ORIGINAL

Supreme Court Case Number S179252 Second Civil Number B209616

In the Supreme Court of the State of California

CENTURY-NATIONAL INSURANCE COMPANY,

Plaintiff and Respondent,

v.

JESUS GARCIA, SR., THEODORA GARCIA and JESUS GARCIA, JR.,

Defendants and Appellants.

California Court of Appeal - Second Appellate District - No. B2009616
Superior Court of Los Angeles County - No. BC379522, The Honorable Maureen Duffy-Lewis, Judge

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CENTURY-NATIONAL INSURANCE COMPANY'S ANSWER BRIEF ON THE MERITS

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To the Honorable Ronald M. George, Chief Justice, and to the Honorable Associate Justices of the Supreme Court of the State of California.

ISSUE PRESENTED

May an insurer enforce an exclusion clause in a fire insurance policy that denies coverage to innocent insureds for damages from a fire intentionally caused by a co-insured, or does such a clause impermissibly reduce coverage that is statutorily mandated?

INTRODUCTION

Arson is not insurable. The trial court sustained respondent Century-National Insurance Company's ("Century-National" or "respondent")

demurrer in its entirety, without leave to amend. The appellate court agreed, affirming the dismissal of appellants' cross-complaint. In disputing that result, appellants argue three points: First, they argue that the insurance policy exclusions in respondent's homeowners policy barring first-party property coverage for intentional and/or criminal acts by "any insured" provided appellants less favorable insurance coverage than authorized by California *Insurance Code* § 2071. Second, appellants argue that invalidating the insurance policy's exclusions is mandated by California's common law. Third, and finally, they contend that a trend in other states favors appellants' position.

In affirming the trial court, the Court of Appeal correctly ruled that there is no conflict with *Insurance Code* section 2071, because the statute is silent on the precise issue under review, and such insurance policy provisions are consistent with the State's broader law of insurance coverage. The case authority cited as common law precedent by appellants actually states that contract provisions like those found in respondent's insurance policy would, in fact, preclude coverage in the manner approved by the trial and appellate courts below. Finally, the trend identified by appellants consists of cases from other jurisdictions not binding on California courts.

A genuine legal dispute over coverage supported the trial court's dismissal of appellants' second cause of action for bad faith. Because appellants' third cause of action for reformation merely sought alternative relief, the courts below were likewise correct in sustaining respondent's demurrer to that claim.

STATEMENT OF FACTS

The relevant facts are not in dispute. On May 3, 2007, Century-National received notice that appellants were submitting a claim for fire damage at the insured premises that had occurred the day before. (Clerk's Transcript ("CT") 0005, ln. 19–21.) Century-National assigned an adjuster to determine the cause of loss and prepare an estimate for repair. (CT 0005, ln. 22–23.) The claim immediately came under suspicion for arson, and a fire investigator was retained to prepare a cause and origin report. (CT

0005, ln. 24–25.) The fire investigator issued a report concluding that all possible accidental causes had been eliminated, that the fire was set with the use of an accelerant applied to the floor and bed, and ignited with a match or cigarette lighter. (CT 0006, ln. 1–6.) The fire investigator concluded that the fire had been intentionally set, *i.e.*, arson. (CT 0006, ln. 5–6.) The members of the family acknowledged that Jesus Garcia, Jr. was responsible. (CT 0005, ln. 26–28.) Based on a separate investigation by the local fire department, Jesus Garcia, Jr. was arrested for arson, and held to answer. (CT 0006, ln. 7–14; Respondent's Request for Judicial Notice ("RJN") Exhibits 1, 2.) The criminal court ruled Jesus Garcia, Jr. competent to stand trial on charges of arson and he remained in custody, with arson charges pending against him. (CT 0006, ln. 7–14; Respondent's RJN, Exhibits 1, 2.)

The Century-National policy bars first-party claims resulting from:

> "9. **Intentional Loss**, meaning any loss arising out of any act committed by or at the direction of any **insured** having the intent to cause a loss.
>
> 10. **Dishonesty, Fraud or Criminal Conduct** of any **insured**."

(CT 0007, ln. 7–12; CT 0017, Exclusions 9, 10.)

The exclusions hinge on wrongdoing by an "insured," defined as follows:

> "**Insured** means you and the following persons if permanent **residents** of the **residence premises**:
>
> a. Your relatives. . . ."

(CT 0007, ln. 13–16; CT 0012, Definition 6.)

With the pendency of criminal arson charges, Century-National advised appellants that it was continuing to investigate the loss but reserved all of its rights, including the right to deny coverage. (CT 0006, ln. 15–16.) It then filed for declaratory relief, pleading those undisputed facts and attaching its insurance policy. (CT 0004–0039.) Jesus Garcia, Jr. entered a plea of nolo contendere to the charge of arson (*Pen. Code* § 451(b)), was convicted and sentenced to prison. (Respondent's RJN, Exhibits 1; 2.)

The appellants did not dispute the operative facts, either in the trial court or on appeal. (CT 0046, ln. 20–CT 0047, ln. 0012; Appellants' Opening Brief on Appeal ("AOB"), p. 1–2.)

LEGAL ARGUMENT

I.
The Intentional and Criminal Act Exclusions Do Not Abrogate Appellants' Rights.

Jesus Garcia, Jr., an insured under respondent Century-National's homeowners policy, was indisputably convicted for felony arson in the burning of his family home. The Century-National homeowners policy covering the Garcia property bars first-party claims resulting from:

> "9. **Intentional Loss**, meaning any loss arising out of any act committed by or at the direction of any **insured** having the intent to cause a loss.
>
> 10. **Dishonesty, Fraud or Criminal Conduct** of any **insured**."

(CT 0007, ln. 7–12; CT 0017, Exclusions 9; 10.)

The exclusions hinge on wrongdoing by an "insured," defined as follows:

> "**Insured** means you and the following persons if permanent **residents** of the **residence premises**:
>
> a. Your relatives. . . ."

(CT 0007, ln. 13–16; CT 0012, Definition 6.)

The courts have been consistent in holding that intentional and criminal act exclusions which bar insurance coverage for the acts of "an" or "any" insured negate all coverage when brought into operation. (*Allstate Insurance Co. v. Condon* (1988) 198 Cal.App.3d 148, 153-54 [an insured "logically refers to any one of all the persons insured under the policy," as

distinguished from "the insured" which refers only to a particular insured]; *Fire Insurance Exchange v. Altieri* (1991) 235 Cal.App.3d 1352, 1361 ["Where, as here, the policy excluded coverage for bodily injury intended or expected by 'an' or 'any' insured, the cases have uniformly denied coverage for all claims"]; *Zelda, Inc. v. Northland Ins. Co.* (1997) 56 Cal.App.4th 1252, 1263; *Western Mut. Ins. Co. v. Yamamoto* (1994) 29 Cal.App.4th 1474, 1486-87; *Safeco Ins. Co. v. Gilstrap* (1983) 141 Cal.App.3d 524, 527; *Castro v. Allstate Ins. Co.* (S.D. Cal. 1994) 855 F.Supp. 1152, 1155; *Allstate Ins. Co. v. Gilbert* (9th Cir. 1988) 852 F.2d 449, 454; *American States Ins. Co. v. Borbor* (9th Cir. 1987) 826 F.2d 888, 894.)

Arson is willful, malicious, inherently harmful and uninsurable. (*Pen. Code* § 451; *Ins. Code* § 533; *USF&G v. American Employer's Ins. Co.* (1984) 159 Cal.App.3d 277, 291 [disapproved on other grounds in *J.C. Penney Cas. Ins. Co. v. M.K.* (1991) 52 Cal.3d 1009, 1019]; *Downey Venture v. LMI Ins. Co.* (1998) 66 Cal.App.4th 478, 506.) Garcia's felony conviction also established a criminal act. (*20th Century Ins. Co. v. Schurtz* (2001) 92 Cal.App.4th 1188, 1196-97.) The trial and appellate courts below agreed that, because the fire was admittedly the result of both intentional and criminal acts of an insured, coverage was barred in its entirety.

Moreover, the appellate court agreed that the statutory provisions of the *Insurance Code* relating to fire insurance were not offended, stating:

> "Century National's policy complies with section 2070 because the addition of the provision at issue is not inconsistent with the fire coverage of the standard form policy, which does not address intentional acts. Because section 2070 governs, the limitation of section 2080 requiring additional language to be placed in riders does not apply; there is nothing to prohibit the additional exclusionary language from being incorporated into the insurance

> contract itself. Section 2071 contains no language relating to exclusion for intentional misconduct or criminal acts, and there is no prescription of the form of exclusionary language relating to such conduct. The exclusionary language at issue here relating to intentional conduct thus did not alter the standard form language of the fire insurance provisions of the Garcias' contract because the standard provisions are silent with respect to intentional conduct. Furthermore, if the policy at issue were solely a fire policy, the insurer properly could have placed the exclusionary language in a rider; it does not alter the insurance coverage to include the exclusions in this insurance policy because, as it covers additional perils, the insured knows there are more provisions to read. As a result, the Garcias' fire coverage was 'substantially equivalent' to that under the standard form policy."

The court below stated the fundamental rule that "[i]n interpreting a statute . . . our primary task is to determine the Legislature's intent. To determine that intent, we turn first to the words of the statute for the answer." (Citing *J.C. Penney Cas. Ins. Co. v. M.K.* (1991) 52 Cal.3d 1009, 1020.) Also, "[a] statute must be construed in the context of the entire statutory scheme of which it is a part, in order to achieve harmony." (Citing *O'Brien v. Dudenhoeffer* (1993) 16 Cal.App.4th 327, 333.)

Yet, according to appellants, "[i]n § 2071 [of the *Insurance Code*] the word 'the' is used throughout, including the three exclusion clauses, when referring to the insured. § 2070, when referring to the peril of fire, could not be clearer that any insurance policy covering a fire loss has to afford the insured coverage equal to or superior to the coverage supplied by § 2071." For appellants,

> "[I]t could not be clearer that. . . . Respondent's policy use of the term 'any insured' instead of the required 'the insured' in an exclusion clause dealing with a fire loss, fails to comply with the requirements of § 2070, as coverage under Respondent's policy is not substantially equivalent to or more favorable to the insured than the standard form fire insurance policy, but is actually less. Respondent's policy exclusion language for 'any insured' provides less or diminished coverage against the peril of fire than the standard form policy's term 'the insured', as the phrase 'any insured' would preclude coverage to an innocent co-insured such as appellants under relevant California law." (AOB, p. 17.)

Thus, appellants assert that *Insurance Code* § 2071, when read in conjunction with sections 2070 and 2080, requires any fire policy exclusion for "malfeasance" by an insured to apply only to "the insured." In other words, appellants assert that a fire insurance policy can only exclude coverage severally and not jointly.

Appellants are mistaken on two counts. They are applying the wrong standard to determine the Legislature's intent, and they are failing to read the words of the statute itself.

Preliminarily, it is noted that appellants refer to "three" exclusions for "malfeasance" in the standard fire policy. Beside the fraud and false swearing provision, they are presumably referring to the provisions for "neglect of the insured to use all reasonable means to save and preserve the property at or after a loss," (*Ins. Code* § 2071, Perils not included, subd. (i); *1943 New York Standard Fire Policy*, ln. 21-22) and the conditions suspending insurance "while the hazard is increased by any means within control or knowledge of the insured" (*Ins. Code* § 2071, Conditions suspending or restricting insurance, subd. (a); *1943 New York Standard*

Fire Policy, lines 31-32). But there is only one actual exclusion based on "malfeasance" in the standard fire policy: the fraud and false swearing exclusion. *Insurance Code* § 2071; *New York Standard Fire Policy*, ln. 1-6.

The other two are not exclusions at all. "Neglect of the insured" is a "peril not included." That is, it is a risk outside the basic parameters of coverage provided by the policy. (*See Garvey v. State Farm Fire & Cas. Co.* (1989) 48 Cal.3d 395, 407 [distinguishing "all risk" from specified perils insurance].) The "increase in hazards" provision is a policy condition – a future and uncertain event which must or must not exist in order for a contractual duty to arise. (Black's Law Dict. (5th ed. 1983) p.154.)

Further, the "neglect to use all reasonable means" provision has been interpreted as inapplicable to an insured's conduct that *causes* a fire; rather, that provision applies to the conduct in *responding* to a fire that originates from some other cause. (*Tuchman v. Aetna Cas. & Sur. Co.* (1996) 44 Cal.App.4th 1607, 1615-16 ["This provision has, of course, no application to negligence of the insured before the origin of the fire. It applies, rather, to situations where no proper diligence was used by the insured at the time of, or following a fire, to save property from destruction. . . . [¶] This language leads to one conclusion only—that the insured must act at or after the time of the loss to save and preserve the property"].)

Regarding the "increase in hazard" provision, respondent explained extensively in the court below that no California court has interpreted this provision as being in the nature of an intentional act exclusion. Rather, the California courts have interpreted this provision to apply to changes in the structure or use of the insured premises. (*See, e.g., Mackintosh v. Agricultural Fire Ins. Co.* (1907) 150 Cal. 440, 446 [erection of a smelting furnace]; *Rizzuto v. National Reserve Ins. Co.* (1949) 92 Cal.App.2d 143, 148 [use as a barber shop].) Moreover, the increase in hazard condition is prefaced: "[u]nless otherwise provided in writing," indicating that it may be modified and is, therefore, not absolute.

The only provision constituting an actual exclusion based upon "malfeasance" by an insured is the concealment and fraud exclusion. In

contending that the Legislature was mandating coverage for all co-insureds regardless of the circumstances, appellants narrowly focus on the provision's use of the words "the insured" as dispositive. The statutory fire policy reads:

> "Concealment, fraud. This entire policy shall be void if, whether before or after a loss, the insured has willfully concealed or misrepresented any material fact or circumstance concerning this insurance, or the subject thereof, or the interest of the insured therein, or in any case of fraud or false swearing by the insured relating thereto. (*Ins. Code* § 2071; *New York Standard Fire Policy*, ln. 1-6.)

Century-National argued below, and continues to contend, that this provision of the fire policy is not dispositive, because it factually does not apply. It was undisputed that nobody lied or inflated the claim. This is literally not a fraud or false swearing case. Yet, despite agreeing that there was no concealment or misrepresentation involved, appellants nonetheless point to the provision as dispositive. Appellants are bootstrapping their argument that any and all exclusions must use the words "the insured" to the standard policy's concealment and fraud exclusion.

The concealment and fraud exclusion in the standard fire policy has no such broad scope. In *Leasure v. MSI Ins. Co.* (1998) 65 Cal.App.4th 244, 248, the Court of Appeal found that the fraud and false swearing provision of the standard policy is limited to misrepresentations concerning the factual circumstances underlying the claim at hand. Thus, the provision did not operate to void coverage where the insureds forged the signatures of lienholders on checks issued to pay prior insurance claims. According to that court: "The false representations that the lienholders endorsed the checks are not material representations because they do not relate to MSI's investigation to determine its obligations under the policy." (*Id.* at 248.)

In *Mitchell v. United National Ins. Co.* (2005) 127 Cal.App.4th 457, 463, the Court of Appeal was asked to rule that the provision's requirement for "willful" concealment or misrepresentation meant that for the risk of fire only, an insurer had to show intentional misrepresentation to avoid coverage. That court disagreed, holding that the generally applicable principles of insurance law permit an insurer to rescind an insurance policy for negligent or unintentional misrepresentations "notwithstanding the willful misrepresentation clause included in the required standard form fire insurance policy." (*Id.,* at 463.)

There was no discussion in those cases of co-insureds, but the fact is that courts reading the fraud and false swearing exclusion have declined to extend the provision beyond its own terms or attach special meaning to it. Despite appellants' claim that the provision governs interpretation of all obligations under a fire policy, the fraud and false swearing provision has no overarching talismanic effect. Thus, there is no authority to support appellants' proposition that the standard fire policy's concealment and fraud exclusion applies to anything other than fraud or false swearing. It simply does not apply here.

As pointed out by the court below, the fire policy statute is silent on intentional and criminal acts, and "there is no statutory prescription of the form of exclusionary language relating to such conduct." Since the exclusions in respondent's policy are outside the terms of the fire policy statute, and are otherwise accepted as consistent with law and public policy, they do not abrogate appellants' rights or provide "less" coverage than required in a fire policy.

However, appellants asked the appellate court to rule, and are once again asserting, that if the Legislature *were to* add intentional and/or criminal acts to the provisions of the statutory fire policy, it would likewise use "the insured," rather than the term "any insured" found in Century-National's policy. In purporting to divine the Legislature's intent, however, appellants fail to account for the context in which the statutory fire policy was enacted, and are judging it by subsequent case law that developed much later.

As explained by the court in *Mitchell v. United National Ins. Co., supra*, the first standard fire policy law was enacted in Massachusetts in 1873. New York enacted its first legislation on the subject in 1886, followed by the 1891 policy and the current 1943 policy. Between 1873 and 1942, many different standard fire policies were used in the several states. The most widely-copied standard fire policy was adopted by law in New York State in 1943. (*Mitchell, supra*, 127 Cal.App.4th at 470, fn. 4.) Further, California law first provided for a standard form fire insurance policy in 1909 (Stats. 1909, ch. 267, p. 404), and the current version, also known as the "165 Line" policy, was enacted in 1949. (Stats. 1949, ch. 556, § 2, p. 955); *Mitchell, supra*, 127 Cal.App.4th at 472, fn. 6.)

Yet, against that historical background spanning the first half of the 20th Century, appellants seek to interpret the statutory fire policy under the modern cases applicable to Century-National's policy. That is, appellants are asking the Court to *infer* that, at the time of the adoption of the current fire policy in 1949, the Legislature was giving the term "the insured" the same singular meaning and importance that it has since been determined to have in relation to modern intentional and criminal act exclusions. However, appellants have not cited (nor can they) to any evidence that either the drafters of the standard fire policy or the California Legislature ever considered the difference between use of the term "any" versus "the" insured, or that a special meaning must attach.

Appellants point to no authority that, at the time the standard fire policy was adopted, such a distinction was recognized, and early decisions generally held that an innocent co-insured *could not* recover under the policy where another insured purposely set the insured property on fire. Rather, the courts reasoned that co-insureds under the policy had a joint responsibility, usually as joint owners of the insured property, to abide by the policy's conditions:

> "When a policy insures joint owners, and contains a condition that the insurance shall not embrace damage resulting from a voluntary increase of hazard, or neglect to use reasonable

> means to preserve the property, committed by 'the insured,' this condition manifestly is intended to apply to the joint tenants, as together constituting 'the insured,' and to impose upon them, by construction, or by implication, whichever expression may be preferred, a joint duty and obligation to observe good faith toward the insurer. If either of them fraudulently violated the good faith owing to the insurer, I think both [insureds] are chargeable with and affected by such violation, to the extent of its operating as an obstacle to recovery; and especially so where, but for the fraudulent breach of faith, there would have been no fire, and hence no liability of the insurer upon the policy could have arisen." (*Matyuf v. Phoenix Ins. Co.* (Pa. 1933) 27 Pa.D.&C.2d 351, 361.)

Thus, the early courts looked to the nature of the property interest – usually joint tenancy – and the marital relationship, to bolster the conclusion that the rights and obligations were joint. The courts reasoned that when the property was jointly owned, the insurance policy was presupposed to be joint because the insurable interest was deemed to be indivisible. That presupposition of a joint insurance policy was also bolstered by the notion that a married couple constitutes a single entity under the law. (*Kosior v. Continental Ins. Co.* (1938) 299 Mass. 601, 604 [fire insurance policy insuring two jointly and void upon fraud of "the insured" was avoided by the fraud of one insured in which the other had no part]; *Klemens v. Badger Mut. Ins. Co.* (1959) 8 Wis.2d 565, 568 [insurance written in the joint names of the insureds, creates a joint obligation to comply with the terms of the policy] [overruled by *Hedtcke v. Sentry Ins. Co.* (1982) 109 Wis.2d 461, 482]; *Jones v. Fidelity & Guaranty Ins. Corp.* (Tex.Civ.App. 1952) 250 S.W.2d 281, 283 [same] [disapproved by *Kulubis v. Texas Farm Bureau Underwriters Ins. Co.* (Tex. 1986) 706 S.W.2d 953, 954].)

Indeed, that was also the law in California. In *Watts v. Farmers Insurance Exchange* (2002) 98 Cal.App.4th 1246, 1252, the insurer argued that joint marital ownership precluded recovery by one spouse where the other burned the house. In that case, the insurer was relying on *Erlin-Lawler Enterprises, Inc. v. Fire Ins. Exchange* (1968) 267 Cal.App.2d 381, 385, which involved the burning of a family-owned supermarket in Inglewood. Rejecting that argument, the *Watts* court pointed out that *Erlin-Lawler* did not involve jointly held marital property, but rather, both family and corporate shareholder interests. (*Watts*, *supra*, 98 Cal.App.4th at 1252.) According to the *Watts* court, the issue and rule of *Erlin-Lawler* was not mere joint ownership but instead, the analysis of benefits that might flow from the actions of the wrongdoer. (*Watts*, *supra*, 98 Cal.App.4th at 1252-53.)

The *Watts* court rejected the *Erin-Lawler* approach, holding that interpretation of insurance contracts is governed in the first instance by the specific words of the policy. (*Id.,* at 1260.) However, one reasonable interpretation of *Erlin-Lawler* is that joint responsibility was, in fact, an accepted theory that barred insurance coverage under California law. "The basic function of the court is to see that no one takes advantage of his own wrong. . . . An analysis must be made in each case to see if the arsonist will benefit by the recovery on the policy, either directly or indirectly." (*Erlin-Lawler, supra*, 267 Cal.App.2d at 385.)

If anything, the *Erlin-Lawler* court laid down an even more restrictive rule than simple reliance on joint marital interests, because that decision can be read as authorizing the denial of coverage to co-insureds other than spouses, including corporate shareholders, directors, officers, partners, joint venturers, community property holders and joint tenants, all of whom could be barred from coverage, if, according to the *Erlin-Lawler* court, some benefit will flow to the wrongdoer as a result of the property's destruction. (*Id.,* at 387.)

While the *Erlin-Lawler* court made no reference to *Insurance Code* section 2071 or the standard fire policy, it was presumably taking the statutory terms into account, since they are automatically incorporated into

every fire policy issued in the State. (*Ins. Code* § 2070.) There is a presumption that in performing their duties, courts are following all laws. (*Civ. Code* § 3548; *Wolfgram v. Wells Fargo Bank* (1997) 53 Cal.App.4th 43, 60.) Yet, the *Erlin-Lawler* court did, in fact, rule that in the proper situation, coverage for a fire loss would be barred for an innocent co-insured. (*Erlin-Lawler, supra,* 267 Cal.App.2d at 385.) The *Erlin-Lawler* court merely sent that matter back to the trial court to make the requisite inquiry into the benefits potentially accruing to the various insureds.

As it stands today, *Erlin-Lawler* has never been overruled or disapproved and is still binding on the trial courts in California. (*Gwartz v. Superior Court* (1999) 71 Cal.App.4th 480, 481-82.) At best, *Watts* creates a split of authority on the topic. (*Auto Equity Sales, Inc. v. Superior Court* (1962) 57 Cal.2d 450, 456.)

But the *Watts* court highlighted an issue raised by *Erlin-Lawler*. Forcing insurers and the courts to engage in some nebulous analysis of the benefits flowing to each respective insured could ultimately prove unworkable. That is particularly true given the current state of the economy. What is a benefit? For example, does a teenager who sees the family being crushed by the weight of an underwater or upside-down mortgage receive a benefit by burning the house? Despite having no ownership interest, he may perceive a benefit in freeing the family from an economic burden. Thus, the answer could be both "yes" and "no" at the same time. That is a vague and ambiguous standard for deciding insurance coverage, and the *Watts* court held that, instead, the outcome is determined by the words of the insurance contract.

The importance of *Erlin-Lawler* here, however, is that, contrary to appellants' claim, it cannot be inferred that the Legislature necessarily intended that all rights and obligations be several under the statutory fire policy merely because it used the words "the insured" in *Insurance Code section* 2071. While the joint responsibility doctrine has been eroded, the fact is that nothing in the prior law suggests that the drafters of the standard policy or the California Legislature sought to imbue the words "the insured" with the meaning or significance that has since been recognized in

relation to the terms "an insured" or "any insured" found in modern personal insurance policies.

Perhaps more significant than the historical context of the standard fire policy, the fact is that appellants are simply misreading the words of the policy. Appellants argue that coverage, and any exclusion for malfeasance, must be purely several. They argue that the Legislature's use of the words "the insured" in the fraud and false swearing exclusion of the statutory policy means that any exclusion for malfeasance will only operate to exclude coverage for the insured wrongdoer. But that ignores the actual words of the statutory policy's concealment and fraud exclusion itself.

In fact, the fraud exclusion of the standard fire policy actually begins with the words "This *entire* policy shall be void if. . . ." *Ins. Code* § 2071, Concealment, fraud; *1943 New York Standard Fire Policy*, ln. 1 [emphasis added].) That phrase completely counters the interpretation advanced by appellants that the exclusion will only operate severally, and instead demonstrates that the Legislature intended for fraud by one to void the policy for all insureds. If the entire policy is void, the only possible meaning is that it is void as to all insureds when one insured commits fraud.

It is incongruous that appellants and the foreign courts on which they rely would attach so much importance and meaning to two words in a contractual provision ("the insured") while utterly ignoring other words in that same provision ("this entire policy shall be void") when the plain and ordinary meaning of those words has precisely the opposite effect that appellants assert. The Michigan Supreme Court in *Borman v. State Farm* (1994) 446 Mich. 482, duly quoted the full wording of the New York standard policy's fraud and concealment provision, including the words "this entire policy shall be void," but then proceeded to fix on the words "the insured" to declare a provision barring coverage for "any insured" to be in "conflict with a standard policy prescribing a provision voiding the policy because of the wrongful conduct of 'the insured.'" (*Id.,* at 492.) But there really is no conflict because a fair reading of the whole of the fraud and concealment provision in the standard policy is that it achieves the

same result as an exclusion for intentional or criminal acts of "any insured," by voiding the "entire policy" when fraud or misrepresentation occurs.

As noted by respondent below, the Michigan courts were actually cognizant that they were going outside the parameters of the standard policy. At the intermediate appellate level of the *Borman* case, the Michigan appeals court noted this point, but dismissed it saying: "While strictly speaking the 'intentional wrongs' exclusion in defendant's policy is distinct from the 'fraud' exclusion, we find that the interests of the innocent insured should be protected in either case." (*Borman v. State Farm Fire & Cas. Co.* (1993) 198 Mich.App.675, 681.) Thus, rather than determining Legislative intent, the Michigan courts were themselves legislating.

As stated by the court in *Watts*, this is really a straightforward matter of contract interpretation. Whether the Legislature was focusing only on the wrongdoer in terms of performing a fraudulent act when it used the words "the insured," the simple fact is the standard policy states that in the event the insured, even if only one particular insured, performs a fraudulent act, the whole policy is void *in its entirety*. The Legislature did not provide that "This entire policy shall be void '*as to the insured*,'" it simply used the words "This entire policy shall be void. . . ." There is no way to read this provision other than that if one insured performs a fraudulent act, the whole policy is void, including for the insureds. Any other interpretation improperly inserts words and limitations not actually contained in the statute. Thus, the standard fire policy is not a purely several policy, but precludes on its face coverage for any co-insured when fraud occurs.

California law requires that an insurance policy be read as a whole, with each part being given effect so as to help interpret the others. (*Civ. Code* § 1641.) Policy language must be construed so as to give effect to every term; a court must strive to give every term meaning unless to do so would render the term inconsistent or contradictory. (*Fireman's Fund Ins. Co. v. Superior Court* (1997) 65 Cal.App.4th 1205, 1217-18.) An interpretation that gives effect to every clause is preferred over one that would render other policy terms meaningless. (*Union Oil Co. v. International Ins. Co.* (1995) 37 Cal.App.4th 930, 935.)

It would violate these fundamental canons of interpretation to give special meaning to two words in the fraud and false swearing provision, while ignoring six other words: six words which, in fact, compel the opposite result from that which appellants assert.

Given the historical setting of the statutory fire policy, and the actual words of the statute itself, it cannot be presumed that the Legislature intended that the statutory policy only exclude coverage severally. Further, the words of the standard policy themselves, when read in full, compel the opposite conclusion. Thus, there is no evidence that modern intentional and criminal act exclusions, as applied to a fire loss, must necessarily be read as applying only to "the insured," or that exclusions applying to "any insured" provide less coverage than required by the statute.

The wording of Century-National's exclusions is plain and clear. Read in their ordinary sense, the exclusions bar all coverage for the intentional or criminal acts of any insured. The arson by Jesus Garcia, Jr. was intentional, inherently harmful and criminal, and hence, barred from coverage under the policy.

II.
The Common Law of California Supports the Exclusion of Coverage for Appellants.

Appellants rely on *Watts v. Farmers Insurance Exchange, supra*, 198 Cal.App.4th 1246, as evidence that the common law supports voiding or at least reforming respondent's intentional and criminal act exclusions. But here, too, appellants neglect to read the entirety of the decision, or give it proper effect.

The common law, or more properly the case law, interpreting modern intentional and criminal act exclusions has distinguished intentional and criminal act exclusions which bar insurance coverage for the acts of "an" or "any" insured from those only barring coverage for "the insured." (*Allstate Insurance Co. v. Condon, supra,* 198 Cal.App.3d 148, 153-54 [an insured "logically refers to any one of the persons insured under the policy," as distinguished from "the insured" which refers only to a

particular insured]; *Fire Insurance Exchange v. Altieri, supra*, 235 Cal.App.3d 1352, 1361 ["Where, as here, the policy excluded coverage for bodily injury intended or expected by 'an' or 'any' insured, the cases have uniformly denied coverage for all claims"); *Zelda, Inc. v. Northland Ins. Co., supra*, 56 Cal.App.4th 1252, 1263; *Western Mut. Ins. Co. v. Yamamoto, supra*, 29 Cal.App.4th 1474, 1486-87; *Safeco Ins. Co. v. Gilstrap, supra*, 141 Cal.App.3d 524, 527; *Castro v. Allstate Ins. Co., supra,* 855 F.Supp. 1152, 1155; *Allstate Ins. Co. v. Gilbert, supra*, 852 F.2d 449, 454; *American States Ins. Co. v. Borbor by Borbor, supra*, 826 F.2d 888, 894.

The cited cases admittedly involved third-party liability insurance, and not first-party property insurance. However, the same fundamental rules of contract interpretation apply to property insurance. If anything, property insurance policies are read more narrowly than liability policies, since there is no duty to defend obligating the insurer to respond for even doubtful claims. (*See Golden Eagle Ins. Corp. v. Cen-Fed, Ltd.* (2007) 148 Cal.App.4th 976, 995.)

The intentional and criminal act cases all support respondent's interpretation of its policy. Contrary to appellant's contention, however, *Watts* did nothing more than apply those rules:

> "We, too, believe that conditioning an innocent spouse's ability to recover insurance benefits on the manner in which title to damaged property is held makes little sense, and see no reason why we should follow an approach deemed outmoded and unnecessarily harsh by nearly every other jurisdiction in the United States. Community property laws exist to protect the innocent spouse from losing his or her rights due to the individual misdeeds of the other spouse. They should not be used as a weapon by an insurance company to reap a windfall where one spouse, acting alone, has violated the

> terms of the policy and the policy does not explicitly warn that this will be the outcome. A rule automatically precluding recovery for community property and joint tenancies, but permitting recovery when the subject property happens to be held separately, seems to bear no rational relationship to the expectations of the parties or the risks involved. *We, therefore, agree with the modern majority that an innocent spouse's ability to recover should be based on the language of the policy rather than the type of property involved.*" (*Watts*, *supra*, 98 Cal.App.4th at 1260 [emphasis added].)

The insurance policy at issue in *Watts* barred coverage stating: "We do not provide coverage if you have intentionally concealed or misrepresented any material fact or circumstance relating to this insurance. . . ." (*Id.* at 1249.) Ms. Watts was demonstrated to have submitted a false and fraudulent sworn statement in proof of loss. That in itself distinguishes *Watts* from the instant case, since *Watts* did, in fact, involve fraud and false swearing. Moreover, as noted above, *Watts* disagreed with, but did not purport to overrule *Erlin-Lawler*, which authorized the exclusion of fire coverage for co-insureds.

The *Watts* court cited *Atlas Assur. Co. v. Mistic* (Alaska 1991) 822 P.2d 897, 900, as involving identical "you" language, and barring coverage. The court distinguished *Reitzner v. State Farm Fire & Cas. Co.* (Minn. 1993) 510 N.W.2d 20, 24, as involving a policy exclusion for intentional or fraudulent acts of "you or any other insured," which prevented recovery by the spouse. (*Watts, supra,* 98 Cal.App.4th, 1246, 1260.)

Regarding *Insurance Code* section 2071 and the standard form policy, the *Watts* court merely noted that the fraud and false swearing provision used the words "the insured," which it saw as consistent with the wording "you" in the policy before it. Thus, there was no reason for the *Watts* court to go any further in its analysis, since it had already reached the

determination that the innocent spouse was afforded coverage. (*Id.*, 98 Cal.App.4th at 1260.)

Because it simply applied the accepted "any" versus "the" rules to a policy excluding coverage "if you have intentionally concealed or misrepresented any material fact," the holding in *Watts* is consistent with, and does nothing to abrogate, the broader case law in California holding that use of "an" or "any" insured in an intentional or criminal act exclusion bars all coverage for all insureds when one insured commits the intentional or criminal act. In fact, as respondent pointed out below, it is appellants' position that injects an anomaly into the decisional law. Specifically, appellants' position inexplicably leads to far broader coverage for a solitary type of loss, in a singular situation, for no rational reason.

There is no dispute that the case law already addressing the distinctions between "any" and "the" insured supports barring coverage for all insureds in the third-party liability context. (*Altieri*, *supra,* 235 Cal.App.3d at 1361.) Thus, if Jesus Garcia, Jr. had set fire to his next door neighbor's house, and been duly convicted for arson, there would be no coverage under the similar exclusions applicable to the third-party insurance provided under respondent's policy. Moreover, the established law would preclude coverage if the neighbor were to also sue appellants for negligent supervision or on some other theory. The existing law precludes coverage for such a loss, in its entirety.

Further, if Jesus Garcia, Jr. had selected some other device to damage the Garcia home, such as using a hose to flood the property, or purposely contaminating it with pollutants or chemicals, coverage for the damage would also be outside the standard fire policy. Indeed, the standard fire policy specifically states that "explosion" is not covered, unless fire ensues. (*Ins. Code* § 2071, Conditions suspending or restricting insurance, subd.(c); *1943 New York Standard Fire Policy*, ln. 29-37.) Thus, if Jesus Garcia, Jr. had been informed enough to use an explosive instead of an accelerant, respondent would be free to exclude the loss for "any" insured, and the loss would be barred. While these are admittedly unconventional scenarios, there is little question that the law would support the exclusion of

coverage for such claims, including for co-insureds. Yet, where Jesus Garcia, Jr. set fire to his own home, appellants argue that coverage cannot be barred.

The adoption of appellants' position would create a major anomaly in the existing common law. There is no reason why the same type of event would lead to radically different results owing simply to the selection of the target or the device used by the wrongdoer. In all cases, the conduct at issue would be intentional, inherently harmful and criminal. The damage would be virtually the same whether Jesus Garcia, Jr. burned his own or the neighbors' house. It does not make sense that coverage would attach for the one and not the other.

Appellants merely assert that the Court of Appeal was wrong to rely on *Altieri*, and *Yamamoto*, both *supra*, without addressing the anomaly in the broader law of insurance coverage that would be created by adopting the position they champion. For appellants, it is sufficient to simply point out that those cases involved losses other than fire. Appellants are comfortable with the result that one singular event (fire) must result in co-insured coverage, despite the courts' approval of exclusion of virtually every other type risk from the same type of coverage.

Indeed, appellants accuse respondent of trying to differentiate between causes of fire, stating that:

> "The Court of Appeal erred by considering arson as a separate form of fire not covered by the standard language of § 2071. Arson is merely one form of fire and the Code does not differentiate between different causes of a fire. The original standard fire insurance code is over one hundred years old and arson is not a new concept. If the Legislature wished to differentiate between the different causes of fire, it had plenty of time to have done so."

The anomaly urged by appellants is all the more incongruous, because the courts approve and enforce intrafamily exclusions in insurance policies. According to the court in *Bjork v. State Farm Fire & Cas. Co.* (2007) 157 Cal.App.4th 1, "[a] resident relative exclusion . . . has long been held to be an enforceable exclusion. . . . The exclusion is premised on the principle that an insurance carrier need not insure risks arising from intrafamily torts unless it chooses to do so." (*Id.,* at 6.)

The policy in *Bjork* excluded coverage for "bodily injury to you or any insured within the meaning of part a. or b. of the definition of insured." (*Id.,* at 4.) The court explained that the purpose of the exclusion was to avoid the potential for collusive claims between family members, although there was no requirement for showing actual collusion. (*Id.*, at 7.) Thus, the courts recognize that claims between family members are inherently suspect, and an insurer is free to exclude such claims if it chooses to do so. Yet, appellants nonetheless feel that when it comes to the sole issue of first-party fire coverage, co-insureds must be paid, regardless.

As noted by respondent below, the court in *Mitchell v. United National Ins. Co., supra,* 127 Cal.App.4th 457, held that where the interpretation being argued for the standard form of the policy is inconsistent with general insurance law applicable to all policies, the provisions of the statutory fire policy must be "harmonized" with the other aspects of insurance law. (*Id.,* at 472.) Although appellants cite *Watts* and claim that respondent's position goes against the grain of California's common law, the simple fact is that appellants are the parties advocating for a special exception to the otherwise generally applicable and accepted decisional law of the State. Appellants' common law argument fails, because the "common law" of California upholds the exclusion of coverage for co-insureds.

III.
The Trend Identified in California is That the Policy Language Controls.

According to the *Watts* court, "the trend noted in *Erlin-Lawler* has been reversed and currently favors permitting recovery by the innocent

insured party up to his or her percentage share of the value of the property *unless the policy contains language which clearly excludes this possibility.*" (*Watts, supra,* 98 Cal.App.4th at 1253-1254 [emphasis added].) The *Watts* court then proceeded to cite a dozen cases, all of which held that the wording of the insurance policy is dispositive.

The cited cases went both ways, with some ruling that the co-insured was entitled to coverage (*Atlas Assur. Co. v. Mistic* (Alaska 1991) 822 P.2d 897, 900); with others holding that the co-insured was barred from recovery (*Reitzner v. State Farm Fire & Cas. Co.* (Minn. 1993) 510 N.W.2d 20, 24). But contrary to appellants' argument here, the trend was not necessarily toward requiring coverage for all co-insureds. Rather, as expressly stated by the *Watts* court, the trend identified was that the insurance policy language would control the outcome, which might, or might not, result in insurance coverage. (*Watts, supra,* 98 Cal.App.4th at 1257-60.)

Thus, the *Watts* court actually identified a trend somewhat at odds with appellants' claim. Namely, although other courts had favored paying co-insureds in the event of arson by one insured, that favored result could, in fact, be affected by the specific wording of the policy. Indeed, the *Watts* court specifically cited to cases finding that the co-insured was barred from coverage. (*Id.*, at 1257-1260.)

Therefore, rather than finding that there is a trend in other states to necessarily pay co-insureds, the trend identified by the one California court to consider the issue found something slightly different: a trend to *favor* paying the co-insured, but only while *giving precedence and effect* to the policy terms as written. (*Id.*)

The foregoing *Watts* finding is nothing more than a statement of generally applicable insurance principles. Insuring clauses are interpreted broadly to protect the objectively reasonable expectations of the insured. (*Montrose Chem. Corp. v. Admiral Ins. Co.* (1995) 10 Cal.4th 645, 667.) Exclusions and limitations on coverage in an insurance policy are strictly construed. (*Delgado v. Heritage Life Ins. Co.* (1984) 157 Cal.App.3d 262, 271 [superseded by statute on other grounds].) The intent of the parties is to be ascertained from the writing alone, if it is possible. (*Civ. Code*

§1639.) The language of the contract is to govern its interpretation, if the language is clear and explicit, and does not involve an absurdity. (*Civ. Code* § 1638.) An insurance policy may not be inequitably redrafted to provide coverage different from or in excess of that which is provided by the plain language of the contract. (*Young's Market v. American Home Assurance Co.* (1971) 4 Cal.3d 309, 316.)

As set forth above, the trend appellants perceive in other states is not the definitive change they claim. Rather, cases go both ways on the issue. Moreover, even if there are decisions supporting appellants' position in other states, they do not bind the courts of this State. Appellants' claim that this Court should carve out an exception from the generally applicable law of California based on what other states do is not persuasive, and there is no reason to deviate from California law as it was applied the courts below.

IV.
The Courts Below Correctly Dismissed Appellants' Second and Third Causes of Action for Insurance Bad Faith and Reformation.

Appellants' have not raised any further argument respecting the dismissal of their second and third causes of action, and the subsequent affirmation by the Court of Appeal. Respondent hereby submits notice of its intent to rely on its appellate brief as respects those issues. (Cal. Rule of Court, rule 5.520.)

V.
Conclusion.

Appellants' position is simply an insupportable claim that public policy—as purportedly divined from the 1949 standard fire policy, a single court decision, and a claimed trend in other states—renders respondent's insurance policy provisions unenforceable. This case was, and remains, a simple question of contract interpretation. There is no dispute as to the operative facts or even the interpretation of respondent's insurance policy. Appellants merely claim that the policy is unenforceable. For the reasons

set forth above, respondent disagrees, and respectfully requests that the Court affirm the trial and appeals courts below.

Respectfully submitted,

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Christopher Kendrick

Attorneys for Plaintiff and Respondent
Century-National Insurance Company

CERTIFICATE OF COMPLIANCE
WITH RULE 8.204(c)(1)

I, the undersigned, Christopher Kendrick, declare that:

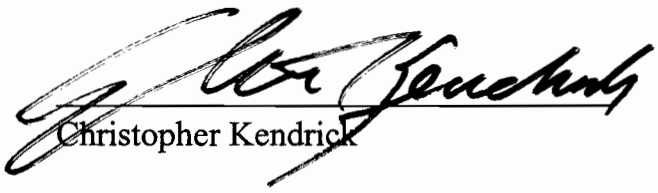
I am an associate in the law firm of Haight Brown & Bonesteel, LLP, which represents plaintiff and respondent, Century-National Insurance Company, in this case.

This certificate of Compliance is submitted in accordance with Rule 8.204(c)(1) of the California *Rules of Court.*

This answer brief on the merits was produced with a computer. It is proportionately spaced in 13 point Times Roman typeface. The brief contains 7,718 words, including footnotes.

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

Executed on June 7, 2010, at Los Angeles, California.



Christopher Kendrick

PROOF OF SERVICE

STATE OF CALIFORNIA)
) ss.:
COUNTY OF LOS ANGELES)

Case Name: CENTURY NATIONAL INSURANCE COMPANY v. JESUS GARCIA, SR., THEODORA GARCIA and JESUS GARCIA, JR.
Case No.: Supreme Court case number: S179252

I, the undersigned, say: I am and was at all times herein mentioned, a citizen of the United States and a resident of the County of Los Angeles, California, over the age of eighteen (18) years and not a party to the within action or proceeding; that my business address is 6080 Center Drive, Suite 800, Los Angeles, CA 90045-1574; that on June 7, 2010, I served the within CENTURY-NATIONAL INSURANCE COMPANY'S ANSWER BRIEF ON THE MERITS in said action or proceeding by depositing a true copy thereof, enclosed in sealed envelopes with postage thereon fully prepaid, in the United States mail at Los Angeles, California, addressed as follows:

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(*Via Federal Express - Original and 13 copies*)

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Julie Dekhtyar