original)).

Moreover, procedurally, it is the insured's burden to prove a claim falls within the terms of the insuring clause. (*Waller v. Truck Ins. Exch., Inc.* (1995) 11 Cal.4th 1, 16, citing *Collin,* 21 Cal.App.4th at 803). If the insured does not meet that initial burden, then the insurer does not have to show that coverage is removed by an exclusion because there is no coverage in the first place. Appellants' argument flips the burden of proof -- placing the initial burden on the insurer - and essentially erases the occurrence requirement in the insurance agreement. However, California courts have long condemned the judicial redrafting of private contracts, acknowledging that judicially created insurance coverage leaves "ordinary insureds to bear the expense of increased premiums necessitated by the erroneous expansion of their insurers' potential liabilities." (*See Garvey v. State Farm Fire & Cas. Co.* (1989) 48 Cal.3d 395, 408).

These standard rules should be followed here. The insurance process is heavily reliant on the predictability of insurance contracts. Insurers agree, by means of carefully tailored contractual instruments, to

bear certain risks for consumers and businesses in return for the consideration of correspondingly priced premiums. Disregarding clear contract provisions would threaten this delicate insurance mechanism. Failure to enforce the terms of insurance policies as written would undermine the stability and predictability of the insurance market. This Court should uphold the occurrence limitation and the "caused by" language in the policy to find no coverage here.

Further, California law demands that only the written provisions of contracts, including insurance contracts, will govern, as long as they are "clear and explicit." (*Bank of the West v. Superior Court* (1992) 2 Cal.4th 1254 1264). Parties expect that courts, if called upon to resolve a dispute, will follow this fundamental rule in interpreting insurance contracts. Judicial fidelity to this basic principle of California law is vital to retain the confidence of insurers and other businesses that the bargain made will be the bargain enforced.

Thus, in deciding the certified question, the Court should not bypass the threshold question of whether the injury in question was caused by an occurrence. Rather, this Court should follow established insurance law principles regarding the interpretation and application of insurance policies by focusing on whether the injury comes within the policy's insuring clause.

### B. The occurrence requirement focuses on the direct cause of the alleged injuries.

Most liability policies, such as those at issue in this case, cover damages for bodily injury caused by an occurrence. Whether there is an occurrence depends on the direct cause of the injury, not some remote act that had the potential for producing a future event.

The insuring clauses in the policies at issue state that the insurer will pay those sums for which the insured becomes liable "because of 'bodily injury' . . . to which this insurance applies." (*Liberty Surplus Ins. Corp. v. Ledesma & Meyer Constr. Co.* (2016) 834 F.3d 998, 1001). Further, the insurer does not have to defend "any 'suit' seeking damages for 'bodily injury' . . . to which this insurance does not apply." (*Id.*). The insurance applies only to "'bodily injury' . . . caused by an occurrence" that takes place in the coverage territory and if the bodily injury occurs during the policy period. (*Id.*). The term "occurrence" means "an accident, including continuous or repeated exposure to substantially the same general harmful conditions." (*Id.*). Finally, pursuant to California law, the term "accident" means "an unexpected, unforeseen, or undesigned happening or consequence from either a known or an unknown cause." (*Delgado v.*

*Interinsurance Exch. of Auto. Club of So. Calif.* (2009) 47 Cal.4th 302, 308).[2]

Insuring clauses focus on the direct cause of the injury because the term occurrence is a causal event, defined as an accident. (*Shell Oil Co.* 12 Cal.App.4th at 750). "[T]he term 'accident' does not apply to an act's consequence, but instead applies to the act itself." (*Id.* at 751 citing *Commercial Union Ins. Co. v. Superior Court* (1987) 196 Cal.App.3d 1209). Moreover, the term "caused by," modifies the term occurrence. In other words, it is not enough for the insured to simply point to conduct at some point in the causal chain of events that may qualify as an occurrence. Rather, an insured must show that the occurrence directly caused the bodily injury or property damage at issue.

California law is clear that the proper focus is on the direct injury-causing conduct in determining whether there is an occurrence. For instance, in *Delgado*, this Court held that the term occurrence "refers to the injury-producing acts," not an earlier act creating the mere possibility of injury. (*Delgado*, 47 Cal.4th at 315). The Court explained that, with respect to intentional assaults, it is the use of force on another that is the direct cause of the injury. This is true even though "[a]ny given event,

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[2] Some other liability policies define an occurrence as "an accident or an event." Because the policies at issue in this case do not do so, that language is not addressed in this brief.

including an injury, is always the result of many causes." (*Id.* at 315). The Court added that looking "to acts within the causal chain that are antecedent to and more remote from the assaultive conduct would render legal responsibilities too uncertain." (*Id.* at 315-16). *See also, Maples v. Aetna Cas. & -Surety Co.* (1978) 83 Cal.App.3d 641, 647-48 ("the term 'accident' unambiguously refers to the event causing damage, not the earlier event creating the potential for injury").

Moreover, in *Quan v. Truck Ins. Exch.*, the Court of Appeal addressed the occurrence requirement in a case involving sexual assault. (*Quan v. Truck Ins. Exch.* (1998) 67 Cal.App.4th 583). There, the court focused on the actual sexual assault, despite allegations of accidental bodily touching, in deciding that there was no occurrence. (*Id.* at 595-96). The court stated that insurance coverage is determined by the nature and kind of risks covered, which depends on the insuring clause, not merely the allegations in a complaint. (*Id.* at 595). The court also explained that "negligent" and "accidental" are not synonymous; an accident is never present when someone performs an intentional act like sexual molestation. (*Id.*).

Indeed, the narrow focus of insuring clauses is required by the phrase "caused by an occurrence." By contrast, other parts of insurance policies use different language, such as "arising out of," which courts have given a broad interpretation and have found does not connate any causal

connection. (*Acceptance Ins. Co. v. Syufy Enterprises* (1999) 69 Cal.App.4th 321, 328 ("It is settled that this language does not import any particular standard of causation or theory of liability into an insurance policy")). However, this broader meaning has not been given to the phrase "caused by." (*Marquez Knolls Prop. Owners Assn., Inc. v. Executive Risk Indem., Inc.* (2007) 153 Cal.App.4th 228, 236 ("the term 'arising out of' is interpreted more broadly than 'caused by'") (citations omitted)).

Accordingly, based on the language of the insuring clause and California law, the direct cause of the alleged bodily injury is the relevant conduct in determining whether the occurrence requirement is met. That is so because insuring clauses unambiguously refer to the conduct directly causing the alleged injury as the risk insured. They do not cover antecedent conduct far down the chain of causation. It follows that claimants cannot manufacture an occurrence by alleging negligence claims against an insured for an injury caused by the intentional conduct of another.

### C. Employers are not entitled to coverage for damages flowing from an employee's intentional conduct such as sexual assault because the injury-causing conduct is not accidental and the employer's involvement is too removed to be considered an occurrence under the policy

In cases involving employee's sexual assault, there is no doubt that the direct cause of the injury is the intentional act of the perpetrator. As the Court of Appeal phrased it: "the act is the harm." (*J.C. Penney Cas. Ins. Co. v. M.K.* (1991) 52 Cal.3d 1009, 1019 ("There is no such thing as

negligent or even reckless sexual molestation. The very essence of child molestation is the gratification of sexual desire. The act is the harm. There cannot be one without the other.")). In fact, courts are nearly unanimous across the country that there is no coverage for sexual assault because, by its very nature, it is intentional, not accidental. (*J.C. Penney*, 52 Cal.3d at 1014 ("near unanimous precedent in this state and others" precludes coverage for damages "caused by an insured's sexual molestation of a child"); (*Merced Mut. Ins. Co. v. Mendez* (1989) 213 Cal.App.3d 41 (oral copulation not an accident); *Quan*, 67 Cal.App.4th at 596 (rape not an accident notwithstanding insured's mistaken belief that victim consented); *Lyons v. Fire Ins. Exch.* (2008) 161 Cal.App.4th 880 (sexual attack not an accident notwithstanding insured's subjective belief of victim's state of mind); *Coit Drapery Cleaners, Inc. v. Sequoia Ins. Co.* (1993) 14 Cal.App.4th 1595, 1606-07 ("the acts of sexual harassment alleged are, by their very nature, intentional and wrongful; it would be contrary to public policy to allow a wrongdoer which is directly and strictly liable for such wrongdoing, such as Coit, to shift the loss resulting from such an unlawful corporate practice to its insurers").

An employer's negligent failure to prevent an employee from committing a sexual assault is not the injury causing event for purposes of insurance. The employer's conduct is too removed and far down the chain of causation to constitute an occurrence. At most, the employer's

malfeasance creates the possibility of future harm. But it cannot be said that the employer is the direct cause of the alleged injury. Regardless of how inattentive the employer is, the injury requires an intentional act by an employee.

California federal courts have addressed this issue and agree that there is no occurrence under an employer's liability policy for claims arising out of sexual assault committed by an employee. In *Farmer v. Allstate Ins. Co.*, a case involving coverage for sexual molestation claims, a California district court held that there was no coverage because "the injury causing events were clearly Mr. Varela's [husband of day care operator] molestations of Plaintiff – without such behavior, Plaintiff would not have brought the underlying action against the Varelas [husband and wife]." (*Farmer v. Allstate Ins. Co.* (C.D. Cal. 2004) 311 F.Supp.2d 484, 493). The court added that negligence that enables a perpetrator to commit sexual assault merely creates the potential for injuries; it does not directly cause the injuries. (*Id.*). Likewise, in *American Empire Surplus Lines Ins. Co. v. Bay Area Cab Lease*, a California district court held that a cab company's alleged negligent hiring and supervision of an employee that committed sexual assault did not constitute an occurrence. The court stated that the negligent hiring and supervision merely created the potential for harm, and that the actual sexual assault was the act that caused the claimants injuries.

(*American Empire Surplus Lines Ins. Co. v. Bay Area Cab Lease* (N.D. Cal. 1991) 756 F. Supp. 1287, 1289-91).

In fact, other jurisdictions have held that negligence claims against an employer that are connected with an employee's intentional tort do not constitute an occurrence. (*See, American Guar. & Liab. Ins. Co. v. 1906 Co.* (5th Cir. 1997) 129 F.3d 802, 810 (no occurrence "where negligence claims against an employer, such as negligent hiring, negligent training, and negligent entrustment, are related to and interdependent on the intentional misconduct of an employee"); *SCI Liquidating Corp. v. Hartford Fire Ins. Co.* (11th Cir. 1999) 181 F.3d 1210, 1215 (pursuant to several Georgia cases, there is no coverage for insured's alleged negligent hiring and retention of employee that sexually harassed former employees); *Smith v. Animal Urgent Care, Inc.* (W. Va. 2000) 542 S.E.2d 664, 669 ("Sexual harassment, and its inherently non-accidental nature, remain the crux of the case regardless of whether negligence is alleged against" an employer)).

Pursuant to the above case law, the only rational conclusion is that the employee's intentional conduct is the direct cause of the harm and there is no occurrence. Indeed, the gravamen of any sexual molestation claim is the actual sexual molestation, not negligent supervision or other related negligence claims against a third party. Without the molestation there is no claim at all. The employer's negligence is too removed and uncertain.

Accordingly, negligence claims asserted against an employer after an employee commits an intentional tort like sexual assault do not involve an occurrence.

In short, the District Court correctly held that the "alleged negligent hiring, retention, and supervision were acts antecedent to the sexual molestation that caused injury," were "too attenuated from the injury-causing conduct" and did not constitute an occurrence causing bodily injury. (*Liberty Ins. Corp. v. Ledesma & Meyer Constr. Co.* 2013 U.S. Dist. LEXIS 198069 *8-9 (C.D. Cal. Jan. 23, 2013)).

### D. California's public policy against insuring intentional torts supports a finding of no coverage for claims based on an employee's intentional sexual assault.

California has a strong public policy that insurance companies cannot insure intentional conduct. That public policy is set forth in Insurance Code § 533, in which the Legislature clearly announced that intentional conduct, such as sexual molestation, is not insurable within California.[3] Because the crux of any claim against an employer of an

[3] Section 533 states that "[a]n insurer is not liable for a loss caused by the wilful act of the insured; but he is not exonerated by the negligence of the insured, or of the insured's agents or others." Section 533 "precludes indemnification for liability arising from deliberate conduct that the insured expected or intended to cause damage." (*Shell Oil*, 12 Cal.App.4th at 743). The statute is read into all insurance policies. (*J.C. Penney*, 52 Cal.3d at 1019).

"employee who intentionally injured the third party" is intentional conduct, public policy also supports a finding of no coverage here.

California courts have held that Section 533 precludes coverage for sexual molestation. For instance, in *J.C. Penney*, based on Insurance Code § 533, this Court held that "there is no coverage as a matter of law" for sexual molestation. (*J.C. Penney*, 52 Cal.3d at 1019). The *Coit Drapery* case reached the same result, stating that a company should not be able to shift liability for sexual assault to its insurers. (*Coit Drapery*, 14 Cal.App.4th at 1603 ("it is clear that section 533, and the public policy it represents, bar the attempt to shift liability for intentional sexual harassment and associated employment-related torts (claims of wrongful discharge, infliction of emotional distress, battery, and sexual assault) to an insurer")). The court added the public policy of this state "would not be well served" by allowing a perpetrator to avoid payment of damages for his own willful acts "by shifting such liability to an insurer." (*Id.* at 1604).

Finding no coverage for negligent employers who face liability based on an employee's intentional conduct such as sexual assault is consistent with existing law and public policy. The perpetrators are the direct cause of the injury and their conduct clearly is not insurable. As stated in the *Coit Drapery* case, employers should not able to shift liability to their insurers for their employee's intentional conduct. Employers should not be rewarded for keeping their heads in the sand, especially for

such egregious conduct. Finding no applicable insurance coverage will encourage employers to be vigilant and to incur the costs of undertaking adequate supervision or running thorough background checks. Enforcing the policy terms to bar coverage here will advance these public policy goals.

## IV. CONCLUSION

For the foregoing reasons, amici respectfully request the Court hold that (i) there is no "occurrence" under an employer's commercial general liability policy when an injured third party brings claims against the employer for the negligent, hiring, retention, and supervision of the employee who intentionally injured the third party and (ii) the judgment of the district court should be affirmed.

Dated: April 24, 2017

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## CERTIFICATION OF WORD COUNT

The text of this Amicus Curiae Brief contains 4,715 words, according to the word count generated by the word-processing program used to prepare the brief.

Dated: April 24, 2017

CROWELL & MORING LLP

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## PROOF OF SERVICE

I, Lisa Fong, state:

My business address is 3 Embarcadero Center, 26th Floor, San Francisco, California 94111. I am over the age of eighteen years and not a party to this action.

On the date set forth below, I served the foregoing document(s) described as:

**APPLICATION FOR PERMISSION TO FILE AN AMICUS CURIAE BRIEF AND PROPOSED BRIEF OF AMICI CURIAE COMPLEX INSURANCE CLAIMS LITIGATION ASSOCIATION AND AMERICAN INSURANCE ASSOCIATION IN SUPPORT OF LIBERTY SURPLUS INSURANCE CORPORATION**

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I declare under penalty of perjury under the laws of the United States and the State of California that the foregoing is true and correct.

Executed on April 24, 2017, at San Francisco, California.

Lisa Fong

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