

DESTROYED COMMUNITY PROPERTY, DAMAGED PERSONS, AND INSURERS' DUTY TO INDEMNIFY INNOCENT SPOUSES AND OTHER CO-INSURED FIDUCIARIES: AN ATTEMPT TO HARMONIZE CONFLICTING FEDERAL AND STATE COURTS' DECLARATORY JUDGMENTS

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I. INTRODUCTION

Perhaps because of habit or a strong aversion to risks, consumers purchase a considerable amount of insurance generally, and consumers purchase property, indemnity, and liability insurance in particular. Typically, national property and casualty insurers sell property, indemnity, and liability insurance contracts. As a result, those insurers' sales and

revenues increase from year to year.¹ At the dawn of the 21st century, foreign property and casualty insurers are realizing similar successes.²

It is expected that anxious or prudent consumers would insure themselves and their various property interests against strangers, strange events, and perils over which consumers have little control or influence. Ironically, a large number of consumers also insure themselves and their property interests against familiar and trustworthy fiduciaries. Therefore, the property and casualty insurance market is huge; both national and foreign insurers are encouraged to expand and sell a wide variety of co-insured indemnity and liability insurance contracts.³ Under many co-insured contracts, the named insureds are familiar pairs of fiduciaries, such as estates and trustees, executors and administrators, professionals and associates, mortgagors and mortgagees, partners and partnerships, corporations and their officers & directors, business entities and their independent contractors, joint ventures, employers and employees, sellers and buyers, parents and children, and husbands and wives.⁴

1. See, e.g., Bob Graham, *Analysis: Property-Casualty Insurers to See Rates of Combined Ratios Rise*, Aug. 19, 2009, <http://ifawebnews.com/2009/08/19/analysis-property-casualty-insurers-to-see-rates-or-combined-ratios-rise/> ("Calendar 2008 marked the fourth consecutive year of favorable reserve releases, a switch from earlier in the decade. During 2008, the property-casualty insurance industry posted nearly \$14.3 billion in favorable reserve development, or about 2.8% of prior year-end carried reserves").

2. See, e.g., David Pilla, *Allianz Sees Double-Digit Premium Growth in "New Europe,"* BESTWIRE, Aug. 26, 2008 (LEXIS) ("Allianz S.E. said its premium growth in 'New Europe' markets rose 14.3% to more than 1 billion euros (795.2 million pounds) in the second quarter, despite what it called 'difficult' market conditions. For the first half, New Europe premium growth rose 10.5% to 2.1 billion euros, compared with the previous year. Allianz includes markets in Azerbaijan, Bulgaria, Croatia, the Czech Republic, Hungary, Kazakhstan, Poland, Russia, Romania, Slovakia, Slovenia and Ukraine in New Europe The group's property and casualty business saw a 21% rise in gross premiums, to 1.6 billion euros, in the first half.").

3. Cf. Fran Lysiak, *Marsh Forms Insurance Agency Focused on Small and Growing U.S. Businesses*, BESTWIRE, Oct. 24, 2008 (LEXIS) ("Marsh said it formed a new insurance agency focused on small and growing businesses in the United States that would do business separately from its brokerage operations The agency will offer commercial property/casualty, directors & officers' liability, surety, employee benefits and personal lines products to customers through a sales and service force in retail locations across the United States MMC is the second-largest broker in the world, with \$4.5 billion in revenues, according to the Best's Review ranking of top global brokers.").

4. Cf. *Jackson v. Cont'l Cas. Co.*, 412 So.2d 1364, 1366 (La. 1982) (concurring Justice observing "that an insurer may substitute an incontestable clause more favorable to the policyholder with the commissioner's approval" and that "members of the employee group or their trustees are deemed to be the policyholder, La.R.S. 22:175(A)"). See *Dunn v. Second Nat'l Bank*, 113 S.W.2d 165, 168 (Tex. Comm'n App. 1938) ("Fain Carter procured the issuance . . . insuring his life [and] . . . designating as beneficiary in his written application 'The estate of S. F. Carter, Sr., The Second National Bank of Houston, Texas., and Carrie B. Carter (mother) co-executor and co-executrix and co-trustees.' The policies when issued promised to pay the amounts stipulated 'to the beneficiary, the executors and administrators or assigns of Samuel F. Carter, Sr., father of the insured.'"); *Am. Auto. Ins. Co. v. CBL Ins. Servs., Inc.*, No. G039051, 2009 WL 1874833, at *1 (Cal. Ct. App. June 30, 2009) ("CBL Insurance Services, Inc. (CBL) was a life insurance agency owned by its president . . . and its vice president American Automobile Insurance Company (American) issued to CBL three annual life insurance agents' and brokers' errors and omissions liability insurance policies. Under the policies American agreed '[t]o pay on behalf of the insured, all sums which the insured shall become legally obligated to

Of course, from the perspective of “innocent” co-insured fiduciaries who have purchased insurance contracts, the prevailing views are these: (1) Insurers should indemnify innocent co-insureds for the latter’s lost interests when deviant co-insured fiduciaries intentionally or negligently destroy jointly owned or community property; and (2) on behalf of innocent co-insured fiduciaries, insurers should pay third-party persons when deviant co-insureds use jointly owned or community property to destroy third-

pay as damages because of: A. Any act, error or omission of the insured, or of any person for whose acts the insured is legally liable in rendering or failing to render professional services for others in the conduct of the . . . insured’s profession as a: 1. Licensed Life Agent, Broker, Brokerage General Agent, General Agent or Manager . . . ; B. Any real or alleged negligence in rendering or failing to render professional services under: 1) the Employee Retirement Income Security Act of 1974, 2) the Securities Act of 1933, 3) the Securities Exchange Act of 1934, 4) the Investment Company Act of 1940, 5) the Investment Advisors Act of 1940, and 6) any amendment to the above acts, which occurs in the conduct of the . . . insured’s profession’ ”); *Atlas Assurance Co. of Am. v. Mistic*, 822 P.2d 897, 898 (Alaska 1991) (“Jeannie Mistic and Del Kirk Rutzebeck were married . . . The couple purchased real property . . . [and] owned the house jointly as tenants in common. First Interstate Bank held a deed of trust note as mortgagee. The property was insured by Atlas Assurance Company of America for \$42,000, with First Interstate named as loss payee”); *Laho v. Century 21 Baltes-Selsberg*, 555 N.W.2d 149, 150-51 (Wis. App. 1996) (“Donna Jantz is a real estate salesperson affiliated with Century 21 Baltes-Selsberg. Jantz has been sued by two of her clients because of drainage problems in the land they purchased. Since the property was previously owned by the sole shareholders in the Baltes-Selsberg firm, the firm’s insurer, Continental Casualty Company, claims that its errors and omissions liability policy does not cover this occurrence. . . . The first clause [appears in] the ‘definitions’ section of Continental’s policy; it states that the words ‘you’ or ‘your’ mean: A. the entity named on the Declarations of this policy as the Named Insured; B. any of your: 1) partners, if you are a partnership; or 2) executive officers, directors, administrators, or stockholders if you are a corporation; [or] 3) brokers, agents, employees, salespersons, or common law or statutory independent contractors”); *Md. Cas. Co. v. Reeder*, 270 Cal. Rptr. 719, 720 (Cal. Ct. App. [4th Dist.] 1990) (“Samuel Pearlman purchased three adjoining parcels of vacant land in Carlsbad Thereafter Pearlman formed. . . Roundtree, Ltd., a partnership. The partnership in turn formed a joint venture with . . . Twelve Trees Corporation. The joint venture was named Roundtree Condominiums. . . . At various stages between 1980 and 1985, Pearlman, Roundtree, Ltd., Twelve Trees, Roundtree Condominiums and DMF were . . . named insureds on a series of comprehensive general liability policies issued by . . . Maryland Casualty Company.”); *King v. Dallas Fire Ins. Co.*, 27 S.W.3d 117, 121-22 (Tex. App.—Houston [1st Dist.] 2000) (“King’s commercial general liability policy . . . provides in pertinent part: . . . ‘We will pay those sums that the insured becomes legally obligated to pay as damages because of ‘bodily injury’ or ‘property damage’ to which this insurance applies. . . . ‘Employee’ includes a ‘leased worker.’ . . . ‘Leased worker’ means a person leased to you by a labor leasing firm under an agreement between you and the labor leasing firm, to perform duties related to the conduct of your business.”); *Nev. Ref. Co. v. Newton*, 497 P.2d 887, 889 (Nev. 1972) (“the policy with Hartford had been and was in effect when the parties signed the conditional sales agreement. . . . [The] parties intended that Nevada Refining Co. (buyer) [to] continue the insurance already in effect, with Refiners Sales Company (seller) as the named insured, for the benefit of the seller, Refiners Sales Company, until the full purchase price had been paid. The record supports that finding. The essence of a conditional sales contract is that the seller shall retain and not relinquish title to the property the subject of the sale until the buyer pays in full the agreed purchase price. . . . The district judge found that . . . was the intent of the parties . . . [and] properly concluded that the seller had an equitable lien on the insurance proceeds[.]”); *Parkview Baptist Church & Sch. v. White*, 971 So. 2d 1078, 1079 (La. App. [1st Cir.] 2007) (“The Farmers’ Insurance Exchange policy provides as follows: ‘Insured’ means you and residents of your household who are: a) your relatives; or b) other persons under the age of 21 and in the care of any person named above.”); *Kulubis v. Tex. Farm Bureau Underwriters Ins. Co.*, 706 S.W.2d 953, 954 (Tex. 1986) (“Betty and John Kulubis were married Her parents subsequently gave them a mobile home upon which they purchased a homeowners insurance policy from Texas Farm. Both Betty and John were named insureds in the policy.”).

parties' persons and property.⁵ To be sure, in light of innocent fiduciaries' expectations, the legal controversies surrounding the enforceability of co-insureds contracts are extremely heated, highly litigated, and fairly dated.⁶

To illustrate, consider the facts and controversy in a Louisiana case decided in 1845.⁷ In *Henderson v. Western Marine & Fire Insurance Co.*, the agent for a commercial firm purchased an insurance contract that insured the firm's property against fire.⁸ The policy also listed the agent as a co-insured.⁹ While the policy was current, a fire destroyed the firm's merchandise.¹⁰ The firm asked the insurer to indemnify the firm for the loss.¹¹ Western Marine & Fire Insurance Company (Western) denied the claim, asserting the following: (1) the deviant co-insured fiduciary breached conditions in the insurance contract; and (2) the deviant co-insured agent committed fraud by intentionally designing and causing the fire.¹²

A jury decided in favor of the commercial firm, and Western appealed to the Louisiana Supreme Court.¹³ Before the Louisiana Supreme Court, the central question was whether the deviant agent's intentional conduct prevented the innocent firm from collecting insurance proceeds.¹⁴ The court addressed this question without deciding whether the principal and the agent were co-insured fiduciaries under Western's insurance contract.¹⁵ To decide the case, the Supreme Court of Louisiana cited and considered several fundamental agency rules, including: A principal is liable for an agent's frauds, deceits, and misrepresentations, if those acts occur within the course of the agent's employment and without the principal's knowledge.¹⁶ Furthermore, the agent's liability may impute to the principal, even if the principal has no direct connection with or influence over the agent's deviant misconduct.¹⁷

However, the Louisiana Supreme Court concluded that those agency principles did not apply to the facts in *Henderson*.¹⁸ Instead, the supreme court affirmed the jury's verdict, concluding that the agent's fraud and intentional conduct did not occur within the course of his agency.¹⁹

5. See William A. McNab, *Minnesota Loss Payable Clauses in Fire Insurance Policies: Falling Short of the Minimum Coverage Requirements*, 26 WM. MITCHELL L. REV. 557, 561-62; Howard Griffin, Inc. v. Progressive Cas. Ins. Co., 409 So.2d 1262, 1262-64 (La. Ct. App. 1982).

6. See *infra* Part II.

7. *Henderson v. W. Marine & Fire Ins. Co.*, 1845 WL 1452 (La. 1845).

8. *Id.* at *1.

9. *Id.*

10. *Id.*

11. *Id.*

12. *Id.*

13. *Id.*

14. *Id.* at *2.

15. *Id.*

16. *Id.*

17. *Id.*

18. *Id.*

19. *Id.*

Because the innocent firm was not responsible for the deviant agent's beyond-the-agency willful, malicious, and unauthorized acts, the court ordered Western to indemnify the commercial firm for the losses resulting from the fire.²⁰

Once more, the *Henderson* decision is dated, as it was delivered nearly 165 years ago; however, *Henderson* is still good law in Louisiana.²¹ Yet, whether innocent co-insured fiduciaries may collect insurance proceeds after deviant co-insureds destroy community property or other property interests still generates lawsuits in Louisiana.²² Interestingly, some very recent Louisiana cases have rejected the decision in *Henderson* and concluded that insurers have no duty to indemnify allegedly innocent co-insured fiduciaries.²³

Without a doubt, conflicting rulings about whether insurers must indemnify innocent fiduciaries appear in other community property and separate property states.²⁴ To illustrate, compare the facts and ruling in *Erlin-Lawler Enters., Inc. v. Fire Insurance Exchange* with those in *Federal Insurance Co. v. Homestore, Inc.*²⁵ In both cases, appellate courts applied California's law and produced very different outcomes. In *Erlin-Lawler*, Dan Erlin, James Lawler and Erlin-Lawler Enterprises, Inc., a California corporation, d/b/a Bestways Market #1, were co-insured fiduciaries under a fire insurance contract.²⁶ Fire Insurance Exchange was the insurer.²⁷ A fire destroyed the corporation's equipment, fixtures, and stock in trade.²⁸ The fire also caused business-interruption losses.²⁹

The insured corporation asked the insurer to indemnify.³⁰ The insurer refused, asserting that the co-insured fiduciaries, Erlin and Lawler, deliberately caused the fire.³¹ In fact, Erlin and Lawler were convicted for

20. *Id.*

21. *Id.*

22. See, e.g., *Crumpler v. State Farm Fire and Cas. Co.*, No. 95-31300, 1996 WL 512065, at *1 (5th Cir. 1996) (citing Louisiana's law and concluding that the insurer had no duty to indemnify the innocent insured spouse after the insured deviant husband's arson destroyed the couple's house in Claiborne Parish, Louisiana).

23. See, e.g., *McNamara v. Augustino Bros., Inc.*, No. 2008-CA-1522, 2009 WL 1332311, at *5 (La. App. [4th Cir.] 2009) (concluding that the insurer had no duty to indemnify the innocent co-insured contractor—under theory of vicarious liability—when for the alleged deviant co-insured employee's criminal and other intentional acts).

24. The community property states are Alaska, Arizona, California, Idaho, Louisiana, New Mexico, Nevada, Texas, Washington, and Wisconsin. See *infra* Part II.B. for a brief discussion of community and separate property laws and statutes.

25. *Erlin-Lawler Enters., Inc. v. Fire Ins. Exch.*, 73 Cal. Rptr. 182 (Cal. Ct. App. 1968); *Fed. Ins. Co. v. Homestore, Inc.*, 144 Fed. App'x. 641 (9th Cir. 2005); see text accompanying notes 26-51.

26. *Erlin-Lawler*, 73 Cal. Rptr. at 183.

27. *Id.*

28. *Id.*

29. *Id.*

30. *Id.*

31. *Id.*

arson.³² Erlin-Lawler Enterprises sued Fire Insurance Exchange asserting that it was an innocent co-insured.³³ Sitting without a jury, the trial court decided against the corporation.³⁴ The trial judge concluded that "Erlin-Lawler Enterprises, Inc., was merely the alter ego of . . . Dan Erlin and James H. Lawler," and the corporation appealed.³⁵ A California Appellate Court reversed the trial court's ruling, embracing the prevailing rule at the time: Recovery under a fire-insurance contract is not defeated when an innocent co-insured corporation's agent intentionally burns corporate property.³⁶

In *Homestore*, the corporation did not prevail.³⁷ Several indemnity insurers sold directors and officers (D & O) insurance contracts to Homestore, Inc.³⁸ The co-insured fiduciaries under the D & O contracts were Homestore, the corporation, and Homestore's current and former directors and officers.³⁹ During the policy's period, federal officials:

[filed] federal information . . . against Homestore's then-CFO Joseph Shew, and two former Homestore officers. The information charged that Mr. Shew conspired to commit securities fraud, in violation of federal law Mr. Shew pleaded guilty to the conspiracy charge and admitted that . . . he conspired to overstate Homestore's advertising revenue to artificially inflate the company's revenues, and [that he] filed false 10Qs with the SEC.⁴⁰

After paying to defend itself and officers in the federal probe, Homestore asked the insurers to reimburse the expended funds.⁴¹ Citing terms under the D & O insurance policies, the corporation claimed that the insurers had a duty to indemnify.⁴² The insurers disagreed.⁴³ They asserted that Homestore's former CFO signed the four insurance applications and materially misrepresented information about Homestore's earnings.⁴⁴

32. *Id.*

33. *Id.*

34. *Id.*

35. *Id.*

36. *Id.* at 183-84.

37. *Fed. Ins. Co. v. Homestore, Inc.*, 144 Fed. App'x. 641, 644 (9th Cir. 2005).

38. *Id.* The insurers were Genesis Insurance Company, Royal Indemnity Company, Federal Insurance Company and Clarendon Insurance Company. *Id.*

39. *Id.*

40. *Id.* at 645.

41. *See id.* at 644.

42. *Id.*

43. *Id.*

44. *Id.* at 644-45.

Homestore submitted a renewal application for D & O liability insurance to Genesis The renewal application required that Homestore provide the "[l]atest 10K and 10Q filed with the SEC." The application was signed by then-CFO Joseph Shew. Homestore also obtained excess D & O liability insurance policies from Royal, Federal, and Clarendon for

Therefore, in light of those material misrepresentations, the insurers claimed that, as a matter of law, they had a right to rescind all insurance policies and deny reimbursements for “all insureds.”⁴⁵

The insurers filed a declaratory judgment action in a federal district court to determine their obligations under the insurance contracts.⁴⁶ Agreeing with the insurers, the district court concluded that the D & O insurance contracts unambiguously allowed the insurers to rescind coverage for “all Insureds” if one or more deviant co-insured fiduciaries signed and misrepresented material information on the insurance application.⁴⁷ Refusing to accept that conclusion, the innocent corporation appealed.⁴⁸

The Court of Appeals for the Ninth Circuit affirmed the district court’s summary judgment.⁴⁹ The Ninth Circuit concluded that “the clear and explicit language” of the D & O policy permitted the insurers to rescind the insurance contracts for “all Insureds” based upon the former co-insured CFO’s misrepresentations in the insurance application.⁵⁰ But even more importantly, the Ninth Circuit fashioned a new law of the circuit: California public policy does not prevent insurers from rescinding coverage for “innocent” directors and officers when deviant directors and officers insert misrepresentations in insurance applications.⁵¹

Moreover, insured, innocent spouses also sue insurers who fail to indemnify after an insured, deviant spouse destroys various property

the same coverage period Section VIII(C) of the Genesis Policy, entitled ‘REPRESENTATIONS’ provides:

It is agreed that the information and statements contained in the Application for this Policy, a copy of which is attached hereto, and any materials submitted therewith (which are on file with the Insurer and shall be deemed to be attached to and part of the Application as if physically attached hereto), are the basis of this Policy and are to be considered as incorporated into and constituting a part of this Policy.

By acceptance of this Policy the Directors and Officers and the Company agree:

(1) That the statements in the Application and in any materials submitted therewith are their representations, that they shall be deemed material to the acceptance of the risk or hazard assumed by the Insurer under this Policy, and that this Policy is issued in reliance upon the truth of such representations; . . .

Homestore’s filings with the SEC disclosed growth in advertising revenues throughout the period. On December 21, 2001, however, Homestore announced that its Board of Directors was conducting a review of the company’s financial statements, and that it would be making restatements of historical earnings at the conclusion of the review As a result of the financial restatements, multiple securities claims and shareholder derivative suits were filed.

Id.

45. *Id.* at 644.

46. *Id.* at 642.

47. *Id.*

48. *Id.* at 647.

49. *Id.* at 648.

50. *Id.*

51. *Id.*

interests.⁵² In fact, innocent spouse cases comprise the largest category of all innocent co-insured disputes.⁵³ Like disagreements between insurers and other co-insureds, innocent co-insured spouses sue insurers in both separate and community property states.⁵⁴ Also, among innocent co-insured spouse cases, about one-third of the disputes concern whether insurers have a duty to indemnify innocent spouses fully or partially when deviant spouses destroy community property.⁵⁵ However, the greater majority of innocent co-insured spouse controversies concern whether insurers have a duty to indemnify innocent spouses when deviant spouses destroy jointly owned property or property that spouses hold as tenants by entirety or tenants in common.⁵⁶

Innocent fiduciary disputes generally, and innocent co-insured spouse actions in particular, generate a lot of conflicting rulings and outcomes within and between state and federal judiciaries.⁵⁷ More significant, even after state supreme courts have issued “definitive” innocent co-insured rulings, intra- and interstate splits continue among state courts.⁵⁸ Similarly, intra- and inter-circuit conflicts also persist among the federal circuits.⁵⁹ Even more relevant, some legislatures in community property states enacted

52. See *Jones v. Fid. & Guar. Ins. Corp.*, 250 S.W.2d 281, 281 (Tex. Civ. App.—Waco 1952, writ ref’d.).

53. See Table 1, *infra* at note 692.

54. *Id.*

55. *Id.*

56. *Id.*

57. Compare *Norman v. State Farm Fire & Cas. Co.*, 804 F.2d 1365, 1366 (5th Cir. 1986) (stressing that denying deviant co-insureds a benefit is the single most important consideration and declaring that the co-insured innocent spouse could not recover any proceeds because there was a possibility that the deviant co-insured spouse might benefit), and *Webster v. State Farm Fire & Cas. Co.*, 953 F.2d 222, 223 (5th Cir. 1992) (concluding that a post-fire divorce between the innocent and deviant co-insured spouses, which awarded half of the insurance proceeds on the destroyed community property to the innocent spouse as separate property, still did not permit the innocent spouse to recover insurance proceeds for a pre-divorce arson fire), with *Tex. Farmers Ins. Co. v. Murphy*, 996 S.W.2d 873, 881 (allowing an innocent co-insured to recover insurance money when a deviant co-insured spouse intentionally destroys community property).

58. Compare *McEwin v. Allstate Tex. Lloyds*, 118 S.W.3d 811, 815-16 (Tex. App.—Amarillo, 2003) (“Kathy’s status as an innocent spouse does not determine her right to recover from Allstate The series of events encompassing James’ intentionally causing loss of the insured home and turning in a loss report without disclosing that the loss was due to his intentional acts comprised perpetration of fraud on Allstate relating to the insurance, even had James not made false statements in his later examinations under oath. Because of James’ fraud, the Concealment or Fraud clause voided the policy as to both James and Kathy”) with *Tex. Farmers Ins. Co. v. Murphy*, 996 S.W.2d 873, 881 (“We reaffirm our longstanding public policy [of] preventing an arsonist from benefitting from fraud by denying recovery of his or her own one-half interest in the claim against the insurer. We conclude, however, that such public policy does not overcome an innocent spouse’s contractual right to recover her or his one-half interest in policy benefits.”).

59. Compare *Commercial Union Ins. Co. v. State Farm Fire & Cas. Co.*, 546 F. Supp. 543, 546 (D.C. Cir. 1982) (stating rights and obligations under homeowner’s insurance policy are several and not joint. Therefore innocent spouse may recover even though co-insured spouse is at fault), with *Cal. Ins. Co. v. Allen*, 235 F.2d 178, 180 (5th Cir. 1956) (concluding that an innocent co-insured spouse may not recover insurance proceeds if the deviant spouse torches community property).

“innocent spouse” statutes.⁶⁰ Put simply, those statutes are designed to protect innocent co-insured spouses’ insurable interests after insured deviant spouses intentionally destroy community property.⁶¹ Still, in light of those statutes, conflicting state and federal court rulings and declarations persist.⁶²

Without doubt, for at least a century and a half, national property insurers have been selling standardized, or fairly identical, property insurance contracts in the majority of states and across the federal circuits.⁶³ Yet, whether insurers must indemnify innocent co-insured spouses and other co-insured fiduciaries under those boilerplate contracts has generated judicial conflicts nearly as long in both community and separate property states.⁶⁴ Assuredly, some commentators and federal judges have recognized the pervasiveness of the conflicts and tried to explain them.⁶⁵ However, those jurists’ and commentators’ efforts have fallen short, and the reason is not complicated. Barring one researcher’s efforts, the overwhelming majority of jurists and scholars have surveyed or analyzed primarily the following: (1) business-related, innocent co-insured cases; (2) innocent co-insured spouse cases in separate property states; or (3) innocent co-insureds cases involving arson.⁶⁶

60. See *infra* Part II.

61. See *infra* Part II.

62. See *infra* Part II.

63. Cf. Willy E. Rice, *Commercial Terrorism from the Transatlantic Slave Trade to the World Trade Center Disaster: Are Insurance Companies & Judges “Aiders and Abettors” of Terror?—A Critical Analysis of American and British Courts’ Declaratory and Equitable Actions, 1654-2002*, 6 SCHOLAR 1, 63-66 nn.287-300 (2003) (reviewing the evolution and sale of marine and other forms of property insurance in America in the mid-1700s).

64. See, e.g., *Kosior v. Cont’l Ins. Co.*, 13 N.E.2d 423, 425 (Mass. 1938); *Jones v. Fid. & Guar. Ins. Corp.*, 250 S.W.2d 281, 281 (Tex. Civ. App.—Waco 1952, writ ref’d).

65. See, e.g., *Trinity Universal Ins. Co. v. Kirsling*, 73 P.3d 102, 105 (Idaho 2003) (listing majority and minority decisions vis-a-vis the rights of innocent co-insured spouses); *Atlas Assur. Co. of Am. v. Mystic*, 822 P.2d 897, 899-901 (Alaska 1991) (highlighting major conflicts without providing analysis of the split decisions); *Hedtcke v. Sentry Ins. Co.*, 326 N.W.2d 727, 737-39 (Wis. 1982) (outlining the a long list of conflicts among courts and presenting plausible explanations); *Murphy v. Tex. Farmers Ins. Co.*, 982 S.W.2d 79, 80-82 (Tex. App.—Houston [1st Dist.] 1998) (chronicling the history of conflicting innocent co-insured decisions among Texas’s courts); *Cal. Casualty Ins. Co. v. Northland Ins. Co.*, 56 Cal. Rptr. 2d 434, 442 (Cal. App. [4th Dist.] 1996) (discussing conflicting innocent co-insured decisions); and *Thoele v. Aetna Cas. & Sur.*, 39 F.3d 724, 727-28 n.1 (7th Cir. 1994) (presenting an extensive list and highlighting various courts’ explanations).

66. See Rachel R. Watkins Schoenig, *Property Insurance and the Innocent Co-Insured: Was It All Pay and No Gain for the Innocent Co-Insured?* 43 DRAKE L. REV. 893 (1995); David L. Nersessian, *Penalty by Proxy: Holding the Innocent Policyholder Liable for Fraud by Coinsureds, Claims Professionals, and Other Agents*, 38 TORT TRIAL & INS. PRAC. L.J. 907 (2003); Benjamin M. Parrott, *For Better or For Worse? The Iowa Supreme Court’s Decision to Compensate the Innocent Coinsured Spouse in Sager v. Farm Bureau Mutual Insurance Company*, 54 DRAKE L. REV. 561 (2006); John F. Dobbyn, *Subrogation and the Innocent Spouse Dilemma*, 78 ST. JOHN’S L. REV. 1095 (2004); Ronald S. Ribaud, *Burning Down the House: Does Limiting the Innocent Spouse’s Right To Recover Make Sense?—DePalma v. Bates County Mutual Insurance Company*, 67 MO. L. REV. 77 (2002); Michael J. Sudekum, *Homeowner’s Policies and Missouri Law Make Recovery for the Domestic Violence Victim/Co-Insured an Olympic Challenge*, 69 UMKC L. Rev. 363 (2000); Brent R. Lindahl, *Insurance*

But, most state and federal courts decide all sorts of innocent co-insureds controversies involving corporations, spouses, partnerships, trustees, estates, executors, administrators, and other persons simply residing or doing business in community and separate property states.⁶⁷ As of this writing, a fairly comprehensive, theoretical, and empirical analysis of these decisions has not occurred. Arguably, such an analysis is warranted. Therefore, this article attempts to fill that gap.

Part II presents a short discussion of selected pairs of persons' fiduciary duties to each other: Corporations and officers, partners and partnerships, joint venturers, executors and administrators, and husbands and wives.⁶⁸ Fairly often, innocent contractual parties are victimized when their deviant co-parties engage in negligent and intentional activities.⁶⁹ In those situations, and from an insurance perspective, those innocent parties are first-party victims under various property and casualty insurance contracts.⁷⁰ After innocent first-party victims spend money to become whole again and ask insurers to indemnify, insurers often refuse.⁷¹ To defend themselves, indemnity insurers raise the "breach of fiduciary duty" affirmative defense, by showing that the innocent fiduciaries' first-party claims are excluded because the innocent or deviant co-insured fiduciary breached a fiduciary duty.⁷² Thus, Part II highlights some of those relationships and fiduciary obligations as they appear in separate and community property states.⁷³

Quite often, the following issue is litigated: whether innocent fiduciaries in a commercial, professional, or familial relationship are vicariously liable when deviant co-parties destroy third-party victims' property or person.⁷⁴ It is relevant here because indemnity insurers often employ the doctrine of "vicarious liability" to prevent innocent co-insured fiduciaries from securing insurance proceeds after deviant co-insureds injure third-parties or destroy the latter's property.⁷⁵ In addition, insurers

Coverage for an Innocent Co-Insured Spouse, 23 WM. MITCHELL L. REV. 433 (1997); Michele E. Randazzo, *Innocent Spouse Not Allowed To Recover Under Joint Insurance Policy Where Other Spouse Intentionally Caused Loss—Dolcy v. Rhode Island Joint Reinsurance Ass'n*, 591 A.2d 313 (R.I. 1991), 26 SUFFOLK U. L. REV. 556 (1992); Leane English Cerven, *The Problem of the Innocent Coinsured Spouse: Three Theories of Recovery*, 17 VAL. U. L. REV. 849 (1983); Jill R. Wilson, *Insurance Law—Innocent Spouse's Right to Recover in Arson Cases*, 17 WAKE FOREST L. REV. 1022, 1034 (1981); Comment, *Spouse's Fraud as a Bar to Insurance Recovery*, 21 WM. & MARY L. REV. 543 (1979-1980); D. E. Evins, *Fraud, False Swearing, or Other Misconduct of Insured as Barring Recovery on Property Insurance by Innocent Coinsured*, 24 A.L.R.3d 450 (1969).

67. See *infra* Part II.

68. See *infra* Part II.

69. See *infra* Part II.

70. See *infra* Part II.

71. See *infra* Part II.

72. See *Lawyers Title Ins. Corp. v. JDC (America) Corp.*, 52 F.3d 1575, 1575-78 (11th Cir. 1995).

73. See *infra* Part II.

74. See *infra* Part II.

75. See *infra* Part II.

raise the vicarious liability defense when deviant co-insured fiduciaries either negligently or intentionally damage third-parties' property or persons.⁷⁶

Therefore, prudent insurance consumers commonly purchase two types of insurance contracts.⁷⁷ Some insurance agreements are called "first-party insurance."⁷⁸ First-party insurance covers innocent insureds' person and property.⁷⁹ The other is labeled "third-party insurance."⁸⁰ The latter covers innocent insureds who might be vicariously liable for deviant co-insureds' negligent or intentional conduct.⁸¹ Unquestionably, there are major and legally significant differences between the two categories of insurance.⁸² Part III briefly discusses those insurance contracts, since innocent co-insured spouses and other co-insured fiduciaries commence legal actions against insurers under both first and third-party insurance contracts.⁸³

What types of legal actions? Generally, innocent co-insured fiduciaries and insurers file declaratory judgment actions in both state and federal courts, asking those tribunals to declare either rights or obligations under first and third-party insurance contracts.⁸⁴ Therefore, Part IV discusses the purpose and scope of declaratory judgment suits under federal and state declaratory judgment statutes.⁸⁵

Part V presents a discussion of whether insurers have a duty to indemnify innocent co-insured fiduciaries under first-party insurance contracts.⁸⁶ Part VI critiques whether insurers have a duty to pay claims on behalf of innocent co-insureds under third-party insurance contracts.⁸⁷ Necessarily, both Parts IV and V will highlight and discuss state and federal courts' conflicting declaratory judgments.⁸⁸ Those discussions will also outline, compare, and contrast the various legal and equitable doctrines that federal and state judges employ to deny or award declaratory relief.⁸⁹

Finally, Part VII presents an empirical study and discusses the disposition of innocent co-insured fiduciary decisions, dating from the 1800s.⁹⁰ That theoretical and empirical analysis is designed to find a more

76. See *infra* Part II.

77. See *infra* Part II.

78. See *infra* Part II.

79. See *infra* Part II.

80. See *infra* Part II.

81. See *infra* Part II.

82. See *infra* Part II.

83. See *infra* Part III.

84. See *infra* Part IV.

85. See *infra* Part IV.

86. See *infra* Part V.

87. See *infra* Part VI.

88. See *infra* Parts IV, V.

89. See *infra* Parts IV, V.

90. See *infra* Part VII.

comprehensive or more plausible explanations for the persistent judicial conflicts among innocent co-insured cases.⁹¹ Stated slightly differently, the presentation in Part VII will attempt to harmonize discordant judicial judgments which appear to be unexplainable conflicts.⁹²

The article concludes by encouraging state and federal judges to apply more carefully settled, equitable doctrines to interpret insurance contracts and to award or deny innocent co-insureds petitions for declaratory relief.⁹³ Current and past courts have considered illusive public policy to interpret valid insurance contracts, and that practice helps to generate judicial conflicts.⁹⁴

II. SELECTED FIRST-PARTY FIDUCIARIES' COMMON LAW AND STATUTORY RIGHTS AND OBLIGATIONS

This section discusses selected co-parties' fiduciary obligations to each other. Insurers have used insured deviant co-parties' breach of fiduciary duty as an affirmative defense to prevent innocent co-insured fiduciaries from recovering under indemnity insurance contracts as illustrated in *Lawyers Title Insurance Corp. v. JDC (Am.) Corp.*⁹⁵ In *Lawyers*, JDC America Corporation (JDC) and Brickell Station Towers, Inc. (BST) were lender/mortgagee and partner/developer, respectively.⁹⁶ They formed a joint venture to develop property, and the venture borrowed \$38 million from JDC.⁹⁷ As mortgagee, JDC held the mortgages and Lawyers Title insured the mortgages under two title insurance contracts.⁹⁸ "The development of the property did not proceed as planned."⁹⁹

JDC filed a foreclosure action against the joint venture and BST.¹⁰⁰ However, the insurer refused to provide legal representation for JDC in the foreclosure action.¹⁰¹ As a consequence, JDC retained independent legal representation and settled the foreclosure action with BST.¹⁰²

JDC asked the title insurer to reimburse the funds used to settle the case and pay attorneys' fees.¹⁰³ The title insurer refused and filed a declaratory judgment action to determine whether it had a contractual duty

91. See *infra* Part VII.

92. See *infra* Part VII.

93. See *infra* Part VIII.

94. See *infra* Part VIII.

95. See generally *Lawyers Title Ins. Corp. v. JDC (Am.) Corp.*, 52 F.3d 1575 (11th Cir. 1995) (illustrating how this defense is used).

96. *Id.* at 1576-77.

97. *Id.* at 1577.

98. *Id.*

99. *Id.*

100. *Id.* (neither party could agree on the scope of representation).

101. *Id.* at 1578-79.

102. *Id.* at 1579.

103. *Id.*

to defend and/or indemnify JDC.¹⁰⁴ JDC filed an answer to the declaratory judgment action.¹⁰⁵ In addition, the JDC filed a counteraction alleging that Lawyers Title breached the title insurance contracts by refusing to defend and indemnify JDC.¹⁰⁶

Lawyers Title fashioned a unique and effective affirmative defense to defend itself against JDC's breach-of-contract action.¹⁰⁷ Before JDC and BST settled the foreclosure action, BST and the joint venture defended themselves by raising several defenses, such as the breach of fiduciary duty and the breach of loyalty among partners affirmative defenses.¹⁰⁸ To raise the breach of fiduciary duty defense effectively, Lawyers Title cited an exclusion clause in one of the title insurance contracts.¹⁰⁹ That clause excluded "[d]efeats, liens, encumbrances, adverse claims, or other matters . . . created, suffered, assumed or agreed to by the insured claimant"¹¹⁰

Embracing the district court's conclusion, the Court of Appeals for the Eleventh Circuit concluded that the title insurer had no duty to indemnify and no duty to defend JDC because BST's attacks were matters that JDC "created, suffered, assumed or agreed to."¹¹¹ Or stated differently, the title insurer asserted that it had no duty to indemnify because JDC entered into an excluded agreement.¹¹² Again this is an example of the breach of fiduciary duty affirmative defense, which is very different from an action that is premised on one's breach of a fiduciary duty.¹¹³

A. Commercial, Business, and Professional Persons' Fiduciary Obligations and Relationships in Community and Separate Property States

Put simply, in both separate and community property states, "[a] fiduciary relationship arises between two persons when one person [has] a

104. *Id.*

105. *Id.*

106. *Id.*

107. *Id.* at 1578.

108. *Id.* at 1578 n.5.

109. *Id.* at 1580.

110. *Id.* (quoting *Lawyers Title Ins. Corp. v. JDC (Am.) Corp.*, 818 F. Supp. 1543, 1546-48 (S.D. Fla. 1993)).

111. *Id.*

112. *Lawyers Title Ins. Corp.*, 52 F. 3d at 1580 (JDC's entered into an adverse fiduciary relationship in which the "deviant," co-insured BST breached its fiduciary duty).

113. *Cf. Zakibe v. Ahrens & McCarron, Inc.*, 28 S.W.3d 373, 384-85 (Mo. App. 2000) ("Plaintiff asserts that the trial court erred in giving [an instruction] which submitted the affirmative defense of breach of fiduciary duty. . . He argues that breach of a fiduciary duty is not a defense to a breach of contract claim As an affirmative defense to plaintiff's breach of employment contract claim, defendant alleged that . . . plaintiff had breached his fiduciary duty . . . and defendant was thereby excused from performing any obligations under the employment contract. . . . This rule has its source in agency law."). See *Liberty Mut. Fire Ins. Co. v. LcL Adm'rs, Inc.*, 78 Cal. Rptr. 3d 200, 202 (Cal. Ct. App. 2008) ("LcL filed an answer to the complaint, generally denying the allegations and raising 28 affirmative defenses, including breach of contract, breach of fiduciary duties and bad faith.").

duty to act for or give advice for the benefit of another on matters within the scope of their relationship.”¹¹⁴ Although courts in community and separate property states have fashioned competing definitions of a “fiduciary duty,” the Minnesota Supreme Court crafted the following definition that summarizes most: A fiduciary relationship is characterized by a fiduciary who enjoys a superior position in terms of knowledge and authority and in whom the other party places a high level of trust and confidence.¹¹⁵

In certain formal relationships, such as an attorney-client or trustee relationship, a fiduciary duty arises as a matter of law.¹¹⁶ In addition, the Texas Supreme Court recognizes that certain informal relationships may give rise to a fiduciary duty.¹¹⁷ “Such informal fiduciary relationships have also been termed ‘confidential relationships’ and may arise ‘where one person trusts in and relies upon another, whether the relation is a moral, social, domestic or merely personal one.’”¹¹⁸ Even more importantly, as a matter of law, each person agrees that equity courts’ standard of loyalties will measure the quality of the person’s conduct towards the other person after the fiduciary relationship forms.¹¹⁹

Courts in both separate and community property states have found fiduciary relationships between the following pairs of commercial, business and professional persons: attorneys and clients, executors/administrators and estates’ beneficiaries, trustees and various other beneficiaries, joint venturers, corporations and directors/officers, partners and partnerships, insurers and insureds, principals and agents, and brokers and clients.¹²⁰ Generally, courts in community and separate property states require parties’

114. *F.G. v. MacDonell*, 696 A.2d 697, 704 (N.J. 1997); *see also* *Manges v. Guerra*, 673 S.W.2d 180, 183 (Tex. 1984) (concluding that the fiduciary duty arises from the relationship of the parties and not from the terms of a contract).

115. *Toombs v. Daniels*, 361 N.W.2d 801, 809 (Minn. 1985); *see also* *Kolodge v. Boyd*, Nos. A10485, A102094, 2004 WL 2669272, at *5 (Cal. App. 1 Dist. Nov. 23, 2004) (“A fiduciary duty may be described as a cluster of obligations owed by one person, the trustee or fiduciary, toward another, the ‘cestui’ or beneficiary, with respect to an identified subject matter, known as the ‘res’ or ‘subject of trust.’”).

116. *See* *Johnson v. Brewer & Pritchard, P.C.*, 73 S.W.3d 193, 199 (Tex. 2002).

117. *See* *Thigpen v. Locke*, 363 S.W.2d 247, 253 (Tex. 1963); *see also* *Crim Truck & Tractor Co. v. Navistar Int’l Transp. Corp.*, 823 S.W.2d 591, 594 (Tex. 1992) (reaffirming that an informal fiduciary relationship exists in a family relationship or otherwise, if one party has become accustomed to being “guided by the judgment or advice” of the other.).

118. *See* *Crim Truck & Tractor Co.*, 823 S.W.2d at 594 (quoting *Fitz-Gerald v. Hull*, 237 S.W.2d 256, 261 (Tex. 1951)).

119. *See* *Texas Bank and Trust Co. v. Moore*, 595 S.W.2d 502, 508 (Tex. 1980) (citing *Johnson v. Peckham*, 120 S.W.2d 786, 788 (Tex. 1938)).

120. *See, e.g., Rhone-Poulenc Agro S.A. v. Monsanto Co.*, 73 F. Supp. 2d 540, 546 (M.D.N.C. 1999) (“Generally, in North Carolina . . . there are two types of fiduciary relationships: (1) those that arise from ‘legal relations such as attorney and client, broker and client . . . partners, principal and agent, trustee and cestui que trust,’ and (2) those that exist ‘as a fact, in which there is confidence reposed on one side, and the resulting superiority and influence on the other.’”); *see also* *Four Bros. Boat Works, Inc. v. Tesoro Petroleum Co.’s, Inc.*, 217 S.W.3d 653, 668-69 (Tex. App.—Houston [14th Dist.] 2006 pet. denied) (providing a list of various fiduciary relationships).

comprising commercial, business, and professional relationships to conform to a very similar or an identical fiduciary standard.

A few examples should support the assertion. First, corporations can only act through individuals—its officers and directors.¹²¹ Therefore, in community and separate property states, corporate directors and officers must discharge their duties as follows: (1) in good faith; (2) in a reasonable manner that serves the best interests of the corporation; and (3) with care that an ordinarily prudent person would exercise under identical or similar circumstances.¹²² Likewise, courts in separate and community property states declare that partners and partnerships have fiduciary relationships, and partners are held to high standards of integrity when dealing with each other.¹²³

In fact, for decades, and as a matter of common law, the Texas Supreme Court has declared: “[T]he relationship between . . . partners . . . is fiduciary in character, and imposes upon all the participants the obligation of loyalty to the joint concern [as well as the duty to exercise] the utmost good faith, fairness, and honesty in their dealings with each other [vis-à-vis matters related] to the enterprise.”¹²⁴ Furthermore, since a partner is a fiduciary, Texas’s law imposes on a partner the same obligation that it imposes on a corporate fiduciary: A partner may not usurp corporate opportunities.¹²⁵

Without a doubt, under rules in community and separate property states, joint ventures and partnerships are not legal twins. Yet, joint venture and partner relationships are quite similar. For example, under the Texas Uniform Partnership Act, a partnership or joint venture is an association of

121. See *Leitch v. Hornsby*, 935 S.W.2d 114, 117 (Tex.1996).

122. See, e.g., N.C. GEN. STAT. § 55-8-30(a) (2007); MINN. STAT. ANN. § 302A.251(1) (2004) (“A director shall discharge the duties of the position of director in good faith, in a manner the director reasonably believes to be in the best interests of the corporation, and with the care [that] an ordinarily prudent person in a like position would exercise under similar circumstances.”); *Malone v. Brincat*, 722 A.2d 5, 10 (Del. 1998) (reiterating that a director’s fiduciary duty to both the corporation and its shareholders is a triad comprising “due care, good faith, and loyalty.”); *Tritek Telecom, Inc. v. Superior Court*, 87 Cal. Rptr. 3d 455, 459 (Cal. Ct. App. 2009) (declaring that corporate directors owe a fiduciary duty of care to the corporation and its shareholders and must serve “in good faith, in a manner such director believes to be in the best interests of the corporation and its shareholders[.]”); *Pierce Concrete, Inc. v. Cannon Realty & Constr. Co.*, 335 S.E.2d 30, 31 (N.C. Ct. App. 1985) (corporate directors owe fiduciary duties to the corporation); *Int’l Bankers Life Ins. Co. v. Holloway*, 368 S.W.2d 567, 577 (Tex. 1963) (stressing that corporate officers or directors have an obligation not to usurp corporate opportunities for their personal gain, and that corporations may seize directors’ and officers’ ill-gained profits).

123. See *Appletree Square I Ltd. P’ship v. Investmark, Inc.*, 494 N.W.2d 889, 892 (Minn. Ct. App. 1993).

124. See *Bohatch v. Butler & Binion*, 977 S.W.2d 543, 545 (Tex. 1998) (quoting *Fitz-Gerald v. Hull*, 237 S.W.2d 256, 264 (Tex. 1951); see also *Lipinski v. Lipinski*, 35 N.W.2d 708, 712 (Minn. 1949) (embracing the view that the partners or joint entrepreneurs’ relationship are based on mutual trust and confidence and reiterating that the law imposes upon partners the highest standard of integrity and good faith in their dealings with each other).

125. See *Int’l Bankers Life Ins. Co. v. Holloway*, 368 S.W.2d 567, 577 (Tex. 1963).

two or more persons who have agreed to be co-owners of a for-profit business or enterprise.¹²⁶ “[A] partnership consists of an express or implied agreement containing four required elements: (1) a community of interest in the venture; (2) an agreement to share profits; (3) an agreement to share losses; and (4) a mutual right of control or management of the enterprise.”¹²⁷ Thus state courts employ partnership rules to determine joint venturers’ rights and liabilities.¹²⁸

When joint venturers consummate an agreement, they also create a fiduciary relationship as a matter of common law.¹²⁹ Therefore, for the benefit of each other, joint venturers must: (1) act in good faith; (2) keep confidences; and (3) be loyal for the benefit of each other.¹³⁰ However, joint venturers’ fiduciary obligations only govern matters within the scope of the joint endeavor.¹³¹ Furthermore, each member has a duty to act responsibly and prudently for the benefit of others when matters are clearly within the scope of the relationship.¹³² In addition, when a joint venturer promotes the venture, the joint venturer is the agent for all members in the relationship.¹³³ Each member has a fiduciary duty to disclose completely all material information that might or could affect the enterprise.¹³⁴ Finally, innocent venturers may sue deviant venturers when the latter’s misrepresentations and fraudulent activities occur within the scope of the joint enterprise and undermine innocent venturers’ interests.¹³⁵

Once more, a fiduciary is a person who does as follows: (1) occupies a position of “peculiar confidence,” (2) has a considerable amount of “integrity and fidelity,” (3) acts in “good faith,” and (4) deals fairly for the benefit of another person.¹³⁶ Therefore, in separate property, community property, and employment-at-will states, an employee may owe his or her employer a fiduciary duty under certain circumstances.¹³⁷ “When a

126. TEX. REV. CIV. STAT. ANN. art. 6132b, § 6 (Vernon Supp. 2007).

127. Schlumberger Tech. Corp. v. Swanson, 959 S.W.2d 171, 176 (Tex. 1997) (citing Coastal Plains Dev. Corp. v. Micrea, Inc., 572 S.W.2d 285, 287 (Tex.1978)).

128. See, e.g., Burtell v. First Charter Service Corp., 394 N.E.2d 380, 384 (Ill. 1979) (“A joint venture may be established without a specified formal agreement. . . . A fiduciary relationship exists between members of the joint venture. . . . When a joint venture is found to exist, the legal principles pertaining to the relationship between partners govern.”); but see Warner v. Winn, 197 S.W.2d 338, 342 (Tex.1946) (holding that parties are not partners in a fiduciary relationship if they carefully defined the extent of their enterprise in a contract).

129. See Carroll v. Caldwell, 147 N.E.2d 69, 71-72 (Ill. 1957).

130. See Ditis v. Ahlvin Const. Co., 97 N.E.2d 244, 250 (Ill. 1951).

131. See Yokel v. Hite, 809 N.E.2d 721, 728 (Ill. App. Ct. 2004).

132. See Carroll, 147 N.E.2d at 75.

133. See Stone v. Guthrie, 144 N.E.2d 165, 170 (Ill. App. Ct. 1957).

134. See Bakalis v. Bressler, 115 N.E.2d 323, 328 (Ill. 1953).

135. See Hagerman v. Schulte, 181 N.E. 677, 684-85 (Ill. 1932).

136. See Daniel v. Falcon Interest Realty Corp., 190 S.W.3d 177, 185 (Tex. App. —Houston [1st Dist.] 2005, no pet.).

137. See, e.g., Cenla Physical Therapy & Rehab. Agency, Inc. v. Laverigne, 657 So. 2d 175, 177 (La. Ct. App. 1995) (discussing whether employees were acting in the interest of their employer).

fiduciary relationship of agency exists between employee and employer, the employee has a duty to act primarily for the benefit of the employer in matters connected with his agency.”¹³⁸

Furthermore, a fiduciary has a duty to deal openly with his employer and to fully disclose material information that might affect the employer’s enterprise.¹³⁹ An employee commits an actionable wrong when he uses his employment status to seize business opportunities, which correctly belong to the employer.¹⁴⁰ Agency principles also prevent an employee from commencing a for-profit enterprise or business that competes with the employer’s enterprise.¹⁴¹ However, a fiduciary relationship does not prevent an employee from preparing to compete with the employer.¹⁴² Absent an anti-competition agreement, an employee does not breach his fiduciary obligation when he prepares to compete with his employer.¹⁴³

Even more significant, an employment-at-will employee may properly plan to compete with their employer, and they may take active steps while they are still their employer’s servant.¹⁴⁴ Like regular or contract-based employees, an employment-at-will employee has no general duty to disclose their plans to their employer.¹⁴⁵ In fact, the employment-at-will fiduciary may secretly plan a future enterprise with other at-will or regular employees without violating their fiduciary duty.¹⁴⁶ To summarize, an employee’s fiduciary obligation is not complicated. More or less, all employees form a fiduciary relationship with their employers, they have a fiduciary duty to protect the employers’ interests, and they must avoid being their employers’ adversaries.¹⁴⁷

138. See *Abetter Trucking Co. v. Arizpe*, 113 S.W.3d 503, 510 (Tex. App.—Houston [1st Dist.] 2003, no pet.).

139. *Daniel*, 190 S.W.3d at 185.

140. See *Bray v. Squires*, 702 S.W.2d 266, 270 (Tex. App.—Houston [1st Dist.] 1985, no writ); *Daniel*, 190 S.W.3d at 185; *Electro-Craft Corp. v. Controlled Motion, Inc.*, 332 N.W.2d 890, 903 (Minn. 1983) (concluding that an employee’s misappropriating his employer’s secret violated the employee’s duty of confidentiality); *Sanitary Farm Dairies, Inc. v. Wolf*, 112 N.W.2d 42, 48 (Minn. 1961) (finding that the employee’s soliciting an employer’s customers before leaving his employment breached employee’s duty of loyalty); *Hlubeck v. Beeler*, 9 N.W.2d 252, 254 (Minn. 1943) (concluding that an employee’s embezzling employer’s fund was a breach of the employee’s duty to serve the employer “faithfully and honestly”); *St. Cloud Aviation, Inc. v. Hubbell*, 356 N.W.2d 749, 751 (Minn. App. 1984) (concluding that an employee’s referring a customer to the employer’s competitor was a breach of the employee’s fiduciary duty).

141. See *Johnson v. Brewer & Pritchard, P.C.*, 73 S.W.3d 193, 200 (Tex. 2002) (embracing the proposition that an employee must perform primarily for the benefit of an employer in matters connected with the agency if a fiduciary relationship of agency exists between the employee and employer).

142. See *Bray*, 702 S.W.2d at 270.

143. *Id.*

144. See *Augat, Inc. v. Aegis, Inc.*, 565 N.E.2d 415, 419 (Mass. 1991).

145. *Id.*

146. *Id.*

147. See *State by McClure v. Sports & Health Club, Inc.*, 370 N.W.2d 844, 858 (Minn. 1985) (citing Restatement (Second) Agency §§ 1, 2, 13 (1957)).

The final discussion in this part highlights executors and administrators' fiduciary duties. Put simply, an executor of an estate is a fiduciary for the estate's beneficiaries.¹⁴⁸ Moreover, the relationship between an executor and the estate's beneficiaries creates a fiduciary duty as a matter of law.¹⁴⁹ Therefore, as a fiduciary, the executor has a duty to protect the beneficiaries' interest and to do so with candor.¹⁵⁰ More specifically, under Texas's law, executors have exclusive management rights; but, executors also owe estates' beneficiaries the highest duties of good faith, fidelity, loyalty, fairness, and prudence.¹⁵¹ Other community property and separate property states also have embraced these general principles.¹⁵²

Additionally, executors and administrators have a duty to fully disclose all material information that might affect the interests of the estate's beneficiaries.¹⁵³ In fact, an executor's administration of a decedent's estate must conform to the same high fiduciary duties and standards that govern the conduct of trustees.¹⁵⁴ That an estate's executor must conform to a higher fiduciary standard should generate little surprise. An independent or a court-ordered executor is a personal representative who "stands in [a decedent's] shoes."¹⁵⁵ Thus, any strained relations

148. See *Montgomery v. Kennedy*, 669 S.W.2d 309, 313 (Tex. 1984).

149. See *Huie v. DeShazo*, 922 S.W.2d 920, 923 (Tex. 1996).

150. See *Welder v. Green*, 985 S.W.2d 170, 175 (Tex. App.—Corpus Christi 1998, pet. denied); *Hawthorne v. Guenther*, 917 S.W.2d 924, 934 (Tex. App.—Beaumont 1996, writ denied).

151. See *Humane Soc'y of Austin & Travis County v. Austin Nat'l Bank*, 531 S.W.2d 574, 577 (Tex. 1975).

152. For community property states see, e.g., *In re Sanders*, 710 P.2d 232, 237 (1985) (declaring that an executor is a fiduciary, an executor owes an estate's beneficiaries a duty to act with the utmost good faith, and an executor must refrain from taking unfair advantage of the beneficiaries); *In re Larson*, 694 P.2d 1051, 1054 (Wash. 1985) (embracing the principle that "[t]he personal representative stands in a fiduciary relationship to those beneficially interested in the estate"); *McKeigue v. Chicago & N. W. R. Co.*, 110 N.W. 384, 385 (1907) (concluding that executors, in all essential respects, are held to the standard of a trustee).

For separate property states see, e.g., *Mankert v. Elmatco Products, Inc.*, 84 Conn. App. 456, 460 (2004) ("The executor of an estate has a fiduciary duty to its creditors . . ."); *In re McCool*, 553 A.2d 761, 765 (N.H. 1988) (concluding that an executor's fiduciary duty requires the executor to handle an estate "with that degree of prudence and diligence that a [person] of ordinary judgment would bestow on his [or her] own affairs of like nature."); *In re Pirie*, 492 N.E.2d 884, 889 (Ill. App. 1986) (reiterating that an executor of an estate has "a fiduciary duty to act with the highest degree of fidelity and utmost good faith in handling estate assets.").

153. See *Chien v. Chen*, 759 S.W.2d 484, 495 (Tex. App.—Austin 1988, no writ).

154. See *Austin Nat'l Bank*, 531 S.W.2d at 577; *Evans v. First Nat'l Bank of Bellville*, 946 S.W.2d 367, 379 (Tex. App.—Houston [14th Dist.] 1997, writ denied); and *Ertel v. O'Brien*, 852 S.W.2d 17, 20 (Tex. App.—Waco 1993, writ denied; see also *Slay v. Burnett Trust*, 143 Tex. 621, 187 S.W.2d 377, 388 (1945) (concluding that a trustee's duty of loyalty prohibits him from using his status to serve his interest rather than the interests of his trust and from allowing his interests to conflict with his obligations as a trustee).

155. See *Belt v. Oppenheimer, Blend, Harrison & Tate, Inc.*, 192 S.W.3d 780, 787 (Tex. 2006); see also *Eastland v. Eastland*, 273 S.W.3d 815, 821 (Tex. App.—Houston [14th Dist.] 2008) ("The primary distinction between an independent administration and a dependent administration is the level of judicial supervision over . . . the executor's power. Executors in a dependent administration and other personal

between executors and estate's beneficiaries do not lessen executors' fiduciary duty to disclose fully and protect the beneficiaries' interests.¹⁵⁶

Arguably, from an insurance law perspective, it is commonsensical for estate executors to have a higher fiduciary duty to protect and settle an estate, and to protect beneficiaries' interests.¹⁵⁷ To illustrate the point, consider, Sections 234(b)(4) and (5) in the Texas Probate Code.¹⁵⁸ Those sections outline the general powers of independent executors and administrators.¹⁵⁹ In pertinent part, the sections read: "The personal representative of the estate of any person may. . . [i]nsure the estate against liability in appropriate cases . . . [and] [i]nsure property of the estate against fire, theft, and other hazards."¹⁶⁰ Unquestionably, if executors of estates breach their fiduciary duty and forget to insure beneficiaries' property interests and various perils destroy those interests, the beneficiaries' financial losses can be substantial.¹⁶¹ Therefore, requiring executors to conform to the highest duties of good faith and prudence is warranted.

B. Spousal Fiduciary Obligations

1. General Spousal Obligations in Community and Separate Property States

Generally, in both community and separate property states, "[a] fiduciary duty exists between spouses"; and it does not terminate until the marriage dissolves.¹⁶² California's general rule is an excellent representation of spousal-fiduciary rules across all states:

representatives can perform only a limited number of transactions without seeking a court's permission, such as paying taxes, voting stocks, insuring property, and releasing liens upon full payment. . . . Transactions such as the purchase or exchange of property, the compounding of debts due to the estate, or the compromise or settlement of estate claims in dispute or litigation typically require the executor in a dependent administration to submit a written application to the court and receive a court order granting authority to enter into the transaction. . . . Independent executors, in contrast, can enter into any transactions deemed necessary for the good of the estate without requesting court authority after (1) the order appointing the independent executor has been signed by the court; and (2) the inventory, appraisal, and list of claims of the estate has been filed by the independent executor and approved by the court."); TEX. PROB. CODE ANN. § 234(b) (Vernon 2008).

156. See *Montgomery v. Kennedy*, 669 S.W.2d 309, 313 (Tex. 1984).

157. See *Coulter v. CIGNA Pro. & Cas. Co's.*, 934 F. Supp. 1101, 1104-05 (N.D. Iowa 1996).

158. § 234(b)(4)-(5).

159. *Id.*

160. *Id.*

161. Cf. *Coulter*, 934 F. Supp. at 1104-05. In the underlying first-party lawsuit, the estate beneficiaries filed an insurance-related, breach of fiduciary action against the executor. *Id.* Allegedly, the estate and the estate's beneficiaries "lost much of the value of the estate of James Kaster and interest income" because the executor "fail[ed] to timely sell Kaster Insurance, in harmony with the intent of the testator, James Kaster, [and failed to] obtain court approval for the continued operation of Kaster Insurance"). *Id.*

162. See, e.g., *Toles v. Toles*, 113 S.W.3d 899, 916 (Tex. App.—Dallas 2003, no pet.); *Eltzroth and Eltzroth*, 679 P.2d 1369, 1372 (Or. App. 1984) ("Oregon courts have long recognized that a husband and

[In] transactions between themselves, a husband and wife are subject to the general rules governing fiduciary relationships which control the actions of persons occupying confidential relations with each other. This confidential relationship imposes a duty of the highest good faith and fair dealing on each spouse, and neither shall take any unfair advantage of the other. This confidential relationship is a fiduciary relationship subject to the same rights and duties of nonmarital business partners.¹⁶³

Spouses occupy a “position of peculiar confidence” for the benefit of each other, and they are “held to the highest standards of good faith and fair dealing.”¹⁶⁴ Consequently, state courts and statutes impose a considerable number of mutual obligations on them.¹⁶⁵ In particular, those obligations may and often do involve the following: child custody and visitation, child support, spousal support, support arrearages, division of community property, separate property, securing life, health and homeowners’ insurance, taxes and debts.¹⁶⁶

2. Additional Spousal Fiduciary Obligations in Community Property States

Depending on one’s source of information or analysis, there are at least ten community property states: Alaska, Arizona, California, Idaho, Louisiana, New Mexico, Nevada, Texas, Washington, and Wisconsin.¹⁶⁷ A

wife do not deal at arms’ length and have imposed a fiduciary duty of the highest degree in transactions between them. . . . Because the fiduciary duty [between husband and wife] is imposed as a result of the confidential relationship between the parties, it continues while the parties contemplate divorce as long as the confidential relationship remains intact, and the parties are not dealing at arms’ length through separate agents or attorneys.”); *Knox v. Knox*, 25 N.W.2d 225, 229 (Minn. 1946) (holding that a relationship between husband and wife is confidential in its nature and fiduciary in its character); *Seals v. Seals*, 590 P.2d 1301, 1304 (Wash. App. 1979) (reaffirming that before and during marriage, parties have a fiduciary duty). See *Grossnickle v. Grossnickle*, 935 S.W.2d 830, 846 (Tex. App.—Texarkana 1996, writ denied) (noting that the fiduciary duty between husband and wife terminates on divorce); *Seals*, 590 P.2d at 1304 (reaffirming that before and during marriage, parties have a fiduciary duty to one another in agreements which have been reached between them and that “[a] fiduciary duty does not cease upon contemplation of the dissolution of a marriage.”).

163. See *In re Marriage of Ford*, Nos. A114997, A115857, 2008 WL 1801535, at *10 (Cal. App. 1 Dist.).

164. See *Kinzbach Tool Co. v. Corbett-Wallace Corp.*, 160 S.W.2d 509, 512 (Tex. 1942); see also *Krapf v. Krapf*, 786 N.E.2d 318, 323 (Mass. 2003) (concluding that “[p]arties to a separation agreement stand as fiduciaries to each other, and will be held to the highest standards of good faith and fair dealing in the performance of their contractual obligations”).

165. CAL. FAM. CODE § 721(b) (West 2003) (stating that the “confidential relationship [of spouses] imposes a duty of the highest good faith and fair dealing on each spouse, and neither shall take any unfair advantage of the other”).

166. See *In re Marriage of Ross*, 2007 WL 1632365, at *3 (Cal. App. 4 Dist.).

167. Alaska has enacted an “elective” community property statute. See ALASKA STAT. 34.77.090 (2009).

(a) A community property agreement must be contained in a written document signed by both spouses and classify some or all of the property of the spouses as community property. It is enforceable without consideration.

(b) A community property agreement must contain the following language in capital letters at

the beginning of the agreement:

THE CONSEQUENCES OF THIS AGREEMENT MAY BE VERY EXTENSIVE, INCLUDING, BUT NOT LIMITED TO, YOUR RIGHTS WITH RESPECT TO CREDITORS AND OTHER THIRD-PARTIES, AND YOUR RIGHTS WITH YOUR SPOUSE BOTH DURING THE COURSE OF YOUR MARRIAGE AND AT THE TIME OF A DIVORCE. ACCORDINGLY, THIS AGREEMENT SHOULD ONLY BE SIGNED AFTER CAREFUL CONSIDERATION. IF YOU HAVE ANY QUESTIONS ABOUT THIS AGREEMENT, YOU SHOULD SEEK COMPETENT ADVICE.

Id.

All property acquired by either husband or wife during the marriage is the community property of the husband and wife except for property that is: 1. Acquired by gift, devise or descent[;] 2. Acquired after service of a petition for dissolution of marriage, legal separation or annulment if the petition results in a decree of dissolution of marriage, legal separation or annulment.

ARIZ. REV. STAT. ANN. § 25-211(A) (2009).

“Except as otherwise provided by statute, all property, real or personal, wherever situated, acquired by a married person during the marriage while domiciled in this state is community property.” CAL. FAM. CODE § 760 (West 1994).

All other property acquired after marriage by either husband or wife is community property. The income, including the rents, issues and profits, of all property, separate or community, is community property unless the conveyance by which it is acquired provides or both spouses, by written agreement specifically so providing, declare that all or specifically designated property and the income, including the rents, issues and profits, from all or the specifically designated property shall be the separate property of one of the spouses or the income, including the rents, issues and profits, from all or specifically designated separate property be the separate property of the spouse to whom the property belongs. Such property shall be subject to the management of the spouse owning the property and shall not be liable for the debts of the other member of the community.

IDAHO CODE ANN. § 32-906(1) (1980).

The community property comprises: property acquired during the existence of the legal regime through the effort, skill, or industry of either spouse; property acquired with community things or with community and separate things, unless classified as separate property under Article 2341; property donated to the spouses jointly; natural and civil fruits of community property; damages awarded for loss or injury to a thing belonging to the community; and all other property not classified by law as separate property.

LA. CIV. CODE ANN. Art. 2338 (2009).

A. Property acquired during marriage by either husband or wife, or both, is presumed to be community property.

B. Property or any interest therein acquired during marriage by a woman by an instrument in writing, in her name alone, or in her name and the name of another person not her husband, is presumed to be the separate property of the married woman if the instrument in writing was delivered and accepted prior to July 1, 1973. The date of execution or, in the absence of a date of execution, the date of acknowledgment, is presumed to be the date upon which delivery and acceptance occurred.

N.M. STAT. ANN. § 40-3-12 (West 2009).

All property, other than that stated in NRS 123.130, acquired after marriage by either husband or wife, or both, is community property unless otherwise provided by:

1. An agreement in writing between the spouses, which is effective only as between them.
2. A decree of separate maintenance issued by a court of competent jurisdiction.
3. NRS 123.190.
4. A decree issued or agreement in writing entered pursuant to NRS 123.259.

NEV. REV. STAT. § 123.220 (2009).

See Wilson v. Wilson, 201 S.W.2d 226, 227 (Tex. 1947) (reaffirming the presumption that property acquired during marriage is community property).

(a) Property possessed by either spouse during or on dissolution of marriage is presumed to be community property.

careful reading of those states' statutes reveals that the respective legislatures have codified "mandatory" or "elective" community property rules.¹⁶⁸ In addition, a few community property states have enacted so-called "quasi-community property" statutes.¹⁶⁹

Put simply, these latter statutes govern the division of property acquired while spouses were living in foreign jurisdictions.¹⁷⁰ State courts apply forum law to determine whether to divide property that was accumulated during a spouse's tenure or residence in another state or country.¹⁷¹ Consider Texas's quasi-community property statute, which reads in relevant part:

[T]he court shall order a division of the following real and personal property, wherever situated, in a manner that the court deems just and right . . . : (1) property that was acquired by either spouse while domiciled in another state and that would have been community property if the spouse who acquired the property had been domiciled in this state at the time of the acquisition; or (2) property that was acquired by either spouse in exchange for [such] real or personal property[.]¹⁷²

(b) The degree of proof necessary to establish that property is separate property is clear and convincing evidence.

TEX. FAM. CODE ANN. § 3.003 (Vernon 2006).

Property not acquired or owned, as prescribed in RCW 26.16.010 and 26.16.020, acquired after marriage or after registration of a state registered domestic partnership by either domestic partner or either husband or wife or both, is community property. Either spouse or either domestic partner, acting alone, may manage and control community property, with a like power of disposition as the acting spouse or domestic partner has over his or her separate property[.]

WASH. REV. CODE § 26.16.030 (2008).

(1) General. All property of spouses is marital property except that which is classified otherwise by this chapter and that which is described in sub. (8).

(2) Presumption. All property of spouses is presumed to be marital property.

(3) Spouse's interest in marital property. Each spouse has a present undivided one-half interest in each item of marital property, subject to all of the following:

(a) *Terminable interest in deferred employment benefit plan.* As provided in s. 766.62(5), the marital property interest of the nonemployee spouse in a deferred employment benefit plan or in assets in an individual retirement account that are traceable to the rollover of a deferred employment benefit plan terminates at the death of the nonemployee spouse if he or she predeceases the employee spouse

....
WIS. STAT. ANN. § 766.31 (West 2009).

168. See *Property Owned By the Decedent and Jointly Owned Property*, SP005 ALI-ABA 37, Aug. 20-22, 2008, at 1.

169. See ARIZ. REV. STAT. ANN. § 25-318; CAL. FAM. CODE §§ 63, 125, 2550; N.M. STAT. ANN. § 40-3-8; and TEX. FAM. CODE ANN. § 7.002.

170. ARIZ. REV. STAT. ANN. § 25-318; CAL. FAM. CODE §§ 63, 125, 2550; N.M. STAT. ANN. § 40-3-8; and TEX. FAM. CODE ANN. § 7.002.

171. ARIZ. REV. STAT. ANN. § 25-318; CAL. FAM. CODE §§ 63, 125, 2550; N.M. STAT. ANN. § 40-3-8; and TEX. FAM. CODE ANN. § 7.002.

172. TEX. FAM. CODE ANN. § 7.002(a) (Vernon 2007). A similar rule also applies to separate property. § 7.002(b).

California and New Mexico, however, apply their respective quasi-community property rules only if both spouses are domiciled in their respective states.¹⁷³

Obviously, spouses' property interests are more intertwined, or commingled, in community property states than in separate property states. Therefore, in community property states, spouses arguably have an even greater fiduciary duty not to destroy tangible marital property or waste the community's intangible assets. But one rule is exceedingly clear: If a spouse controls or manages community property, that spouse has a fiduciary duty to protect the community's assets for the benefit of the other spouse.¹⁷⁴ In fact, in California, a duty to protect community assets extends beyond the marriage.¹⁷⁵ One court declared: "The spouse who controls community property assets occupies a position of trust which is not terminated . . . after separation. 'It is the managing spouse's fiduciary duties to account . . . for the community property when the spouses are negotiating a property settlement agreement.'"¹⁷⁶

There is more: "Although a spouse has the right to dispose of community property under his or her control, he may not dispose of his spouse's interest in community funds if actual or constructive fraud exists."¹⁷⁷ Briefly explained, "fraud on the community" is a judge-made rule that evolved from the theory of constructive fraud.¹⁷⁸ Texas's courts are likely to apply the fraud on the community rule when a deviant spouse breaches a legal or an equitable duty, or violates spousal fiduciary obligations.¹⁷⁹

A presumption of constructive fraud arises when one spouse disposes of another spouse's interest in community property without the latter's knowledge or consent.¹⁸⁰ However, to prove constructive fraud, one only has to establish that an offender breached a legal or an equitable duty.¹⁸¹ That breach is fraudulent as a matter of law because the breach violates a

173. See generally *Yield Dynamics, Inc. v. Zavec*, No. H028146, 2005 WL 3485656, at *5 (Cal. Ct. App. 2005) (concluding that "a fundamental requirement before common law separate property of the non-debtor spouse will be treated as quasi-community property is the requirement that both spouses must have established a California domicile."); see also N.M. STAT. ANN. § 40-3-8.

174. See *Zieba v. Martin*, 928 S.W.2d 782, 789 (Tex. App.—Houston [14th Dist.] 1996, no writ) ("A fiduciary duty exists between a husband and a wife as to the community property controlled by each spouse.").

175. See *In re Marriage of Koppelman*, 159 Cal. App. 3d 627, 634 (1984).

176. *Id.*

177. *Greco v. Greco*, No. 04-07-00748, 2008 WL 4056328, at *5 (Tex. App.—San Antonio, 2008, no pet.); see *Loaiza v. Loaiza*, 130 S.W.3d 894, 900-01 (Tex. App.—Fort Worth 2004, no pet.); see also *Mazique v. Mazique*, 742 S.W.2d 805, 807-08 (Tex. App.—Houston [1st Dist.] 1987, no writ).

178. See *Zieba*, 928 S.W.2d at 789.

179. *Id.*

180. See *Jean v. Tyson-Jean*, 118 S.W.3d 1, 9 (Tex. App.—Houston [14th Dist.] 2003, pet. denied); see also *Mazique*, 742 S.W.2d at 808.

181. See *Jean*, 118 S.W.3d at 9.

fiduciary relationship.¹⁸² The victim does not have to prove that the offending party had the intent to defraud.¹⁸³ Similarly, a breach of one's fiduciary duty in a community property union is not fraud per se, but it can be fraud on the community.¹⁸⁴ For example, if a spouse wastes community assets, that conduct qualifies as fraud on the community.¹⁸⁵ The justification for the rule is not terribly complicated. Like actual fraud, fraud on the community also generates adverse financial and legal consequences for the innocent spouse.¹⁸⁶

Finally, courts in Texas may weigh a deviant spouse's waste of community assets when deciding to divide the community estate.¹⁸⁷ However, although a deviant spouse's fraud on the community may cause a court to divide the estate unequally, the innocent spouse's remedies in law are few.¹⁸⁸ Put simply, "there is no independent tort cause of action for wrongful disposition by a spouse of community assets."¹⁸⁹ Consequently, purchasing first-party insurance and insuring against the perils of a deviant spouse can be the next best alternative for innocent spouses in community property states. Securing indemnity insurance could also be the next best option for victimized innocent spouses, tenants in common or tenants by the entirety, in separate property states.¹⁹⁰

III. THE LEGAL DISTINCTION BETWEEN FIRST-PARTY AND THIRD-PARTY INSURANCE CONTRACTS

Deviant fiduciaries—partners, joint venturers, parents and children, employees, executors, officers and directors, mortgagors, and spouses—share two common characteristics: They often violate their fiduciary duties negligently or intentionally.¹⁹¹ In the course of violating their obligations,

182. *Id.*

183. *Id.*

184. *Id.*

185. *Id.*; see *Zieba v. Martin*, 928 S.W.2d 782, 789 (Tex. App.—Houston [14th Dist.] 1996, no writ).

186. *Id.*

187. See *Schlueter v. Schlueter*, 975 S.W.2d 584, 589 (Tex. 1998); *Harper v. Harper*, 8 S.W.3d 782, 783-84 (Tex. App.—Fort Worth 1999, pet. denied).

188. See *Schlueter*, 975 S.W.2d at 589; *Harper*, 8 S.W.3d at 783-84.

189. *Schlueter*, 975 S.W.2d at 589.

190. Cf. *Donnan v. Atl. Richfield*, 732 S.W.2d 715, 717 (Tex. App.—Corpus Christi 1987, writ denied) (declaring that no fiduciary or agency relationship exists between co-tenants or tenants in common).

191. See *Ashton v. Thompson*, 18 N.W. 918, 923 (Minn. 1884) (holding that a guardian stands in a fiduciary relation to his or her ward); see also *Thigpen v. Locke*, 363 S.W.2d 247, 257 (Tex. 1962) (embracing the principle that a parent owes a fiduciary duty to his child). But see *Ware v. Ware*, 161 P.3d 1188, 1194 (Alaska 2007) (adopting the principle that "[the presence] of a parent-child relationship does not necessarily create fiduciary duties"); *Ahlberg v. Bargo*, No. 040085705, 2009 WL 659309, at *5 (Conn. Super. 2009) (concluding that "[i]n the absence of additional factors, the mere relationship of parent and child is insufficient to establish a fiduciary relationship"); *In re Draper v. Bank of America, N.A.*, 205 P.3d 698, 707 (Kan. 2009) ("For purposes of constructive fraud, the mere relationship

deviant co-fiduciaries often destroy, reduce, or cloud their innocent co-parties' pecuniary interests in various forms of shared property—jointly owned, community, tenancy by the entirety, and tenancy in common properties.

Deviant fiduciaries also share another trait. In the course of intentionally or negligently violating their fiduciary obligations, deviant co-fiduciaries destroy or severely damage third-party victims' persons and property, both tangible and intangible property. When deviant fiduciaries injure third-parties, the innocent fiduciaries are often vicariously liable. For example, under the doctrine of respondeat superior, an employer is vicariously liable for the tortious acts of its employees when the employees act is within their scope of employment.¹⁹² Also, the fiduciaries in a joint venture share a community of interest in the venture.¹⁹³ They share profits, losses, and have a mutual right to control or direct the venture.¹⁹⁴ But more relevant, joint-venture fiduciaries may be jointly and severally liable for each other's deviant, negligent, or intentional acts.¹⁹⁵

As mentioned at the outset, property and casualty insurers sell an array of insurance services.¹⁹⁶ Arguably, most prudent fiduciaries purchase both first and third-party insurance because innocent fiduciaries can be victims of and vicariously liable for their deviant co-fiduciaries' negligence and/or intentional acts.¹⁹⁷ Again, there are significant legal distinctions between property and liability insurance, and between first and third-party insurance.¹⁹⁸ Those differences are discussed below.

A. First-party Insurance Contracts

Marine, fire, general property, life, health, disability, floater, automobile, and homeowners' insurance contracts are familiar forms of first-party, residential, and commercial insurance.¹⁹⁹ In fact, first-party

between parent and child or between spouses does not raise a presumption of a confidential and fiduciary relationship"); *Salvner v. Salvner*, 84 N.W.2d 871, 875-76 (Mich.1957); and *Hatton v. Turner*, 622 S.W.2d 450, 458-59 (Tex. Civ. App.—Tyler 1981, no writ) (concluding that poor health and evidence of trust may give rise to a confidential or fiduciary relationship between parent and child).

192. See *Baptist Mem'l Hosp. Sys. v. Sampson*, 969 S.W.2d 945, 947 (Tex. 1998); see also *St. Joseph Hosp. v. Wolff*, 94 S.W.3d 513, 537-38 (Tex. 2002) (concluding that the controlling factor is the employer's right to direct and control the details of the employee's work if there is uncertainty about whether the fiduciary was an "employer" for the purposes of vicarious liability).

193. See *Schlumberger Tech. Corp. v. Swanson*, 959 S.W.2d 171, 176 (Tex. 1997).

194. *Id.*

195. See *Battaglia v. Alexander*, 177 S.W.3d 893, 904 (Tex. 2005) (finding two professional associations providing anesthesia services to a hospital jointly and severally liable because they were engaged in joint venture).

196. See *supra* Part I.

197. See *supra* Part I.

198. See *Garvey v. State Farm Fire & Cas. Co.*, 770 P.2d 704, 705 (Cal. 1989).

199. See *Montrose Chem. Corp. v. Admiral Ins. Co.*, 913 P.2d 878, 886 (Cal. 1995) ("[A] first-party insurance policy provides coverage for loss or damage sustained directly by the insured (e.g., life,

insurance contracts define coverage in a manner that often confuses ordinary insurance consumers as well as seasoned judges.²⁰⁰ First, to be covered under a property insurance contract, an insured must establish that a certain enumerated peril(s) in the insurance contract is the “dominant efficient cause” or the “efficient proximate cause” of the insured’s loss.²⁰¹ If the insured cannot prove that connection, there is no coverage.²⁰² Thus, the insurer does not have to indemnify.²⁰³

Quite simply, perils are “fortuitous, active, physical forces such as lightning, wind, and explosion, which bring about [a] loss.”²⁰⁴ There are two types of first-party insurance: “all-risk coverage” and “specified-risk coverage.” An all-risk policy covers all risks except those specifically excluded.²⁰⁵ Conversely, under a specified-risk contract, an insurer must

disability, health, fire, theft and casualty insurance))).

200. See *Garvey*, 770 P.2d at 705.

In recent years, some courts have misinterpreted and misapplied our decisions In so doing, they have allowed coverage in first-party property damage cases . . . by inappropriately using the . . . concurrent causation approach as an alternative to . . . efficient proximate cause analysis. . . . Such reasoning ignores . . . the important distinction between property loss coverage under a first-party property policy and tort liability coverage under a third-party liability insurance policy.

Id.

201. See *Travelers Indem. Co. v. McKillip*, 469 S.W.2d 160, 162 (Tex. 1971) (reaffirming that “where a loss occurs under a standard fire, windstorm and extended coverage policy. . . , and such loss is contributed to by an excluded risk of the policy, the plaintiff may, nevertheless, recover if plaintiff proves that the dominant efficient cause of the loss is the covered risk.”); see also *Freedman v. State Farm Ins. Co.*, 93 Cal. Rptr. 3d 296, 300 (Cal. App. [2nd Dist.] 2009) (quoting *State Farm Fire & Cas. Co. v. Von Der Lieth*, 54 Cal. 3d 1123, 1131-32 (1991)) (“Under the efficient proximate cause doctrine, ‘[w]hen a loss is caused by a combination of a covered and specifically excluded risks, the loss is covered if the covered risk was the efficient proximate cause of the loss,’ but ‘the loss is not covered if the covered risk was only a remote cause of the loss, or the excluded risk was the efficient proximate, or predominate cause.’ . . . The efficient proximate cause of a loss is the ‘predominant’ or ‘most important’ cause of the loss.”).

202. See *Stroburg v. Ins. Co. of N. Am.*, 464 S.W.2d 827, 831 (Tex. 1971) (“[W]e have held that ‘proximate cause’ as applied in insurance cases has essentially the same meaning as that applied by our . . . courts in negligence cases, except that in the former the element of foreseeableness or anticipation of the injury as a probable result of the peril insured against is not required”); *Id.* (quoting *Fed. Life Ins. Co. v. Raley*, 109 S.W.2d 972, 974 (Tex. 1937)) (“[I]n cases where the insurance policy does not in express terms so provide . . . the insurer becomes liable for a loss unless the loss is proximately caused by the peril insured against Moreover . . . the term ‘proximate cause’ as applied in insurance cases has essentially the same meaning as that applied by our own courts in negligence cases, except that in the former the element of foreseeableness or anticipation of the injury as a probable result of the peril insured against is not required.”).

203. See *Montrose Chem. Corp. v. Admiral Ins. Co.*, 913 P.2d 878, 886 (Cal. 1995) (reaffirming that “[p]roperty insurance . . . is an agreement . . . in which the insurer agrees to indemnify the insured in the event that the insured property suffers a covered loss.”); *Newmont Mines Ltd. v. Hanover Ins. Co.*, 784 F.2d 127, 136 (2d Cir.1986) (stating that first-party property insurance policies “provide financial protection against damage to property”).

204. See *Garvey*, 770 P.2d at 710.

205. *Id.*; see *Murray v. State Farm Fire & Cas. Co.*, 509 S.E.2d 1, 7 (W. Va. 1998) (“Under an all-risk policy, recovery is allowed for all losses arising from any fortuitous cause, unless the policy contains an express provision excluding loss from coverage.”).

indemnify only if a listed peril caused the insured's property loss.²⁰⁶ Each type of insurance contract may cover residences or commercial establishments.²⁰⁷ Or alternatively, a single all-risk or specific-risk insurance contract may cover a variety of property interests simultaneously.

B. Third-party Insurance Contracts—Liability and Indemnity Insurance

Commercial general liability policies, directors' and officers' liability policies, errors and omissions liability agreements, various types of automobile policies, some homeowners' policies, professional malpractice policies, and multi-peril policies are examples of third-party insurance contracts.²⁰⁸ Under these contracts, insurers promise to pay judgments which the insureds become "legally obligated to pay as damages" after the insureds injure third-party victims' persons—"bodily injury"—or property.²⁰⁹

The Supreme Court of California presented an excellent discussion of the significant difference between third-party and first-party insurance.²¹⁰ The court wrote:

[T]he right to coverage in the third-party liability insurance context draws on traditional tort concepts of fault, proximate cause and duty. This liability analysis differs substantially from the coverage analysis in the property insurance context, which draws on the relationship between perils that are either covered or excluded in the contract. *In liability insurance, by insuring for personal liability, and agreeing to cover the insured for his own negligence, the insurer agrees to cover the insured for a broader spectrum of risks.*²¹¹

It is important to note that third-party insurance comes in two forms: Liability contracts and indemnity contracts.²¹² First, liability insurance contracts have certain general characteristics: (1) coverage provisions that outline the "named insureds" and the "risks insured against"; (2) a right-to-

206. *Opera Boats, Inc. v. La Reunion Francaise*, 893 F.2d 103, 105 (5th Cir.1990).

207. *See TAG 380, LLC v. ComMet 380, Inc.*, 890 N.E.2d 195, 199 (N.Y. 2008) ("Commercial property insurance is generally offered in either an all-risk policy or a named-perils policy. . . . 'Named-perils' covers only specifically enumerated risks, whereas an 'all-risk' agreement generally covers all risks of physical loss, except for those perils specifically excluded. Those losses caused by fraud or, in some cases, by a fortuitous and unforeseen event are likewise excluded."); *Ingersoll Milling Machine Co. v. M/V Bodena*, 829 F.2d 293, 307 (2d Cir. 1987) (commercial property insurance generally is offered in the form of either an all-risk policy or a named perils policy, and under an all-risk policy, losses caused by any fortuitous peril not specifically excluded under the policy will be covered.).

208. *See Montrose Chem. Corp.*, 913 P.2d at 886.

209. *Id.*

210. *Id.*

211. *Id.*

212. *See, e.g., LaBatt Co. v. Hartford Lloyd's Ins. Co.*, 776 S.W.2d 795, 798 (Tex. App.—Corpus Christi 1989, no pet.).

settle clause that gives the insurer the exclusive right to settle third-party claims and causes; (3) a duty-to-defend phrase that requires the insurer to secure competent legal representation for the insured and pay defense costs; (4) a duty-to-pay clause that describes the conditions under which the insurer will pay third-party claims; (5) an exclusion clause that outlines the risks that the insurer refuses to accept; and (6) a clause that excludes “intentional conduct,” refers to third-party injuries which are “expected or intended from the perspective of the insured.”²¹³ In a nutshell, liability insurance precludes insureds from having to use out-of-pocket money to compensate victims for the insureds’ tortious conduct.²¹⁴ Those out-of-pocket expenses arise when the insureds cause third-party bodily injuries, or when insureds damage or destroy third-party property.²¹⁵

On the other hand, indemnity insurance contracts require insurers “to indemnify or make whole the insured after he has sustained [an] actual loss, meaning after the insured has paid or been compelled to make a payment” to a third-party claimant.²¹⁶ Generally, those agreements do not require

213. See, e.g., *LaBatt Co.*, 776 S.W.2d at 798. The language of the commercial multiperil liability insurance contract reads:

The Company [Hartford] will pay on behalf of the insured [LaBatt] all sums which the insured shall become legally obligated to pay as damages because of bodily injury or property damage to which this insurance applies, caused by an occurrence and arising out of the ownership, maintenance or use of the insured premises and all operations necessary or incidental to the business of the named insured conducted at or from the insured premises and the Company shall have the right and duty to defend any suit against the insured seeking damages on account of such bodily injury or property damage, even if any of the allegations of the suit are groundless, false or fraudulent, and may make such investigation and settlement of any claim or suit as it deems expedient, but the Company shall not be obligated to pay any claim or judgment or to defend any suit after the applicable limit of the Company’s liability has been exhausted by payment of judgments or settlements.

Id. (emphasis added). The exclusion clause reads:

It is agreed that the insurance does not apply to bodily injury or property damage included within the Completed Operations Hazard or the Products Hazard. The term “products hazard” is defined on a different page of the policy as follows: “products hazard” includes bodily injury and property damage arising out of the named insured’s products or reliance upon a representation or warranty made at any time with respect thereto, but only if the bodily injury or property damage occurs away from premises owned by or rented to the named insured and after physical possession of such products has been relinquished to others[.]

Id. (emphasis added); see, e.g., *Westchester Fire Ins. Co. v. Admiral Ins. Co.*, 152 S.W.3d 172, 181 (Tex. App.—Fort Worth 2004, pet. denied) (“The commercial general liability (CGL) portion of Admiral’s policy covered ‘those sums which the Insured shall become legally obligated to pay as damages because of . . . bodily injury . . . caused by an occurrence.’ The policy defined ‘occurrence’ as ‘an accident . . . which results in bodily injury . . . neither expected nor intended from the standpoint of the Insured.’”) (emphasis added).

214. See *Universal Underwriters Group v. Heibel*, 901 A.2d 398, 403 (N.J. Super. Ct App. Div. 2006).

215. *Id.*

216. See *Fight Against Coercive Tactics Network, Inc. v. Coregis Ins. Co.*, 926 F. Supp. 1426, 1432-33 (D. Colo. 1996); see also *Little v. MGIC Indem. Corp.*, 836 F.2d 789, 793 (3rd Cir. 1987) (“In general, under an indemnity policy the insurer is obligated only to reimburse the insured for covered loss that the insured himself has already paid.”).

insurers to provide a legal defense or to settle third-party claims.²¹⁷ Insurers sell a variety of indemnity insurance contracts, professional indemnity plans, hospital indemnity insurance, workers compensation indemnity plans, excess employers' indemnity policy, and industrial indemnity insurance. Of course, directors' and officers' policies (D&O) appear to be the most common and well known indemnity insurance contracts.

IV. THE PURPOSE AND SCOPE OF FEDERAL AND STATE DECLARATORY JUDGMENTS ACTS

As discussed carefully in succeeding sections, first-party insurers frequently refuse to indemnify innocent insureds when deviant co-insured fiduciaries waste, deplete, reduce, or destroy jointly owned or community property interests.²¹⁸ Likewise, liability insurers often refuse to settle third-party claims on behalf of innocent co-insureds when deviant co-insured fiduciaries injure third-parties' persons and destroy or diminish third-parties' property interests.²¹⁹ Liability insurers also refuse to indemnify innocent co-insureds after the latter use out-of-pocket funds to defend deviant co-fiduciaries against third-party lawsuits, or to settle those claims against deviant co-insured fiduciaries.²²⁰

Quite frequently, both property and liability insurers follow a standard industry-wide legal protocol. First, insurers apply a very effective procedure that can defeat innocent co-insured fiduciaries' efforts from the start: Insurers assert that the fiduciaries did not file a notice of loss "as soon as practicable" which prejudiced the insurers' interests.²²¹ Of course, if the co-insureds filed a timely notice and it does not prejudice the interests of the insurers, the latter may deny a first or third-party claim on other grounds.²²²

217. See, e.g., *Coregis Ins. Co.*, 926 F. Supp. at 1430-31.

218. See *infra* Part V.

219. See *infra* Part VI.A.

220. See *infra* Part VI.B.

221. See *PAJ, Inc. v. Hanover Ins. Co.*, 243 S.W.3d 630, 636-37 (Tex. 2008) (holding that "an insured's failure to timely notify its insurer of a claim or suit does not defeat coverage if the insurer was not prejudiced by the delay"); *Prodigy Comm'ns Corp. v. Agric. Excess & Surplus Ins. Co.*, 288 S.W.3d 374, 382 (Tex. 2009) ("In a claims-made policy, when an insured gives notice of a claim within the policy period or other specified reporting period, the insurer must show that the insured's noncompliance with the policy's 'as soon as practicable' notice provision prejudiced the insurer before it may deny coverage."). But see *Fin. Indus. Corp. v. XL Specialty Ins. Co.*, 285 S.W.3d 877, 878 (Tex. 2009) (declaring that "under Texas law, an insurer need not demonstrate prejudice from late notice to avoid coverage on a claims-made policy"). See also *F.D.I.C. v. Mijalis*, 15 F.3d 1314, 1330 (5th Cir.1994) (noting that "[t]he notice requirements in claims made policies allow the insurer to 'close its books' on a policy at its expiration and thus to 'attain a level of predictability unattainable under standard occurrence policies.'" (quoting *Burns v. Int'l Ins. Co.*, 709 F. Supp. 187, 191 (N.D. Cal. 1989), *aff'd*, 929 F.2d 1422 (9th Cir.1991))).

222. See *Alaska Nat. Ins. Co. v. Bryan*, 104 P.3d 1, 9 (Wash. Ct. App. 2004).

After the insurers deny those claims, the companies send reservation of rights letters to innocent or deviant co-insured fiduciaries.²²³ Generally, those letters state that although the insurers believe they are not liable, they will conduct a thorough investigation of the first or third-party claims to be sure.²²⁴ The letters may also state that the insurers will attempt to settle a claim or indemnify insureds while reserving the insurers' right to challenge the co-insured fiduciaries' alleged rights under the insurance contracts.²²⁵

How do insurers challenge the co-insured fiduciaries? Put simply, the liability and property insurers file declaratory judgment actions in federal or state court.²²⁶ The insurers petition those courts to declare insurers and co-insured fiduciaries' respective rights and responsibilities under first and third-party insurance contracts.²²⁷ Below, a brief discussion highlights the purpose and scope of a declaratory judgment trial.²²⁸ In addition, state and federal courts employ a variety of equitable doctrines to construct and interpret rights and obligations under insurance contracts.²²⁹ Therefore, a brief discussion of those doctrines also appears in this part.

A. *Uniform Declaratory Judgments Act of 1922 and Federal Declaratory Judgments Act of 1934*

The National Conference of Commissioners on Uniform State Laws and the American Bar Association proposed the Uniform Declaratory Judgments Act.²³⁰ The Act's stated purposes are: (1) to give state courts the "power to declare rights, status, and other legal relations," (2) to unify the laws of the various states, and (3) "to harmonize . . . federal laws and

223. See *id.* ("The purpose of a reservation of rights letter is not to change the contractual relationship of the parties, but rather it is to identify the insurer's position regarding coverage and serves to protect the parties by providing a conditional defense to the insured and protecting the insurer from a bad faith claim if coverage is due."); see also *Katerndahl v. State Farm Fire & Cas. Co.*, 961 S.W.2d 518, 521 (Tex. App.—San Antonio 1997, pet. ref'd) ("When an insurer is faced with the dilemma of whether to defend or refuse to defend a proffered claim, it has four options: (1) completely decline to assume the insured's defense; (2) seek a declaratory judgment as to its obligations and rights; (3) defend under a reservation of rights or a non-waiver agreement; and (4) assume the insured's unqualified defense." Once a defense is taken under a valid reservation of rights, the insurer may withdraw the defense when it becomes clear that there is no coverage under the applicable policy. The purpose of the reservation of rights letter is to permit the insurer to provide a defense for its insured while it investigates questionable coverage issues.") (quoting *Farmers Tex. County Mut. Ins. Co. v. Wilkinson*, 601 S.W.2d 520, 522 (Tex. Civ. App.—Austin 1980, writ ref'd n.r.e.)).

224. See *Alaska Nat. Ins. Co.*, 104 P.3d at 9.

225. *Id.*

226. See *infra* Part IV.A.

227. See *infra* Part IV.A.

228. See *infra* Part IV.A.

229. See *infra* Part IV.A.

230. See Willy E. Rice, *Insurance Contracts and Judicial Discord Over Whether Liability Insurers Must Defend Insureds' Allegedly Intentional and Immoral Conduct: A Historical and Empirical Review of Federal and State Courts' Declaratory Judgments 1900-1997*, 47 AM. U. L. REV. 1131, 1142 (June 1998).

regulations on the subject of declaratory judgment[.]”²³¹ “Any person interested under a . . . written contract . . . or whose rights, status or other legal relations are affected by a . . . contract[,] may [petition a court to determine] any question of construction or validity arising under the . . . contract . . . and obtain a declaration of rights, status or other legal relations”²³² Nearly all states adopted the Uniform Declaratory Judgments Act of 1922, and two states enacted substantially equivalent versions.²³³

The Federal Declaratory Judgments Act was enacted in 1934.²³⁴ It reads in relevant part:

In a case of actual controversy within its jurisdiction . . . any court in the United States . . . may declare the rights and other legal relations of any interested party seeking such declaration. . . . Any such declaration shall have the force and effect of a final judgment or decree and shall be reviewable as such.²³⁵

231. Uniform Declaratory Judgments Act §§ 1, 15.

232. Uniform Declaratory Judgments Act § 2.

233. See ALA. CODE §§ 6-6-220 to 6-6-232 (1935); ARIZ. REV. STAT. ANN. §§ 12-1831 to 12-1846 (1927); ARK. CODE ANN. §§ 16-111-101 to 16-111-111 (1953); COLO. REV. STAT. ANN. §§ 13-51-101 to 13-51-115 (West 1923); DEL. CODE ANN. tit. 10, §§ 6501 to 6513 (1981); FLA. STAT. ANN. §§ 86.011 to 86.111 (WEST 1943); GA. CODE ANN. §§ 9-4-1 to 9-4-10 (1945); IDAHO CODE. §§ 10-1201 to 10-1217 (1933); ILL. ANN. STAT. CH. 735, para. 5/2-701 (SMITH-HURD 1945); IND. CODE ANN. §§ 34-4-10-1 to 34-4-10-16 (WEST 1927); IOWA CODE ANN. §§ 261 to 269 (WEST 1943); KAN. STAT. ANN. § 202 (1993); LA. CIV. CODE PROC. ANN. arts. 1871 to 1883 (WEST 1948); ME. REV. STAT. ANN. tit. 33, §§ 5951 to 5963 (WEST 1941); MD. CTS. & JUD. PROC. CODE ANN. §§ 3-401 to 3-415 (1944); MASS. GEN. LAWS ANN. ch. 231A, §§ 1 to 9 (WEST 1945); MINN. STAT. ANN. §§ 555.01 to 555.16 (1933); MO. ANN. STAT. §§ 527.010 to 527.140 (VERNON 1935); MONT. CODE ANN. §§ 27-8-101 to 27-8-313 (1935); NEB. REV. STAT. §§ 25-21,149 to 25-21,164 (1929); NEV. REV. STAT. §§ 30.010 to 30.160 (1929); N.J. STAT. ANN. §§ 2A :16-50 to 2A:16-62 (WEST 1924); N. M. STAT. ANN. §§ 44-6-1 to 44-6-15 (MICHIE 1975); N.C. GEN. STAT., §§ 1-253 to 1-267 (19331); N.D. CENT. CODE §§ 32-23-01 to 32-23-13 (1923); OHIO REV. CODE ANN §§ 2721.01 to 2721.15 (ANDERSON 1933); OKLA. STAT. ANN. tit. 12, §§ 1651 to 1657 (1961); OR. REV. STAT. §§ 28.010 to 28.160 (1927); PA. CONS. STAT. ANN. tit. 42, §§ 7531 to 7541 (1923); P.R. LAWS ANN. tit. 32, § 59 (1931); R. I. GEN. LAWS §§ 9-30-1 to 9-30-16 (1959); S.C. CODE ANN. §§ 15-53-10 to 15-53-140 (LAW. CO-OP 1948); S.D. CODIFIED LAWS ANN. §§ 21-24-1 to 21-24-16 (1925); TENN. CODE ANN. §§ 29-14-101 to 29-14-113 (WEST 1923); TEX. CIV. PRAC. & REM. CODE ANN. §§ 37.001 to 37.011 (WEST 1943); UTAH CODE ANN. §§ 78-33-1 to 78-33-13 (1951); VT. STAT. ANN. tit. 12 §§ 4711 to 4725 (1931); V.I. CODE. tit. 5, §§ 1261 to 1272 (1957); VA. CODE ANN. §§ 8.01-184 to 8.01-191 (MICHIE 1922); WASH. REV. CODE ANN. §§ 7.24.010 to 7.24.144 (WEST 1935); W. VA. CODE §§ 55-13-1 to 55-13-16 (1941); WIS. STAT. ANN. § 806.04 (WEST 1927); and, WYO. STAT. §§ 1-37-101 to 1-37-115 (1923).

Although some jurisdictions have not adopted the Uniform Declaratory Judgments Act of 1922, parties in those states may commence declaratory judgment actions under local laws. See Alaska—A.S. 22.10.020(g); California—Local Ch. I, Civ. Rule 57; Connecticut—C.G.S.A. § 52-29; Hawaii—H.R.S. Ch. 632; Kansas—K.S.A. 60-257; Kentucky—K.R.S. § 418.040; Mississippi—M.R.C.P. Rule 57; New Hampshire—N.H. REV. STAT. § 491:22 and New York—McKinney’s CPLR § 3001.

234. 28 U.S.C. § 2201 (2009).

235. § 2001(a).

Like state court justices, federal judges have a considerable amount of discretion under the federal act and must carefully consider an array of variables before awarding or denying a declaratory judgment.²³⁶ For example, federal judges must weigh the following: (1) whether a declaratory judgment would settle a dispute; (2) whether a declaration would clarify legal relations; (3) whether the respective litigants are using a declaratory judgment suit primarily for “procedural fencing”; (4) whether a declaratory action would increase friction between federal and state courts; and (5) whether a more effective legal remedy exists.²³⁷

Again, like their counterparts who hear and resolve controversies in state courts, federal district courts have a lot of discretion to grant or deny declaratory relief under contracts generally, and under first and third-party insurance contracts in particular.²³⁸ Federal appellate courts, however, may not review those declarations unless evidence establishes some measurable level of judicial abuse.²³⁹ Without doubt, federal judges may abuse their discretion in numerous ways.²⁴⁰ However, to decrease the likelihood of abusing their power when litigants petition for declaratory relief, justices should consider whether a state court occupies a superior position to resolve a particular controversy between parties in light of the “scope [and nature] of [a] pending state court proceeding.”²⁴¹ If a pending state court proceeding is a better forum to settle the issues, the district court should dismiss the federal action because “it would be uneconomical as well as vexatious” for the federal court to try the declaratory judgment action.²⁴²

236. See *Rivet v. State Farm Mut. Auto. Ins. Co.*, 316 Fed. Appx. 440, 448-49 (6th Cir. 2009) (citing *Grand Trunk W. R.R. Co. v. Consol. Rail Corp.*, 746 F.2d 323, 326 (6th Cir.1984)); see also *St. Paul Ins. Co. v. Trejo*, 39 F.3d 585, 590-91 (5th Cir. 1994) (Some additional relevant factors are: “1) whether there is pending state action in which all matters in controversy may be fully litigated, 2) whether plaintiff filed suit in anticipation of lawsuit filed by defendant, 3) whether plaintiff engaged in forum shopping in bringing the suit, 4) whether possible inequities in allowing declaratory plaintiff to gain precedence in time or to change forums exist, 5) whether the federal court is a convenient forum for parties and witnesses, and 6) whether retaining the lawsuit in federal court would serve the purposes of judicial economy,” and 7) “whether the federal court is being called on to construe a state judicial decree involving the same parties and entered by the court before whom the parallel state suit between the same parties is pending.”).

237. See *Rivet*, 316 Fed. Appx. at 448-49.

238. See, e.g., *Nat’l Council on Comp. Ins. v. Paradis*, No. C.A. 92-6230, 1994 WL 930908, at *9 (R.I. Super. 1994) (“Section 9-30-11 in the Uniform Declaratory Judgments Act gives ‘broad discretion’ to this Court to decline to render a declaration of rights as requested by the plaintiff.” (citing *Fireman’s Fund Ins. Co. v. Burman, Inc.*, 120 R.I. 841, 845 (1978)); *Missouri Prop. Ins. Placement Facility v. McRoberts*, 598 S.W.2d 146, 148 (Mo. Ct. App. 1978) (concluding that trial courts have wide discretion to administer the Uniform Declaratory Judgments Act to provide relief from uncertainty and to serve other purposes for which the Act was intended).

239. See, e.g., *Huntsville Util. Dist. of Scott County, Tenn. v. Gen. Trust Co.*, 839 S.W.2d 397, 400 (Tenn. Ct. App. 1992) (holding that trial court’s declaratory judgment should not be disturbed on appeal unless the trial court’s declaration was arbitrary).

240. See *Nat’l Council on Comp. Ins.*, 1994 WL 930908, at *9.

241. Cf. *Brillhart v. Excess Ins. Co.*, 316 U.S. 491, 495 (1942).

242. *Id.*

B. Equitable and Legal Doctrines for Constructing and Interpreting First and Third-party Insurance Agreements

One purpose of this article is to present a plausible explanation of federal and state courts' numerous splits over whether property and liability insurers have a duty to indemnify innocent co-insured fiduciaries.²⁴³ Arguably, there should be very few, if any, conflicting declarations because nearly every state supreme court embraces and applies the same five equitable doctrines to interpret first- and third-party insurance contracts.²⁴⁴ More specifically, the highest courts in the overwhelming majority of community property states have adopted the adhesion doctrine, the doctrine of ambiguity, the plain-meaning rule, the doctrine of reasonable expectations, and traditional rules of contract construction and interpretation.²⁴⁵ And, barring an extremely few supreme court decisions in

243. See cases *infra* note 245.

244. See cases *infra* note 245.

245. See **Alaska**—*West v. Umialik Ins. Co.*, 8 P.3d 1135, 1138 (Alaska 2000) (concluding that insurance policies are contracts of adhesion); *State Farm Mut. Auto. Ins. Co. v. Lawrence*, 26 P.3d 1074, 1080 (Alaska 2001) (“We interpret ambiguities in insurance contracts in favor of the insured”); *Williams v. Crawford*, 982 P.2d 250, 253 (Alaska 1999) (deciding that court may not depart from the plain language of an insurance contract if the contract language is unambiguous); *West v. Umialik Ins. Co.*, 8 P.3d 1135, 1138 (Alaska 2000) (adopting the doctrine of reasonable expectations because insurance policies are contracts of adhesion); *Stordahl v. Gov’t Emp. Ins. Co.*, 564 P.2d 63, 66 n.7 (Alaska 1977) (adopting the view that that insurance contracts should be construed according to their entirety.); **Arizona**—*Gordinier v. Aetna Cas. & Sur. Co.*, 742 P.2d 277, 282-83 (Ariz. 1987) (“Arizona recognizes that an adhesion contract is a different creature than the traditional bargained-for exchange of terms to which the courts apply the ordinary meeting-of-the-minds contract rules.”); *Samsel v. Allstate Ins. Co.*, 59 P.3d 281, 284 (Ariz. 2002) (stating that to determine “whether . . . ambiguity . . . should be construed against the insurer, the language should be examined from the viewpoint of one not trained in law or the insurance business”); *Sparks v. Republic Nat’l Life Ins. Co.*, 534, 647 P.2d 1127, 1132 (Ariz. 1982) (declaring that insurance contracts must be construed in a manner consistent with their plain and ordinary meaning); *Stearns Roger Corp. v. The Hartford Acc. & Indem. Co.*, 165, 571 P.2d 659, 662 (Ariz. 1977) (concluding that “[t]he terms of the insurance policy should be given a practical and reasonable construction which support the intent of the parties.”); *Darner Motor Sales, Inc. v. Universal Underwriters Ins. Co.*, 682 P.2d 388, 394-95 (Ariz. 1984) (recognizing the doctrine of reasonable expectations); **California**—*Gray v. Zurich Ins. Co.*, 419 P.2d 168, 171 (Cal. 1966) (applying “the doctrine of the adhesion contract to insurance policies.”); *Ensign v. Pac. Mut. Life Ins. Co.*, 306 P.2d 448, 450 (Cal. 1957) (concluding that “in insurance law that any ambiguity or uncertainty in an insurance policy is to be resolved against the insurer.”); *Aller v. Truck Ins. Exch., Inc.*, 900 P.2d 619, 627 (Cal. 1995) (“The rules governing policy interpretation require us to look first to the language of the contract in order to ascertain its plain meaning or the meaning a layperson would ordinarily attach to it.”); *AIU Ins. Co. v. Superior Court*, 799 P.2d 1253, 1264 (Cal. 1990) (reasserting that “we generally interpret the coverage clauses of insurance policies broadly, protecting the objectively reasonable expectations of the insured.”); *Boyer v. U.S. Fid. & Guar. Co.*, 274 P. 57, 59 (Ca. 1929) (holding that “[i]nsurance policies are governed by the same general rules which pertain to all contracts. There must be a meeting of the minds.”); **Idaho**—*Clark v. Prudential Prop. & Cas. Ins. Co.*, 66 P.3d 242, 245 (Idaho 2003) (repeating that insurance contracts are contracts of adhesion); *Clark v. Prudential Property and Cas. Ins. Co.*, 66 P.3d 242, 245 (Idaho 2003) (reasserting that ambiguities in insurance contract must be construed most strongly against the insurer); *Mut. of Enumclaw Ins. Co. v. Roberts*, 912 P.2d 119, 122 (Idaho 1996) (concluding that coverage in insurance contract must be determined, as a matter of law, according to the plain meaning of the words used where the policy language is clear and unambiguous);

Ryals v. State Farm Mut. Auto. Ins. Co., 1 P.3d 803,805 (Idaho 2000) (rejecting the doctrine of reasonable expectations); Brinkman v. Aid Ins. Co., 766 P.2d 1227, 1233 (Idaho 1988) (holding that courts must apply the general rules of contract law subject to certain special canons of construction when interpreting insurance contracts); **Louisiana**—Duncan v. Kan. City S. Ry. Co., 747 So. 2d 656, 674 (3d Cir. 1999) (observing that “[i]t is well settled that . . . insurance policies are generally contracts of adhesion.”); Succession of Fannaly v. Lafayette Ins. Co., 805 So. 2d 1134, 1138 (La. 2002) (repeating that “ambiguous contractual provision is construed against the insurer who furnished the contract’s text and in favor of the insured.”); Louisiana Ins. Guar. Ass’n v. Interstate Fire & Cas. Co., 630 So. 2d 759, 763 (La. 1994) (holding that the parties’ intent must “be determined in accordance with the general, ordinary, plain and popular meaning of the words used in the policy.”); La. Ins. Guar. Ass’n v. Interstate Fire & Cas. Co., 630 So. 2d 759, 764 (La. 1994) (holding that a court should construe an insurance contract “to fulfill the reasonable expectations of the parties in the light of the customs and usages of the industry” quoting Trinity Industries, 916 F.2d 267, 269 (5th Cir. 1990)); Ledbetter v. Concord Gen. Corp., 665 So. 2d 1166, 1169 (La. 1996) (holding that ‘a]n insurance policy is an agreement between the parties and should be interpreted by using ordinary contract principles”); **Nevada**—Harvey’s Wagon Wheel, Inc. v. MacSween, 606 P.2d 1095, 1098 (Nev. 1980) (concluding that an insurance contract is contract of adhesion, requiring courts to interpret it broadly and affording the greatest possible coverage to the insured); Rubin v. State Farm Mut. Auto. Ins. Co., 43 P.3d 1018, 1020 (Nev. 2002) (reaffirming that any ambiguity in an insurance contract must be construed against the insurer and in favor of coverage for the insured); Farmers Ins. Exch. v. Young, 832 P.2d 376, 377 (Nev. 1992) (concluding that provisions in insurance contracts should be given their plain meaning when they are clear on their face); Hartford Ins. Group v. Winkler, 508 P.2d 8, 13 (Nev. 1973) (reaffirming that an insurance contract must be construed according to the ordinary, plain meaning of the terms in the contract); Farmers Ins. Exch. v. Young, 832 P.2d 376, 379 n.3 (Nev. 1992) (holding that the reasonable expectations doctrine only applies if the policy is ambiguous); Home Indem. Co. v. Desert Palace, Inc., 468 P.2d 19, 21 (Nev. 1970) (embracing traditional rules of contract construction to interpret insurance contracts); **New Mexico**—Pribble v. Aetna Life Ins. Co., 501 P.2d 255, 259 (N.M. 1972) (recognizing that insurance contracts are adhesion contracts); Lopez v. Found. Reserve Ins. Co., Inc., 646 P.2d 1230, 1232 (N.M. 1982) (re-emphasizing that courts must construe ambiguous language in insurance contracts against the insurers); Wesco Ins. Co. v. Velasquez, 540 P.2d 203, 204-05 (N.M. 1975) (reasserting that courts must construe unambiguous insurance contracts in their usual and ordinary sense like any other contract unless the language of the policy requires something different); W. Commerce Bank v. Reliance Ins. Co., 732 P.2d 873, 875 (N.M. 1987) (embracing the doctrine of reasonable expectation); March v. Mountain States Mut. Cas. Co., 687 P.2d 1040, 1042 (N.M. 1984) (concluding that general principles of contract govern the construction and interpretation of insurance contracts); **Texas**—Arnold v. Nat’l County Mut. Fire Ins. Co., 725 S.W.2d 165, 167 (Tex. 1987) (concluding without deciding definitively that insurance contracts are adhesion contracts because they “arise out of the parties’ unequal bargaining power” and they “allow unscrupulous insurers to take advantage of their insureds’ misfortunes” during the bargaining process); Nat’l Union Fire Ins. Co. v. Hudson Energy Co., 811 S.W.2d 552, 555 (Tex. 1991) (re-emphasizing that ambiguous language in an insurance contract must be construed in favor of the insured); Transp. Ins. Co. v. Standard Oil Co. of Tex., 337 S.W.2d 284, 288 (Tex. 1960) (reiterating that courts must give words appearing in insurance contracts their plain meaning when there is no ambiguity); Kulubis v. Tex. Farm Bureau Underwriters Ins. Co., 706 S.W.2d 953, 955 (Tex. 1986) (“permit[ting] an innocent victim whose property has been destroyed to collect under an insurance contract for a loss reasonably expected to be covered”); Forbau v. Aetna Life Ins. Co., 876 S.W.2d 132, 145 n. 8 (Tex. 1994) (observing that Texas law does not recognize the doctrine of reasonable expectation as a basis to disregard unambiguous policy provisions); Balandran v. Safeco Ins. Co. of Am., 972 S.W.2d 738, 741 (Tex. 1998) (reiterating that insurance contracts are subject to the same rules of construction as other contracts); **Washington**—Mendoza v. Rivera-Chavez, 999 P.2d 29, 40 (Wash. 2000) (declaring that insurance contracts “are usually contracts of adhesion”); Vadheim v. Cont’l Ins. Co., 734 P.2d 17, 20 (Wash. 1987) (declaring that ambiguous clauses must be construed in favor of the insured, “even though the insurer may have intended another meaning”); Panorama Vill. Condo. Owners Ass’n Bd. of Dirs. v. Allstate Ins. Co., 26 P.3d 910, 915 (Wash. 2001) (reiterating that courts must interpret the plain meaning of terms in insurance contracts as an average person, rather than as a technician, would understand or interpret those terms); Keenan v. Indus. Indem. Ins. Co. of the Nw., 738 P.2d 270, 275 (Wash. 1987) (reporting that “[w]e have not adopted a ‘reasonable expectations’ doctrine

separate property states, the greater majority have embraced those same equitable doctrines—adhesion, ambiguity, reasonable expectation and plain-meaning—along with traditional contract principles to declare rights and obligations under insurance contracts.²⁴⁶

with respect to insurance policies”); *Jeffries v. Gen. Cas. Co. of Am.*, 283 P.2d 128, 130 (Wash. 1955) (reiterating that courts must construe insurance contracts using the general rules that apply to other contracts); **Wisconsin**—*Katze v. Randolph & Scott Mut. Fire Ins. Co.*, 341 N.W.2d 689, 691 (Wis.1983) (refusing to declare that all insurance contracts are contracts of adhesion); *Badger Mut. Ins. Co. v. Schmitz*, 647 N.W.2d 223, 234 (Wis. 2002) (reiterating that courts construe ambiguous terms in insurance against the insurer); *Kremers-Urban Co. v. Am. Employers Ins. Co.*, 351 N.W.2d 156, 163 (Wis. 1984) (re-emphasizing that courts must interpret an insurance contract according to its plain and ordinary meaning as understood by a reasonable insured); *Taylor v. Greatway Ins. Co.*, 628 N.W.2d 916, 920 (Wis. 2001) (reiterating that “the interpretation of language in an insurance policy should advance the insured’s reasonable expectations of coverage”); *Wisc. Label Corp. v. Northbrook Prop. & Cas. Ins. Co.*, 607 N.W.2d 276, 282 (Wis. 2000) (reiterating a settled principle that contracts of insurance “are governed by the same rules that govern interpretation of contracts in general”).

246. See **Alabama**—*Travelers Ins. Co., Inc. v. Jones*, 529 So. 2d 234, 239 (Ala. 1988) (embracing the view that “[i]nsurance contracts continue to be contracts of adhesion under which the insured is left little choice beyond electing among standardized provisions offered to him.”); **Arkansas**—*Parker v. S. Farm Bureau Cas. Ins. Co.*, 935 S.W.2d 556, 567 (Ark. 1996) (reaffirming that “[i]nsurance contracts are adhesion contracts in the truest sense of the word.”); **Colorado**—*Huizar v. Allstate Ins. Co.*, 952 P.2d 342, 344 (Colo.1998) (embracing the principle that insurance policies are essentially adhesion contracts); **Delaware**—*State Farm Mut. Auto. Ins. Co. v. Johnson*, 320 A.2d 345, 347 (Del. 1974) (declaring that an insurance contract is an adhesion contract); **Florida**—*Firemans Fund Ins. Co. of S.F., Cal. v. Boyd*, 45 So. 2d 499, 501 (Fla. 1950) (declaring that “a contract of insurance prepared and phrased by the insurer [an adhesion contract] is to be construed liberally in favor of the insured and strictly against the insurer.”); **Georgia**—*First Fin. Ins. Co. v. Am. Sandblasting Co.*, 477 S.E.2d 390, 392 (Ga. App. 1996) (observing that “insurance policies are contracts of adhesion, drawn by the legal draftsman of the insurer.”); **Hawaii**—*State Farm Mut. Auto. Ins. Co. v. Fermahin*, 836 P.2d 1074, 1077 (Haw. 1992) (embracing the proposition that “insurance contracts are contracts of adhesion.”); **Illinois**—*Cramer v. Ins. Exch. Agency*, 675 N.E.2d 897, 906 (Ill. 996) (reaffirming that insurance contracts are contracts of adhesion); **Indiana**—*Huff v. Travelers Indem. Co.*, 363 N.E.2d 985, 993 (Ind. 1977) (deciding that insurance contracts are adhesion contracts); **Iowa**—*Bankers Life Co. v. Aetna Cas. & Surety Co.*, 366 N.W.2d 166, 169 (Iowa 1985) (reaffirming that an insurance policy is a contract of adhesion); **Kansas**—*W. Cas. & Sur. Co. v. Budig*, 516 P.2d 939, 941 (Kan. 1973) (declaring that “[a]n insurance contract is the prime example of an adhesion contract possessing the distinctive characteristics of unequal bargaining strength between the . . . insurer and insured”); **Kentucky**—*Woodson v. Manhattan Life Ins. Co. of N.Y.*, 743 S.W.2d 835, 838 (Ky. 1987) (embracing the proposition that insurance contracts are adhesion contracts); **Maine**—*Ouellette v. Me. Bonding & Cas. Co.*, 495 A.2d 1232, 1235 (Me. 1985) (recognizing that an insurance contract is typically a contract of adhesion); **Maryland**—*Collier v. MD-Individual Practice Ass’n, Inc.*, 607 A.2d 537, 539 (Md. 1992) (concluding that insurance contracts are contracts of adhesion when the insurer drafts and supplies the contract language); **Massachusetts**—*Santos v. Lumbermens Mut. Cas. Co.*, 556 N.E.2d 983, 992 (Mass. 1990) (acknowledging that standardized insurance contracts are adhesion contracts); **Michigan**—*Powers v. Detroit Auto Inter-Ins. Exch.*, 398 N.W.2d 411, 413 (Mich. 1986) (reasserting that insurance contracts are adhesion contracts); **Minnesota**—*Atwater Creamery Co. v. W. Nat. Mut. Ins. Co.*, 366 N.W.2d 271, 277 (Minn. 1985) (explaining and adopting the theory that insurance contracts are contracts of adhesion); **Mississippi**—*J & W Foods Corp. v. State Farm Mut. Auto. Ins. Co.*, 723 So. 2d 550, 551-52 (Miss.1998) (concluding that insurance policies are contracts of adhesion and as such ambiguities are to be construed liberally in favor of the insured and against the insurer); **Missouri**—*Robin v. Blue Cross Hosp. Serv., Inc.*, 637 S.W.2d 695, 697 (Mo. 1982) (declaring that an insurance contract is an adhesion contract if the insurer offered it on a “‘take this or nothing’ basis”); **Montana**—*Leibrand v. Nat’l Farmers Union Prop. & Cas. Co.*, 898 P.2d 1220, 1227 (Mont. 1995) (acknowledging that insurance contracts are generally adhesion contracts); **Nebraska**—*Milbank Ins. Co. v. Henry*, 441 N.W.2d 143,

148 (Neb. 1989) (reasserting that insurance contracts are adhesion contracts); **New Hampshire**—*Magulas v. Travelers Ins. Co.*, 327 A.2d 608, 609 (N.H. 1974) (adopting the proposition that insurance contracts are adhesion contracts); **New Jersey**—*Bd. of Educ. of Borough of Florham Park v. Utica Mut. Ins. Co.*, 798 A.2d 605, 610 (N.J. 2002) (reaffirming that insurance contracts are contracts of adhesion); **New York**—*Allstate Ins. Co. v. Furman*, 444 N.E.2d 996, 998, (N.Y. 1982) (emphasizing that insurance policies are contracts of adhesion); **North Carolina**—*Barker v. Ins. Co.*, 85 S.E.2d 305, 307; (N.C. 1955) (declaring that insurance policies are essentially contracts of adhesion); **North Dakota**—*Cont'l Cas. Co. v. Kinsey*, 499 N.W.2d 574, 578 (N.D. 1993) (embracing the adhesion doctrine as one of several theories to interpret insurance contracts); **Ohio**—*Hounshell v. Am. States Ins. Co.*, 424 N.E.2d 311, 314 (Ohio, 1981) (adopting the proposition that insurance contracts are contracts of adhesion); **Oklahoma**—*Dodson v. St. Paul Ins. Co.*, 812 P.2d 372, 376 (Okla. 1991) (reiterating that an insurance policy is a contract of adhesion); **Oregon**—*Knappenberger v. Cascade Ins. Co.*, 487 P.2d 80, 83 (Or. 1971) (acknowledging that an insurance contract is a contract of adhesion); **Pennsylvania**—*Standard Venetian Blind Co. v. Am. Empire Ins. Co.*, 469 A.2d 563, 574 (Pa. 1983) (holding that insurance contracts are generally contracts of adhesion); **Rhode Island**—*Pickering v. Am. Employers Ins. Co.*, 282 A.2d 584, 593 (R.I. 1971) (recognizing that most insurance contracts are contracts of adhesion, which insurers offer to consumers on a take-it-or-leave-it-basis); **South Carolina**—*Johnston v. Commercial Travelers Mut. Acc. Ass'n of Am.*, 131 S.E.2d 91, 94-95 (S.C. 1963) (recognizing that insurance contracts are primarily contracts of adhesion); **South Dakota**—*Cheney v. Metro. Life Ins. Co.*, 370 N.W.2d 569, 573 (S.D. 1985) (applying the doctrine of adhesion to interpret an insurance contract); **Tennessee**—*Bill Brown Constr. Co., Inc. v. Glens Falls Ins. Co.*, 818 S.W.2d 1, 12 (Tenn. 1991) (concluding that “[a]n insurance policy is a contract of adhesion drafted by the insurer”); **Utah**—*U.S. Fid. and Guar. Co. v. Sandt*, 854 P.2d 519, 522 (Utah 1993) (declaring that “an insurance policy is a classic example of an adhesion contract”); **Vermont**—*State Farm Mut. Auto. Ins. Co. v. Roberts*, 697 A.2d 667, 672 (1997) (embracing the view that insurance contracts are “largely adhesive in nature, often contain[ing] boilerplate terms that are not bargained for, not read, and not understood by the insureds”); **Virginia**—*Great Am. Ins. Co. v. Cassell*, 1988 WL 626029, at *9 (Va. Cir. Ct. 1988) (embracing the view that “insurance agreements are classic examples of contracts of adhesion”); **West Virginia**—*Nat'l Mut. Ins. Co. v. McMahon & Sons, Inc.*, 356 S.E.2d 488, 495 n. 6 (W.Va. 1987) (embracing the doctrine of adhesion to interpret insured's contractual rights and expectations); and, **Wyoming**—*St. Paul Fire & Marine Ins. Co. v. Albany County Sch. Dist. No. 1*, 763 P.2d 1255, 1258 (Wyo. 1988) (declaring that insurance policies represent contracts of adhesion where the insured has little or no bargaining power to vary the terms).

See **Alabama**—*Ala. Ins. Guar. Ass'n v. Magic City Trucking Serv., Inc.*, 547 So. 2d 849, 855 (Ala., 1989) (declaring that “ambiguities are to be construed liberally in favor of the insured and against the insurer, in order to provide the maximum coverage for the insured.”); **Arkansas**—*Smith v. Prudential Prop. & Cas. Ins. Co.*, 10 S.W.3d 846, 850 (Ark. 2000) (“It is also a cardinal rule of insurance law that a policy of insurance is to be construed liberally in favor of the insured and strictly against the insurer.”); **Colorado**—*Simon v. Shelter Gen. Ins. Co.*, 842 P.2d 236, 239 (Colo. 1992) (holding ambiguity in the policy language must be construed against the drafter of the document and in favor of the insured.”); **Connecticut**—*Izzo v. Colonial Penn Ins. Co.*, 203 Conn. 305, 309-10 (1987) (holding that ambiguities are to be construed against the insurer when the contract language is unclear); **Delaware**—*Rhone-Poulenc Basic Chem. Co. v. Am. Motorists Ins.*, 616 A.2d 1192, 1196 (Del. 1992) (declaring that to the extent an ambiguity exists, courts must employ the doctrine of *contra proferentum*, and construe policy language most strongly against the insurer which drafted it); **District of Columbia**—*Chase v. State Farm Fire & Cas. Co.*, 780 A.2d 1123, 1127 (D.C. 2001) (“[A]mbiguities in an insurance policy are construed against the insurer”); **Florida**—*Aetna Cas. & Sur. Co. v. Cartmel*, 100 So. 802, 803 (Fla. 1924) (holding that ambiguities in insurance contracts “must be liberally construed in favor of the insured”); **Georgia**—*Richards v. Hanover Ins. Co.*, 299 S.E.2d 561, 563 (Ga. 1983) (“Any ambiguities in the contract are strictly construed against the insurer as drafter of the document”); **Hawaii**—*Sturla, Inc. v. Fireman's Fund Ins. Co.*, 684 P.2d 960, 964 (Haw. 1984) (restating that ambiguities in insurance contract are resolved against the insurer); **Illinois**—*Healey v. Mut. Accident Ass'n*, 25 N.E. 52, 53 (Ill. 1890) (“[I]n all cases [ambiguities] must be liberally construed in favor of the insured”); **Indiana**—*Am. States Ins. Co. v. Kiger*, 662 N.E.2d 945, 947 (Ind. 1996) (“Where there is ambiguity, insurance policies are to be construed strictly against the insurer.”); **Iowa**—*Gen. Cas. v. Hines*, 156 N.W.2d 118, 122 (Iowa 1968) (holding that ambiguous terms in

insurance contracts will be accorded a construction most favorable to the insured); **Kansas**—*Nat'l Inspection & Repair, Inc. v. Valley Forge Life Ins. Co.*, 56 P.3d 807, 817 (Kan. 2002) (declaring that ambiguities must be decided in favor of the insured); **Kentucky**—*St. Paul Fire & Marine Ins. Co. v. Powell-Walton-Milward, Inc.*, 870 S.W.2d 223, 225 (Ky. 1994) (holding that all ambiguities in insurance policies must be construed against the insurer); **Maine**—*Patrons-Oxford Mut. Ins. Co. v. Dodge*, 426 A.2d 888, 891 (Me. 1981) (quoting *Westcott v. Allstate Ins.*, 397 A.2d 156, 167 (Me. 1979)) (declaring that any ambiguity in an insurance contract is construed “strictly against the insurer and liberally in favor of the insured . . .”); **Massachusetts**—*Cody v. Conn. Gen. Life Ins. Co.*, 439 N.E.2d 234, 237 (Mass. 1982) (holding that ambiguous words in insurance contracts must be resolved against the insurance company that employed them and in favor of the insured); **Michigan**—*State Farm Mut. Auto Ins. Co. v. Enter. Leasing Co.*, 549 N.W.2d 345, 351 (Mich. 1996) (reaffirming that courts must construe ambiguities against the insurer); **Minnesota**—*Columbia Heights Motors, Inc. v. Allstate Ins. Co.*, 275 N.W.2d 32, 36 (Minn.1979) (reiterating that ambiguities in insurance contracts must be resolved against the insurer); **Mississippi**—*Nationwide Mut. Ins. Co. v. Garriga*, 636 So. 2d 658, 662 (Miss.1994) (“[T]he general rule [is] that provisions of an insurance contract are to be construed strongly against the drafter.”); **Missouri**—*Meyer Jewelry Co. v. Gen. Ins. Co. of Am.*, 422 S.W.2d 617, 623 (Mo.1968) (embracing the view that ambiguity in an insurance contract should be resolved against the insurer); **Montana**—*Bauer Ranch v. Mountain W. Farm Bureau Mut. Ins. Co.*, 695 P.2d 1307, 1309 (Mont. 1985) (reaffirming that contractual ambiguities are construed against the insurer); **Nebraska**—*Farm Bureau Ins. Co. of Neb. v. Martinsen*, 659 N.W.2d 823, 827 (Neb. 2003) (“[A]n ambiguous insurance policy will be construed in favor of the insured . . .”); **New Hampshire**—*Trombly v. Blue Cross/Blue Shield of N.H.-Vt.*, 423 A.2d 980, 985 (N.H. 1980) (adopting the proposition that an ambiguous insurance policy will be construed in favor of the insured and against the insurer, but only where there is ambiguity in the contract); **New Jersey**—*Mazzilli v. Accident & Cas. Ins. Co. of Winterthur*, 170 A.2d 800, 803 (N.J. 1961) (“If the controlling language will support two meanings, one favorable to the insurer, and the other favorable to the insured, the interpretation sustaining coverage must be applied.”); **New York**—*Thomas J. Lipton, Inc. v. Liberty Mut. Ins. Co.*, 314 N.E.2d 37, 39 (N.Y. 1974) (holding that ambiguities in an insurance policy are to be construed against the insurer); **North Carolina**—*Williams v. Nationwide Mut. Ins. Co.*, 152 S.E.2d 102, 107 (N.C. 1967) (holding that uncertainty or ambiguous language of an insurance policy must be resolved in the insured’s favor); **North Dakota**—*Mills v. Agrichemical Aviation, Inc.*, 250 N.W.2d 663, 671 (N.D. 1977) (reasserting that ambiguous policies are construed most strongly against the insurers and in favor of providing insurance coverage); **Ohio**—*Faruque v. Provident Life & Accident Ins. Co.*, 508 N.E.2d 949, 952 (Ohio 1987) (reiterating that doubtful, uncertain, or ambiguous language in insurance contracts must be construed strictly against the insurer and liberally in favor of the insured); **Oklahoma**—*N.Y. Life Ins. Co. v. Sullivan*, 129 P.2d 71, 73 (Okla. 1942) (holding that ambiguous terms in an insurance contract must be resolved against the insurer); **Oregon**—*N. Pac. Ins. Co. v. Hamilton*, 22 P.3d 739, 741 (Or. 2001) (restating that courts must resolve an ambiguous term in insurance contract “by construing the term against the drafter of the policy”); **Pennsylvania**—*Bateman v. Motorists Mutual Ins. Co.*, 590 A.2d 281, 283 (Pa. 1991) (reiterating that courts must construe ambiguous provisions in insurance contracts against the insurer and in favor of the insured); **Rhode Island**—*Sjogren v. Metro. Prop. & Cas. Ins. Co.*, 703 A.2d 608, 612 (R.I. 1997) (reasserting that courts must construe ambiguous language in insurance contracts against will be construed against insurers and in favor of the insureds); **South Carolina**—*Spinx Oil Co. v. Federated Mut. Ins.*, 427 S.E.2d 649, 651 (S.C. 1993) (“Ambiguous or conflicting terms in an insurance policy must be construed liberally in favor of the insured and strictly against the insurer.”); **South Dakota**—*State Farm Mut. Auto. Ins. Co. v. Vostad*, 520 N.W.2d 273, 275 (S.D. 1994) (quoting *Kremer v. Am. Family Mut. Ins. Co.*, 501 N.W.2d 765, 767-68 (S.D. 1993)) (reiterating that courts must choose an interpretation most favorable to the insured if a provision in an insurance policy is “fairly susceptible” to different interpretations); **Tennessee**—*Palmer v. State Farm Mut. Auto. Ins. Co.*, 614 S.W.2d 788, 789 (Tenn.1981) (reiterating that courts must resolve any ambiguity and doubt in favor of the insured when interpreting insurance contracts); **Utah**—*Gressler v. N.Y. Life Ins. Co.*, 163 P.2d 324, 330 (Utah 1945) (endorsing the principle that ambiguous insurance policies should “be construed in favor of the insured and against the insurer”); **Vermont**—*Noyes v. Commercial Travelers*, 215 A.2d 495, 497 (Vt. 1965) (declaring that ambiguous language in insurance contracts will be strictly construed against the insurer); **Virginia**—*Nat'l Fire Ins. Co. of Hartford v. Dervishian*, 145 S.E.2d 184, 187 (Va. 1965) (construing ambiguities against the insurer); **West**

Virginia—Thompson v. State Auto. Ins. Co., 11 S.E.2d 849, 850 (W. Va. 1940) (“[A] cardinal rule of construction [is] that clauses in insurance contracts should be construed liberally [in favor of] the insured.”); and **Wyoming**—T.M. *ex rel.* Cox v. Executive Risk Indem. Inc., 59 P.3d 721, 725 (Wyo. 2002) (re-emphasizing that courts must construe ambiguous terms in insurance contracts against the insurer). *But see* Cheney v. Bell Nat’l Life, 556 A.2d 1135, 1138 (Md. 1989) (“Maryland does not follow the [ambiguity] rule, adopted in many jurisdictions, that an insurance policy is to be construed most strongly against the insurer.”).

See **Alabama**—State Farm Fire & Cas. Co. v. Shady Grove Baptist Church, 838 So. 2d 1039, 1042 (Ala. 2002) (“A contract of insurance, like other contracts, is governed by the general rules of contracts.” (quoting Twin City Fire Ins. Co. v. Alfa Mut. Ins. Co., 817 So. 2d 687, 691 (Ala. 2001))); State Farm Fire & Cas. Co. v. Slade, 747 So. 2d 293, 311 (Ala. 1999) (quoting Lambert v. Liberty Mut. Ins. Co., 331 So. 2d 260, 263 (Ala. 1976)) (“[T]he objectively reasonable expectations of applicants and intended beneficiaries regarding the terms of insurance contracts will be honored”); Little Cahaba Coal Co. v. Aetna Life Ins. Co., 68 So. 317, 318 (Ala. 1915) (“[P]olicies of insurance, when vague, ambiguous, or inconsistent, are generally construed with favor to the party indemnified . . . [but judges cannot wrestle] the contract from its plain meaning when reasonably construed upon an examination of the whole instrument.”); **Arkansas**—Jordan v. Atl. Cas. Ins. Co., 40 S.W.3d 254, 255-56 (Ark. 2001) (“[W]here terms of the policy are clear and unambiguous, the policy language controls, and absent statutory strictures to the contrary, exclusionary clauses are generally enforced according to their terms.” . . . [T]he terms of an insurance contract are not to be rewritten under the rule of strict construction against the company issuing it so as to bind the insurer to a risk which is plainly excluded” (quoting Vincent v. Prudential Ins. Brokerage, 970 S.W.2d 215, 216 (Ark. 1998))); Duvall v. Mass. Indem. & Life Ins. Co., 748 S.W.2d 650, 656 (Ark. 1988) (“[A]ccident policies should be so interpreted that provisions of the policies effectuate the reasonable expectations of the purchaser.” (quoting Robert Keeton, Basic Text on Insurance Law 351 (West Group) (1971))); **Colorado**—Allstate Ins. Co. v. Huizar, 52 P.3d 816, 820 (Colo. 2002) (“[I]nsurance policies are contracts, which must be construed according to their plain meaning and well-settled principles of contract interpretation.”); State Farm Mut. Auto Ins. Co. v. Nissen, 851 P.2d 165, 168 (Colo. 1993) (recognizing the “principle of reasonable expectations as expressed in insurance cases”); Wota v. Blue Cross & Blue Shield of Colo., 831 P.2d 1307, 1309 (Colo.1992) (ruling that the terms of an insurance “should be construed in accordance with general principles of contractual interpretation”); **Connecticut**—Agosto v. Aetna Cas. & Sur. Co., 239 Conn. 549, 552 n.3 (Conn. 1996) (embracing the doctrine of reasonable expectation); Hammer v. Lumberman’s Mut. Cas. Co., 573 A.2d 699, 704 (Conn. 1990) (concluding that courts must interpret terms in an insurance contract according to their natural and ordinary meaning if the terms are plain and unambiguous); Weingarten v. Allstate Ins. Co., 363 A.2d 1055, 1059 (Conn. 1975) (stressing that the terms of an insurance policy are to be construed according to the general rules of contract construction); **Delaware**—Rhone-Poulenc Basic Chems. Co. v. Am. Motorists Ins. Co., 616 A.2d 1192, 1195 (Del. 1992) (“Clear and unambiguous language in an insurance policy should be given its ordinary and usual meaning.”); E.I. du Pont de Nemours v. Shell Oil Co., 498 A.2d 1108, 1113 (Del. 1985) (“The basic rule of contract construction gives priority to the intention of the parties.”); Hallowell v. State Farm Mut. Ins. Co., 443 A.2d 925, 927 (Del.1982) (reaffirming the doctrine of reasonable expectation); **District of Columbia**—Chase v. State Farm Fire & Cas. Co., 780 A.2d 1123, 1131-32 (D.C. 2001) (restating the doctrine of reasonable expectation); GLM P’ship v. Hartford Cas. Ins. Co., 753 A.2d 995, 998 (D.C. 2000) (reaffirming that rules of contract construction govern the interpretation of contracts); Nichols v. N.C. Mut. Life Ins. Co., 162 A.2d 499, 501 (D.C. 1960) (“[I]f the language has but one clear meaning that meaning will be adopted whether favorable to the insured or not.” (quoting Belland v. Am. Auto. Ins. Co., 101 A.2d 517, 518 (D.C. 1953))); **Florida** — Watson v. Prudential Prop. & Cas. Ins. Co., 696 So. 2d 394, 396 (Fla. 1997) (“Florida courts commonly adopt the plain meaning of words contained in legal and non-legal dictionaries” to decipher clear and unambiguous terms in insurance contracts (quoting Brill v. Indianapolis Life Ins. Co., 784 F.2d 1511, 1513 (11th Cir. 1956))); Aetna Cas. & Sur. Co. v. Cartmel, 100 So. 802, 803 (Fla. 1924) (“[Insurance] contracts are subject to the same rules of construction applied to other contracts”); **Georgia**—Boardman Petroleum, Inc. v. Federated Mut. Ins. Co., 498 S.E.2d 492, 494 (Ga. 1998) (“[C]ontracts of insurance are interpreted by ordinary rules of contract construction”); Park ‘N Go of Ga., Inc. v. U.S. Fid. & Guar. Co., 471 S.E.2d 500, 503 (Ga. 1996) (“[W]hen the terms of a written contract are clear and unambiguous, the court is to look to the contract alone to find the parties’ intent.”); Roland v. Ga. Farm Bureau Mut. Ins. Co., 462 S.E.2d 623,

625 (Ga. 1995) (“A contract of insurance should be strictly construed against the insurer and read in favor of coverage in accordance with the reasonable expectations of the insured.”); **Hawaii**—*Park v. Gov’t Employees Ins. Co.*, 974 P.2d 34, 38 (Haw. 1999) (embracing the position that courts must construe insurance policy terms in accord with the reasonable expectations of a insured laypersons); *First Ins. Co. of Haw., Inc. v. State*, by *Minami*, 665 P.2d 648, 655 (Haw. 1983) (adopting the position that insurance policies are subject to the general rules of contract construction, and stating that the “terms of [an insurance] policy should be interpreted according to their plain, ordinary, and accepted sense in common speech unless it appears from the policy that a different meaning is intended”); **Illinois**—*Luechtefeld v. Allstate Ins. Co.*, 656 N.E.2d 1058, 1063 (Ill. 1995) (reaffirming that insurance contracts be construed and enforced to accord with the objectively reasonable expectations of the insured); *U.S. Fid. & Guar. Co. v. Wilkin Insulation Co.*, 578 N.E.2d 926, 930 (Ill. 1991) (“Where a policy provision is clear and unambiguous, its language must be taken in its ‘plain, ordinary and popular sense’” (quoting *Hartford Accident & Idem. Co. v. Case Found. Co.*, 294 N.E.2d 7, 12 (Ill. 1973))); *Martindell v. Lake Shore Nat’l Bank*, 154 N.E.2d 683, 689 (Ill. 1958) (embracing and outlining the general rules of contract construction and interpretation); **Indiana**—*Colonial Penn. Ins. Co. v. Guzorek*, 690 N.E.2d 664, 667 (Ind. 1997) (“Contracts of insurance are governed by the same rules of construction as other contracts.”); *Allstate Ins. Co. v. Boles*, 481 N.E.2d 1096, 1101 (Ind. 1985) (“[A] contract is clear and unambiguous, the language therein must be given its plain meaning.”); *Eli Lilly & Co. v. Home Ins. Co.*, 482 N.E.2d 467, 470 (Ind. 1985) (adopting the doctrine of reasonable expectation); **Iowa**—*Westfield Ins. Cos. v. Econ. Fire & Cas. Co.*, 623 N.W.2d 871, 881 (Iowa 2001) (“Under the reasonable expectations doctrine ‘the objectively reasonable expectations of applicants and intended beneficiaries regarding insurance policies will be honored’” (quoting *Krause v. Krause*, 589 N.W.2d 721, 727 (Iowa 1999))); *Cairns v. Grinnell Mut. Reinsurance Co.*, 398 N.W.2d 821, 823 (Iowa 1987) (reasserting that “well-established principles” govern the interpretation of insurance contracts where the intent of the parties control); *Iowa Nat’l Mut. Ins. Co. v. Fid. & Cas. Co. of N.Y.*, 128 N.W.2d 891, 893 (Iowa 1964) (meaning “[An insurance] contract should be construed as a whole, and the clear and unambiguous language must be given its plain meaning.”); *Farm Bureau Mut. Ins. Co. v. Horinek*, 660 P.2d 1374, 1376 (Kan. 1983) (“The construction and effect of insurance contracts are questions of law to be determined by the court.”); **Kansas**—*Bramlett v. State Farm Mut. Auto. Ins. Co.*, 468 P.2d 157, 159 (Kan. 1970) (holding that unambiguous terms in insurance contracts must be construed according to their plain, ordinary and popular meanings); **Kentucky**—*Kemper Nat’l Ins. Cos. v. Heaven Hill Distilleries, Inc.*, 82 S.W.3d 869, 875 (Ky. 2002) (“We are cognizant of the general principles of insurance contract construction”); *Simon v. Continental Ins. Co.*, 724 S.W.2d 210, 212 (Ky. 1986) (embracing the doctrine of reasonable expectation); *Weaver v. Nat’l Fid. Ins. Co.*, 377 S.W.2d 73, 75 (Ky. 1964) (“[C]ourts cannot make a different insurance contract for the parties by enlarging the risks contrary to the natural and obvious meaning of the existing contract.”); **Maine**—*Am. Prot. Ins. Co. v. Acadia Ins. Co.*, 814 A.2d 989, 993 (Me. 2003) (“[T]he interpretation of an unambiguous contract ‘must be determined from the plain meaning of the language used’” (quoting *Portland Valve, Inc. v. Rockwood Sys. Corp.*, 460 A.2d 1383, 1387 (Me. 1983))); *Baybutt Constr. Corp. v. Commercial Union Ins. Co.*, 455 A.2d 914, 921 (Me. 1983) (“The objectively reasonable expectations of an insured will be honored even though painstaking study of the policy provisions would have negated those expectations.”); *Swift v. Patrons’ Androscoggin Mut. Fire Ins. Co.*, 132 A. 745, 746 (Me. 1926) (holding that an insurance contract, like any other contract, must be construed in accordance with the intention of the parties by examining the whole instrument); **Maryland**—*ABC Imaging of Wash., Inc. v. Travelers Indem. Co. of Am.*, 820 A.2d 628, 633 (Md. 2003) (“Under the objective interpretation principle, where the language employed in a contract is unambiguous, a court shall give effect to its plain meaning”); *Bailer v. Erie Ins. Exch.*, 687 A.2d 1375, 1383 (Md. 1997) (citing *Knowles v. United Servs. Auto. Ass’n*, 832 P.2d 394, 399 (N.M. 1992)) (“The reasonable expectations of the insured can be upheld only if the repugnant clause is not given effect.”); *Pac. Indem. Co. v. Interstate Fire & Cas. Co.*, 488 A.2d 486, 488 (Md. 1985) (“An insurance contract, like any other contract, is measured by its terms unless a statute, a regulation, or public policy is violate thereby.”); **Massachusetts**—*Hazen Paper Co. v. U.S. Fid. & Guar. Co.*, 555 N.E.2d 576, 583 (Mass. 1990) (concluding that when interpreting an insurance policy, it is appropriate, to consider “what an objectively reasonable insured . . . would expect to be covered” under the contract); *Cody v. Conn. Gen. Life Ins. Co.*, 439 N.E.2d 234, 237 (Mass. 1982) (concluding that insurance contracts must be construed like other contracts, “according to the fair and reasonable meaning of the words in which the agreement

of the parties is expressed” (quoting *MacArthur v. Mass. Hosp. Serv. Inc.*, 180 N.E.2d 449, 450 (Mass. 1962)); *Freelander v. G. & K. Realty Corp.*, 258 N.E.2d 786, 788 (Mass. 1970) (adopting the view that words will be given their plain or well established meaning where the language in an insurance contract is not ambiguous); **Michigan**—*Allstate Ins. Co. v. Keillor*, 537 N.W.2d 589, 591 (Mich. 1995) (“A court must look at the policy language from an objective standpoint and determine whether an insured could have reasonably expected coverage.”); *Upjohn Co. v. N.H. Ins. Co.*, 476 N.W.2d 392, 397 (Mich. 1991) (adopting the traditional rules of contract to interpret insurance contracts and enforcing contractual terms as written); *Kingsley v. Am. Cent. Life Ins. Co.*, 242 N.W. 836, 836 (Mich. 1932) (reaffirming the view that terms in an insurance contract must be construed as written when the policy is plain and easily understood); **Minnesota**—*Kersten v. Minn. Mut. Life Ins. Co.*, 608 N.W.2d 869, 873 (Minn. 2000) (“General contract principles govern the construction of insurance policies and insurance policies are interpreted to give effect to the intent of the parties. *Jenoff, Inc. v. N.H. Ins. Co.*, 558 N.W.2d 260, 262 (Minn. 1997) (reiterating that terms in an insurance policy “must be given their plain, ordinary, or popular meaning” if they are not specifically defined (quoting *Smith v. St. Paul Fire & Marine Ins. Co.*, 353 N.W.2d 130, 132 (Minn. 1984))); *Atwater Creamery Co. v. W. Nat’l Mut. Ins. Co.*, 366 N.W.2d 271, 276-77 (Minn. 1985) (explaining, embracing, and applying the doctrine of reasonable expectation); **Mississippi**—*Blackledge v. Omega Ins. Co.*, 740 So. 2d 295, 298 (Miss.1999) (holding that courts must give terms used in insurance policies their ordinary and popular definition); *Sessoms v. Allstate Ins. Co.*, 634 So. 2d 516, 519 (Miss. 1993) (“Like all other contracts, insurance policies which are clear and unambiguous are to be enforced according to their terms as written.”); *Brown v. Blue Cross & Blue Shield of Miss., Inc.*, 427 So. 2d 139, 141 (Miss.1983) (“The objectively reasonable expectations of applicants and intended beneficiaries regarding the terms of insurance contracts will be honored even though painstaking study of the policy provisions would have negated those expectations.”); **Missouri**—*Peters v. Employers Mut. Cas. Co.*, 853 S.W.2d 300, 301-02 (Mo. 1993) (“[G]eneral rules for interpretation of other contracts apply to insurance contracts as well.”); *Rodriguez v. Gen. Accident Ins. Co. of Am.*, 808 S.W.2d 379, 382 (Mo. 1991) (holding that the reasonable expectation doctrine applies only to satisfy insureds’ objective reasonable expectations under an adhesion contract of insurance); *State ex rel. Prudential Ins. Co. of Am. v. Bland*, 185 S.W.2d 654, 656 (Mo. 1945) (holding that unequivocal language in an express, written insurance contract must be given its plain, ordinary, and usual meaning); **Montana**—*Truck Ins. Exch. v. Waller*, 828 P.2d 1384, 1386 (Mont. 1992) (holding clear and explicit language governs the interpretation of insurance contracts); *Transamerica Ins. Co. v. Royle*, 656 P.2d 820, 824 (Mont. 1983) (adopting the doctrine of reasonable expectations); *Anaconda Co. v. Gen. Accident Fire & Life Assur. Corp.*, 616 P.2d 363, 367 (Mont. 1980) (“The general rules of contract law apply to an insurance policy.”); **Nebraska**—*Daehnke v. Neb. Dept. of Soc. Servs.*, 557 N.W.2d 17, 21 (Neb. 1996) (“The terms of a contract are to be accorded their plain and ordinary meaning as ordinary, average, or reasonable persons would understand them.”); *Amco Ins. Co. v. Norton*, 500 N.W.2d 542, 544 (Neb. 1993) (“[A]n insurance policy is to be construed as any other contract to give effect to the parties’ intentions at the time the contract was made”); *Kraci v. Aetna Cas. & Sur. Co.*, 374 N.W.2d 40, 44 (Neb. 1985) (Neb. 1985) (holding that an insured’s reasonable expectation of coverage must be measured by the clear terms of the insurance contract as understood by the reasonable, ordinary person); **New Hampshire**—*Contoocook Valley Sch. Dist. v. Graphic Arts Mut. Ins. Co.*, 788 A.2d 259, 262 (N.H. 2001) (stressing that terms of an insurance contract must be accorded their plain meaning as indicated by the words and their relation to each other as a whole); *Magulas v. Travelers Ins. Co.*, 327 A.2d 608, 609-10 (N.H. 1974) (embracing the view that courts should take into consideration the reasonable expectations of the insured when interpreting and enforcing an insurance contract); *Stone v. Granite State Fire Ins. Co.*, 45 A. 235, 236 (N.H. 1899) (declaring that courts must employ the same general rules that are applicable to other written contracts when construing insurance policies); **New Jersey**—*Zacarias v. Allstate Ins. Co.*, 775 A.2d 1262, 1268 (N.J. 2001) (restating that a court must first attribute to the words their plain and ordinary meaning when interpreting the language of an insurance contract); *Kievit v. Loyal Protective Life Ins. Co.*, 170 A.2d 22, 26 (N.J. 1961) (adopting the doctrine of reasonable expectation to ensure that courts will construe insurance contracts liberally in favor of insureds); *Kindervater v. Motorists Cas. Ins. Co.*, 199 A. 606, 608 (N.J. 1938) (concluding that the rule adopted for constructing of other contracts is applicable for interpreting the language of an insurance contract); **New York**—*Teichman v. Cmty. Hosp. of W. Suffolk*, 663 N.E.2d 628, 630 (N.Y. 1996) (reiterating that courts must give unambiguous terms their plain and ordinary meaning); *Breed v. Ins. Co. of N. Am.*, 385 N.E.2d 1280, 1282 (N.Y. 1978)

(declaring that an insurance contract must be interpreted by the same general rules that govern the construction of any written contract and enforced according to the intent of the parties as expressed in the language in the contract); *Bird v. St. Paul Fire & Marine Ins. Co.*, 120 N.E. 86, 87 (N.Y. 1918) (declaring that courts must consider the reasonable expectation and purpose of the ordinary business person when interpreting and enforcing terms of insurance contracts); **North Carolina**—*Great Am. Ins. Co. v. C.G. Tate Constr. Co.*, 279 S.E.2d 769 (N.C. 1981) (adopting the reasonable expectations doctrine and declaring an insurance contract must be interpreted according to the reasonable expectations of the insured); *Woods v. Ins. Co.*, 246 S.E.2d 773, 777 (N.C. 1978) (“As with all contracts, the goal of construction is to arrive at the intent of the parties when the policy was issued.”); *Walsh v. United Ins. Co. of Am.*, 44 S.E.2d 817, 820 (N.C. 1965) (“[W]here the language of an insurance policy is plain, unambiguous, and susceptible of only one reasonable construction, the courts will enforce the contract according to its terms.”); **North Dakota**—*Aid Ins. Servs., Inc. v. Geiger*, 294 N.W.2d 411, 414-15 (N.D. 1980) (holding that plain, ordinary meaning of undefined term must guide courts’ interpretation of insurance contracts); *N.W.G.F. Mut. Ins. Co. v. Norgard*, 518 N.W.2d 179, 181 (N.D. 1994) (reaffirming that insurance contracts construed as other contracts to give effect to the mutual intention of the parties when the parties formed the agreement); **Ohio**—*Gomolka v. State Auto. Mut. Ins. Co.*, 436 N.E.2d 1347, 1348 (Ohio 1982) (holding that courts should employ general rules of contract construction and interpretation to interpret insurance contracts); *Olmstead v. Lumbermens Mut. Ins. Co.*, 259 N.E.2d 123, 126 (Ohio 1970) (holding that courts may not change meaning of terms in an insurance contract when words have a plain and ordinary meaning, unless the plain meaning would lead to an absurd result); **Oklahoma**—*Cranfill v. Aetna Life Ins. Co.*, 49 P.3d 703, 706 (Okla. 2002) (reaffirming that holding that plain, ordinary and popular meanings of unambiguous terms must guide courts’ interpretation of insurance contracts); *Max True Plastering Co. v. U.S. Fid. & Guar. Co.*, 912 P.2d 861, 870 (Okla. 1996) (adopting the doctrine of reasonable expectation); *Carraco Oil Co. v. Mid-Continent Cas. Co.*, 484 P.2d 519, 521 (Okla. 1971) (“A policy of insurance should be construed as every other contract, that is, where not ambiguous, according to its terms.”); **Oregon**—*Botts v. Hartford Accident & Indem. Co.*, 585 P.2d 657, 659 (Or. 1978) (concluding that an insurance policy should be interpreted according to the understanding of the ordinary purchaser); *Weidert v. State Ins. Co.*, 24 P. 242, 245 (Or. 1890) (“Contracts of insurance must have effect like all other written contracts. The intention of the parties must govern and control.”); **Pennsylvania**—*Prudential Prop. & Cas. Ins. Co. v. Colbert*, 813 A.2d 747, 750 (Pa. 2002) (“[C]ourts must give plain meaning to a clear and unambiguous contract provision unless to do so would be contrary to a clearly expressed public policy.”); *Madison Constr. Co. v. Harleysville Mut. Ins. Co.*, 735 A.2d 100, 106 (Pa. 1999) (adopting “well-settled principles of contract interpretation” to interpret insurance contracts); *Collister v. Nationwide Life Ins. Co.*, 388 A.2d 1346, 1351 (Pa. 1978) (holding that courts must assure that insurance consumers’ reasonable expectations are fulfilled when courts interpret insurance contracts); **Rhode Island**—*Am. Commerce Ins. Co. v. Porto*, 811 A.2d 1185, 1195 (R.I. 2002) (repeating that courts must read insurance contracts literally, and give each word its plain and ordinary meaning when terms are not ambiguous); *Colagiovanni v. Metro. Life Ins. Co.*, 190 A. 459, 460 (R.I. 1937) (declaring that insurance contract are controlled by the same principles of law that are applicable to other contracts); **South Carolina**—*Rhame v. Nat’l Grange Mut. Ins. Co.*, 121 S.E.2d 94, 96 (S.C. 1961) (holding that insurance contracts, like other contracts, must be construed according to the terms which the parties have used, and reaffirming that unambiguous terms in insurance contracts must be construed according to their plain, ordinary and popular meaning); **South Dakota**—*Biegler v. Am. Family Mut. Ins. Co.*, 621 N.W.2d 592, 599 (S.D. 2001) (restating that language of an insurance contract must be construed according to the plain meaning of its terms); *Dairyland Ins. Co. v. Wyant*, 474 N.W.2d 514, 518 (S.D. 1991) (holding that the interpretation and construction of insurance contracts are controlled by the same rules applicable to contracts generally); **Tennessee**—*McKimm v. Bell*, 790 S.W.2d 526, 527 (Tenn. 1990) (reiterating that insurance policies are subject to the same rules of construction that are used to interpret other types of contracts); *Parker v. Provident Life & Accident Ins. Co.*, 582 S.W.2d 380, 383 (Tenn., 1979) (reaffirming that courts must employ the usual and ordinary meaning of language to interpret insurance contracts); **Utah**—*Marriot v. Pac. Nat’l Life Assur. Co.*, 467 P.2d 981, 983 (Utah 1970) (“[I]t is proper to look to the ordinary usage and connotations of words to determine the meaning intended.”); *Pac. Auto. Ins. Co. v. Commercial Cas. Ins. Co. of N.Y.*, 161 P.2d 423, 426 (Utah 1945) (“An insurance contract like any other contract must be interpreted in the light of the intention of the parties.”); **Vermont**—*State Farm Mut. Auto. Ins. Co. v. Roberts*, 697 A.2d 667, 672 (Vt. 1997) (declaring that

determining the insured's reasonable expectations is important to help determine the scope of coverage under insurance contracts); *Dunsmore v. Coop. Fire Ins. Ass'n of Vt.*, 298 A.2d 853, 855 (Vt. 1972) ("Words in a[n insurance] contract will be assigned their common meaning and usage where they can be sensibly applied to the subject matter."); *Noyes v. Order of United Commercial Travelers of Am.*, 215 A.2d 495, 497 (Vt. 1965) ("Like other contracts, [insurance contracts] must receive practical, reasonable, and fair interpretations, consonant with the apparent object and intent of the parties . . ."); **Virginia**—*London Guarantee & Accident Co. v. C.B. White & Bros.*, 49 S.E.2d 254, 259 (Va. 1948) (embracing the theory that courts must give words and phrases in an insurance contract their usual and ordinary meaning); **Virginia**—*Home Ins. Co. v. Gwathmey*, 1 S.E. 209, 211 (Va. 1887) (adopting the principle that insurance policies are contracts whose terms must be interpreted in accordance with general principles of construction); **West Riffe v. Home Finders Assocs., Inc.**, 517 S.E.2d 313, 318-19 (W. Va. 1999) (adopting the doctrine of reasonable expectations to interpret only ambiguous language in insurance contracts); *McGann v. Hobbs Lumber Co.*, 145 S.E.2d 476, 481 (W. Va. 1965) ("[L]ike other contracts, must receive a practical and reasonable interpretation consonant with the apparent object and intent of the parties."); *Stone v. Nat'l Sur. Corp.*, 125 S.E.2d 618, 619 (W. Va. 1962) (reiterating that courts must accord unambiguous terms in an insurance contract their plain meaning without attempting to construct or interpret terms); **Wyoming**—*Gainsco Ins. Co. v. Amoco Prod. Co.*, 53 P.3d 1051, 1066 (Wyo. 2002) (reiterating that court must interpret insurance contracts as they interpret other contracts and use the plain meaning of words "that a person in the position of the insured would understand them to mean" when courts interpret insurance contracts); *see also Oregon*—*Collins v. Farmers Ins. Co. of Or.*, 822 P.2d 1146, 1161 (Or.1991) (Unis, J., dissenting) ("This court has not explicitly adopted the doctrine of 'reasonable expectation,' at least by name, in any of its forms. Neither has this court explicitly rejected it. Language in at least two of our recent opinions, however, suggests support for the doctrine."); **Rhode Island**—*Taft v. Cerwonka*, 433 A.2d 215, 218 (R.I. 1981) (recognizing that insureds have expectation of coverage after paying insurance premiums but failing to explicitly adopt the doctrine of reasonable expectation); **Tennessee**—*Harrell v. Minn. Mut. Life Ins. Co.*, 937 S.W.2d 809, 810 (Tenn. 1996), (recognizing that insureds have some expectations under an insurance policy but failing to adopt the doctrine of reasonable expectation formally); **Virginia**—*Compare St. Paul Fire & Marine Ins. Co. v. S.L. Nusbaum & Co., Inc.*, 316 S.E.2d 734, 736 (Va. 1984) ("[R]easonable men . . . may reach reasonable, but opposite, conclusions . . . [Nevertheless it] was incumbent upon the insurer to employ exclusionary language clear enough to avoid any such ambiguity . . ."), *with Morrow Corp. v. Harleysville Mut. Ins. Co.*, 110 F. Supp. 2d 441,451 (E.D. Va. 2000) ("An ambiguous term must be accorded the meaning that a reasonable person in the position of the insured would have given to the term and that is consistent with the reasonable expectations of a person in the insured's position, for it is well-settled in Virginia and in all other jurisdictions that ambiguities in meaning are resolved in favor of the insured."); *But see Florida*—*Deni Assocs. of Fla., Inc. v. State Farm Fire & Cas. Ins. Co.*, 711 So. 2d 1135, 1140 (Fla. 1998) (refusing to adopt the doctrine of reasonable expectation); **Idaho**—*Casey v. Highlands Ins. Co.*, 600 P.2d 1387, 1390-91 (Idaho 1979) (embracing traditional rules of contract construction instead of reasonable expectation doctrine); **Kansas**—*Halsey v. Farm Bureau Mut. Ins. Co., Inc.*, 61 P.3d 691, 700 (Kan. 2003) ("[T]he Michigan court prefaced its analysis by affirming the reasonable expectations doctrine. . . which is not the law in Kansas . . ."); **North Dakota**—*RLI Ins. Co. v. Heling*, 520 N.W.2d 849, 855 (N.D. 1994) ("The doctrine of reasonable expectations has yet to be accepted by a majority of this court . . ."); **Ohio**—*Wallace v. Balint*, 761 N.E.2d 598, 606 (Ohio 2002) ("[T]here is not yet a majority on this court willing to accept the reasonable-expectations doctrine."); **South Carolina**—*Allstate Ins. Co. v. Mangum*, 383 S.E.2d 464, 467 (S.C. Ct. App. 1989) (reporting that the reasonable expectations doctrine "has never been accepted by the Supreme Court of this State"); **South Dakota**—*Dakota, Minn. & E.R.R. v. Heritage Mut. Ins. Co.*, 639 N.W.2d 513, 514 (S.D. 2002) ("[T]he doctrine of reasonable expectations has never been adopted by South Dakota . . .") (quoting *S.D. State Cement Plant Comm'n v. Wausau Underwriters Ins. Co.*, 616 N.W.2d 397, 407 (S.D. 2000)); **Utah**—*Allen v. Prudential Prop. & Cas. Ins. Co.*, 839 P.2d 798, 805 (Utah 1992) (rejecting the concept of the reasonable expectations doctrine); **Wyoming**—*Ahrenholtz v. Time Ins. Co.*, 968 P.2d 946, 950 (Wyo. 1998) ("We declined to apply the reasonable expectations theory of recovery in insurance cases."); Gregory T. Lawrence, *Sheets v. Brethren Mutual: Maryland's High Court Misconstrues CGL To Cover Excluded Economic Loss Caused By Negligent Misrepresentation*, 27 U. BALT. L. REV. 189, 194 n.24 (1997) (reporting that reasonable expectations that Maryland courts do not apply the doctrine of reasonable expectations).

Stated briefly, the adhesion doctrine requires courts to interpret questionable clauses in first and third-party insurance contracts in favor of the insureds.²⁴⁷ The justification is quite commonsensical. Courts generally recognized the following: (1) insurers draft and supply the terms under various provisions in insurance contracts, which are usually “boilerplates” or standardized forms; (2) insurers typically offer insurance on a “take-it-or-leave-it-basis,” leaving insurance applicants with no viable options; and (3) insureds and insurers’ bargaining positions are generally unequal because insurers occupy the superior positions as a matter of law.²⁴⁸

Generally, under the doctrine of ambiguity, courts must interpret or construe ambiguous words and phrases in first and third-party insurance contracts against insurers and in favor of insureds.²⁴⁹ But some supreme courts in community and separate property states require lower courts to construe insurance contracts “strongly” or “strictly” in favor of insureds.²⁵⁰ Moreover, courts must examine and interpret terms in first and third-party insurance agreements from the perspectives of laypersons, who have not received any formal legal training or who have no experience in the insurance industry.²⁵¹ Quite simply, courts must always construe ambiguous language in favor of an insured and declare that the agreement covers the insured’s property or person, if the insurance agreement’s “controlling language” has two equally plausible interpretations; one that favors the insured and the other one that favors the insurer.²⁵²

Courts also will interpret first and third-party insurance contracts quite broadly to protect the “objectively reasonable expectations of the insureds.”²⁵³ For example, Louisiana courts must construe an insurance contract to satisfy insureds’ reasonable expectations by considering and using customary practices within the insurance industry.²⁵⁴ In Georgia, an insurance agreement must be read strictly in favor of coverage to satisfy insureds’ reasonable expectations of the insured.²⁵⁵ Furthermore, the Supreme Court of Maine issued an arguably even more pro-insureds rule, holding that the insureds’ objectively reasonable expectations must be honored even though painstaking investigation of various contract clauses

247. See *supra* note 245.

248. See *W. Cas. & Sur. Co. v. Budig*, 516 P.2d 939, 941 (Kan. 1973); *Collier v. MD-Individual Practice Ass’n*, 607 A.2d 537, 539 (Md. 1992); *Pickering v. Am. Employers Ins. Co.*, 282 A.2d 584, 593 (R.I. 1971).

249. See *supra* notes 245 and 246.

250. See *supra* notes 245 and 246.

251. See *Samsel v. Allstate Ins. Co.*, 59 P.3d 281, 284 (Ariz. 2002).

252. See *Mazzilli v. Accident & Cas. Ins. Co. of Winterthur*, 170 A.2d 800, 803 (N.J. 1961).

253. See *AIU Ins. Co. v. Superior Court*, 799 P.2d 1253, 1264 (Cal. 1990).

254. See *La. Ins. Guar. Ass’n v. Interstate Fire & Cas. Co.*, 630 So. 2d 759, 764 (La. 1994).

255. See *Roland v. Ga. Farm Bureau Mut. Ins. Co.*, 462 S.E.2d 624, 625 (Ga. Ct. App. 1979).

might negate those expectations.²⁵⁶ Perhaps the Supreme Court of New Mexico presents the better summary of the reasonable expectation doctrine: To determine an insured's reasonable expectation under an insurance contract, "the test is not what the insurer intended its words to mean, but what a reasonable person in the insured's position would have understood them to mean."²⁵⁷

When interpreting first and third-party insurance contracts, the doctrine of plain meaning requires courts to consider and apply the plain, ordinary, and popular meaning of questionable words and phrases.²⁵⁸ Stated slightly differently, the doctrine of plain meaning ensures that insurance contracts are construed as a whole and that courts apply the plain meaning to fairly clear or unambiguous language in the contracts.²⁵⁹ Finally, in Texas and in all states, insurance contracts are subject to the same rules of construction as other contracts.²⁶⁰ Therefore, courts also must construe first and third-party insurance contracts by examining the entire contract and weighing the intent of the parties.²⁶¹ Simply put, when interpreting and construing insurance agreements, courts may not ignore settled common law rules that govern all bargained-for-exchange contracts.²⁶²

V. CONFLICTING STATE AND FEDERAL COURT DECLARATORY JUDGMENTS—WHETHER PROPERTY INSURERS HAVE A DUTY TO INDEMNIFY INNOCENT CO-INSURED FIDUCIARIES UNDER FIRST-PARTY INSURANCE CONTRACTS

Debatably, since the vast majority of state supreme courts embraced the same equitable and legal doctrines to construe and interpret first and third-party insurance contracts, the likelihood of insurers or innocent co-insured fiduciaries receiving fairly predictable rulings or declaratory relief should not be a major issue.²⁶³ Certainly innocent co-insured fiduciaries' likelihood of receiving declaratory relief should not correlate in any meaningful way with, for example: (1) whether those fiduciaries live in community or separate property jurisdictions; (2) whether they reside in the Fifth or Ninth Circuit; or (3) whether innocent co-insured fiduciaries are

256. See *Baybutt Constr. Corp. v. Commercial Union Ins. Co.*, 455 A.2d 914, 921 (Me. 1983).

257. See *W. Commerce Bank v. Reliance Ins. Co.*, 732 P.2d 873, 875 (N.M. 1987).

258. See *U.S. Fid. & Guar. Co. v. Wilkin Insulation Co.*, 578 N.E.2d 926, 930 (Ill. 1991).

259. See *Iowa Nat. Ins. Co. v. Fid. & Cas. Co.*, 128 N.W.2d 891, 893 (Iowa 1964).

260. See *infra* note 288.

261. See *Stordahl v. Gov't Emp. Ins. Co.*, 564 P.2d 64, 66 (Alaska 1997); see also *Stearns Roger Corp. v. Hartford Accident & Indem. Co.*, 571 P.2d 659, 662 (Ariz. 1977).

262. See *Brinkman v. Aid Ins. Co.*, 766 P.2d 1227, 1233 (Idaho 1988).

263. See discussion *supra* Part IV.B.

husbands and wives, executors and estate's beneficiaries, or some other combination.²⁶⁴

Yet, as revealed in this part, both federal and state courts are seriously divided over whether national and state-based property and liability insurers must indemnify innocent co-insured fiduciaries.²⁶⁵ These divisions among federal courts of appeals and state courts have a long history.²⁶⁶ To be sure, such conflicts can generate a considerable amount of uncertainty among insurers and innocent fiduciaries.²⁶⁷ Furthermore, the duty-to-indemnify splits reported below arguably reduce significantly innocent co-insured fiduciaries' abilities to predict their likelihood of success in declaratory judgment trials.²⁶⁸ Arguably, that limitation causes fiduciaries to waste resources needlessly, re-litigating the same duty-to-indemnify question in state and federal courts.²⁶⁹

A. *Whether Property Insurers Have a Duty to Indemnify Innocent Co-Insured Spouses*

1. *Conflicting Declarations and Rulings in Community Property States*

Among Texas's courts, conflicting rulings over innocent co-insured spouses' rights under first-party insurance contracts began more than a half century ago with the Waco Appellate Court's decision in *Jones v. Fidelity & Guaranty Insurance Corp.*²⁷⁰ In *Jones*, Fidelity & Guaranty Insurance Corporation (Fidelity) insured Edward and Annie Mae Jones' community property under a standard fire insurance contract.²⁷¹ The insured property was the co-insured couple's homestead.²⁷²

The policy limit was \$1,500, and under the terms of the agreement, Fidelity promised to indemnify the co-insured spouses if fire was the dominant proximate cause of their destroyed community property.²⁷³ However, the first-party insurance contract contained several conditions subsequent.²⁷⁴ One condition stated that the insured's "fraud or false swearing" would void the entire policy.²⁷⁵ The other stated that Fidelity would not indemnify if a fire destroyed the spouses' community property

264. See discussion *supra* Part III.A-B.

265. See discussion *supra* Part IV.B.

266. See discussion *supra* Part IV.B.

267. See discussion *infra* Part V.A.

268. See discussion *supra* Part IV.A-B.

269. See discussion *supra* Part IV.A-B.

270. *Jones v. Fid. & Guar. Ins. Corp.*, 250 S.W.2d 281, 281 (Tex. Civ. App.—Waco 1952, writ *ref'd*).

271. *Id.* at 282.

272. *Id.*

273. *Id.* at 281.

274. *Id.*

275. *Id.*

“directly or indirectly” and the insured failed “to use all reasonable means to save and preserve the property at and after a loss.”²⁷⁶

While the community property was insured, Annie divorced her husband.²⁷⁷ The disposition of the community property, however, did not appear in the divorce decree.²⁷⁸ After the divorce, “Edward Jones feloniously burned the insured building,” without Annie Mae’s participation or prior knowledge of the arson.²⁷⁹ Citing her interest in the destroyed community property, she asked Fidelity to cover her losses.²⁸⁰ Fidelity refused, asserting that it had no duty to indemnify because Edward’s criminal act voided or canceled the entire policy.²⁸¹

The Waco Court of Appeals embraced Fidelity’s argument and concluded that the insurer had no contractual duty to indemnify Annie Mae, the innocent co-insured spouse.²⁸² To reach that conclusion, the appellate court conducted an arguably two-step analysis.²⁸³ First, citing settled law, the appellate court observed:

Fraudulent losses are generally [excluded under] fire insurance contracts upon grounds of public policy and morals. Accordingly, [an insured’s] voluntary and intentional burning of insured property . . . does not ordinarily give rise to a cause of action for the recovery of loss resulting from the fire, even though such loss is not expressly excepted from the coverage of the policy.²⁸⁴

For sure, Annie was a co-insured spouse under the fire insurance contract.²⁸⁵ However, she was totally innocent because she did not torch the community property.²⁸⁶ Therefore, to hold that she could not recover under the insurance contract, the Waco Appellate Court had to find a way to tarnish Annie’s innocence with her divorced husband’s deviance.²⁸⁷ To help achieve that end, the court of appeals applied traditional rules of contract construction and interpretation.²⁸⁸ First, the court examined the

276. *Id.*

277. *Id.*

278. *Id.*

279. *Id.*

280. *Id.* at 282.

281. *Id.*

282. *Id.*

283. *Id.*

284. *Id.* at 281-82.

285. *Id.*

286. *Id.* at 281.

287. *Id.*

288. *Id.* at 282. “If such was not the clearly expressed intention of the parties as evidenced by the language used in the policy . . . , then . . . courts in construing the same should look to the situation of the parties as it existed at the time when the contract was made.” *Id.*

“clear” language in the contract to determine the insureds’ and the insurer’s intent.²⁸⁹

Second, after concluding that the parties’ intentions were mutual, the Waco Court of Appeals declared that Edward’s or Annie’s “contingent right . . . to recover anything [under the fire insurance contract] . . . was a joint right which inured to the mutual benefit of both [spouses].”²⁹⁰ Consequently, the deviant as well as the innocent spouse had a joint, contractual obligation “to use all reasonable means to save and preserve the insured property at and after a loss.”²⁹¹ Because innocent Annie breached her contractual duty to protect the community property from her deviant husband’s destructive activities, the property insurer had no duty to indemnify her.²⁹²

To augment its breach-of-contractual-obligation explanation, the Waco Court of Appeals also used a property interest analysis to reach the same conclusion.²⁹³ Citing Texas’s settled marital property rights rules, the court of appeals concluded that if Fidelity indemnified either the deviant or innocent co-insured spouse under the terms of the insurance contract, the proceeds “would have been community property . . . as long as [Edward and Annie were] husband and wife.”²⁹⁴ That fact would remain even if one were to characterize the insurance proceeds as being a joint, several, or divisible interest.²⁹⁵ The court of appeals also observed that even after the probate court granted Annie’s request for a divorce without dividing the community property, the deviant husband still had property rights.²⁹⁶ Therefore, if Fidelity was forced to indemnify Annie for her losses after the divorce, deviant Edward still would have access to the insurance money.²⁹⁷ The reason is not complicated. Under settled Texas’s marital property laws, innocent Annie and her deviant husband continued “to be joint owners of the insured property . . . as tenants in common.”²⁹⁸

289. *Id.*

290. *Id.*

291. *Id.* “Being husband and wife when they accepted the policy insuring their community property, each was acting with the other in a joint undertaking for the common benefit of both at the time they entered into the contract of insurance.” *Id.*

292. *Id.*

293. *Id.*

294. *Id.*

295. *Id.*

296. *Id.*

297. *Id.*

298. *Id.* (citing *Kirkwood v. Domnan*, 16 S.W. 428, 429 (Tex. 1891, no writ).

“We think . . . that the husband’s interest in the property can be . . . only in the divorce suit, and as a part of the decree of divorce. It not having been . . . done, the former husband and wife stood towards each other, after the decree of divorce, as if they had never borne that relation to each other. They then owned the property as tenants in common, and subject to all the rules and regulations of strangers bearing to each other that relation.”

Id.

After *Jones*, first-party property insurers and innocent co-insured spouses presented the same question before two different appellate courts.²⁹⁹ Those tribunals reached the same conclusion, although citing different reasons.³⁰⁰ In *Bridges v. Commercial Standard Insurance Co.*, the Eastland Court of Appeals embraced some of the court's reasoning in *Jones* and declared that an innocent co-insured spouse may not recover under a property insurance contract if the deviant co-insured spouse destroys or sets fire to jointly owned or community property.³⁰¹ In *Western Fire Insurance Co. v. Sanchez*, the Tyler Court of Appeals declared that public policy prevents an innocent insured wife from recovering under a fire insurance contract after a deviant husband sets fire to a homestead.³⁰²

In light of the appellate courts' rulings in *Jones*, *Bridges*, and *Sanchez*, Texas's law was clear and fairly predictable for nearly thirty-five years: First-party property insurers had no contractual duty to indemnify innocent co-insured spouses after deviant spouses destroyed jointly owned or community property.³⁰³ However, in 1986, the Texas Supreme Court decided *Kulubis v. Texas Farm Bureau Underwriters Insurance Co.* without rejecting any portion of the holdings in *Jones*, *Bridges*, and *Sanchez*.³⁰⁴

Briefly, in *Kulubis*, John and Betty Kulubis were married and lived in Betty's mobile home.³⁰⁵ Betty, the innocent co-insured spouse under the fire insurance contract, decided to get a divorce and served a divorce citation to John.³⁰⁶ In a fit of rage, "John set fire to the mobile home, destroying it and all of the personal property inside."³⁰⁷ Betty asked the insurer to compensate her for her share of the destroyed property.³⁰⁸ The insurer refused, asserting that it had no duty to indemnify.³⁰⁹

The Texas Supreme Court ruled against the property insurer.³¹⁰ Citing Betty's "reasonable expectations," the supreme court declared that she could recover her share of the insurance proceeds.³¹¹ In reaching that conclusion, the court stated "that the proper test to be applied was what a reasonable person would have understood the fire insurance policy to

299. See *W. Fire Ins. Co. v. Sanchez*, 671 S.W.2d 666, 669 (Tex. App.—Tyler 1984, writ ref'd n.r.e.); *Bridges v. Commercial Standard Ins. Co.*, 252 S.W.2d 511, 512 (Tex. Civ. App.—Eastland 1952, no writ).

300. Cf. *Sanchez*, 671 S.W.2d at 512 with *Bridges*, 252 S.W.2d at 669.

301. *Bridges*, 252 S.W.2d at 512 (citing *Jones v. Fid. & Guar. Ins. Corp.*, 250 S.W.2d 281, 282 (Tex. Civ. App.—Waco 1952, writ ref'd)).

302. *Sanchez*, 671 S.W.2d at 669.

303. See, e.g., *Sanchez*, 671 S.W.2d at 666; *Bridges*, 252 S.W.2d at 511; *Jones*, 250 S.W.2d at 282.

304. *Kulubis v. Tex. Farm Bureau Underwriters Ins. Co.*, 706 S.W.2d 953, 955 (Tex. 1986, writ granted).

305. *Id.* at 954.

306. *Id.*

307. *Id.*

308. *Id.*

309. *Id.*

310. *Id.*

311. *Id.* at 955.

mean.”³¹² Citing public policy, the *Kulubis* court also held that innocent co-insured Betty had a contractual right to recover her share of the insurance money.³¹³

In dicta, the Texas Supreme Court embellished its reasonable expectation and public policy rulings by highlighting some commonsensical observations.³¹⁴ First the supreme court noted that Texas Farm Bureau would be unjustly enriched by avoiding its contractual obligation if the court barred Betty’s recovery.³¹⁵ Second, preventing innocent Betty’s recovery would impute the estranged and deviant husband’s wrongdoing to Betty, the intended and actual victim.³¹⁶ Third, the Texas Supreme Court noted that allowing Betty, a completely innocent co-insured spouse, to recover would not be “a fraud on the insurance company.”³¹⁷ Finally, the supreme court observed that innocent Betty had a separate property interest in the mobile home, rather than a community property interest.³¹⁸ Consequently, the deviant co-insured and estranged husband would not have benefitted directly by allowing Betty to recover her share of the insurance proceeds.³¹⁹

The declaration and five public policy considerations in *Kulubis* arguably comprised the settled law in Texas for a while.³²⁰ But a careful review of the entire eleven year period after *Kulubis* reveals that Texas’s appellate courts were seriously divided over whether deviant spouses’ destruction of community or jointly owned property bars innocent spouses’ recovery of insurance proceeds.³²¹ During that eleven-year span, the Corpus Christi and Amarillo Courts of Appeals decided, respectively, *Auto. Insurance Co. of Hartford Connecticut v. Davila* and *Travelers Cos. v. Wolfe*.³²² Both the *Davila* and *Wolfe* appellate courts concluded that first-party property insurers have a duty to indemnify innocent co-insured spouses.³²³

312. *Id.* at 954 (citing *Hoyt v. N.H. Fire Ins. Co.*, 29 A.2d 121, 123 (N.H. 1942)).

313. *Id.* at 955.

314. *Id.*

315. *Id.*

316. *Id.*

317. *Id.*

318. *Id.* The mobile home was not community property because Betty’s parents had given it to Betty and her estranged husband. *Id.* See also TEX. CONST. art. XVI, § 15 (stating that all property a spouse acquires by gift shall be the separate property of that spouse).

319. *Id.*

320. *Id.* Again, the five policy considerations were as follows: (1) preventing a wrongdoer from benefitting from wrongdoing; (2) meeting the reasonable expectations of an innocent co-insured; (3) preventing fraud on the insurance company; (4) preventing the insurance company’s unjust enrichment; and (5) preventing a deviant spouse’s criminal acts from being imputed to innocent victim—the co-insured innocent spouse. *Id.*

321. See, e.g., *infra* text accompanying notes 322-54.

322. *Travelers Cos. v. Wolfe*, 838 S.W.2d 708 (Tex. App.—Amarillo 1992, no writ); *Auto. Ins. Co. of Hartford Conn. v. Davila*, 805 S.W.2d 897 (Tex. App.—Corpus Christi 1991, writ denied).

323. See *Davila*, 805 S.W.2d at 911 (upholding the jury’s verdict in favor of co-insured spouses

On the other hand, in *Saunders v. Commonwealth Lloyd's Insurance Co.* and *Chubb Lloyds Insurance Co. of Texas v. Kizer*, the courts' rulings were decidedly different for the innocent co-insured spouses.³²⁴ More specifically, in *Saunders*, the San Antonio Court of Appeals held that the property insurer had a reasonable basis, as a matter of law, to deny the innocent co-insured spouse's first-party claim.³²⁵ The insurer had a legal foundation to support its decision, even though the allegedly deviant co-insured husband was acquitted of setting fire to the spouses' community property home.³²⁶

In *Kizer*, the Fort Worth Court of Appeals upheld the jury's findings that the co-insured deviant husband torched the home and its furnishings, and declared, as a matter of law, that the innocent co-insured wife could not recover insurance proceeds for her share of destroyed community property or for any part of the house not owned separately.³²⁷ To justify that conclusion, the Fort Worth Court of Appeals cited *Kulubis* and focused on the types of property interests that were insured in *Kulubis* and in *Kizer*.³²⁸

Again, in *Kizer and Kulubis*, community property and separate property interests, respectively, were insured against specified perils under the first-party insurance contracts.³²⁹ However, in *Kulubis*, the Texas Supreme Court allowed the innocent co-insured spouse to recover insurance proceeds for separate property and expressly left the question of community property for another day.³³⁰ In the wake of that void, the Fort Worth Court of Appeals ruled against the innocent spouse to keep the deviant spouse from benefitting from the insurance proceeds.³³¹ The *Kizer* court of appeals provided the following justification for the decision:

(1) after the husband allegedly set fire to the house, (2) after the insurer denied the claim, and (3) after the insurer breached its duty of good faith and the insurance contract); *Wolfe*, 838 S.W.2d, at 712 (allowing the innocent spouse to recover her separate property interest in the insurance proceeds after the deviant husband torched the insured community property—a corporation, even though (1) the deviant co-insured husband was the “named insured” on the insurance contract—doing business as the corporation, and (2) the deviant husband committed arson and destroyed the community property after the wife secured her divorce).

324. See *Saunders v. Commonwealth Lloyd's Ins. Co.*, 928 S.W.2d 322 (Tex. App.—San Antonio 1996, no writ); see also *Chubb Lloyds Ins. Co. of Tex. v. Kizer*, 943 S.W.2d 946 (Tex. App.—Fort Worth 1997, writ denied).

325. See *Saunders*, 928 S.W.2d at 325.

326. *Id.*

327. See *Kizer*, 943 S.W.2d at 953.

328. *Id.* at 951.

329. See *id.*

330. See *Kulubis*, 706 S.W.2d at 955 (“Texas courts are faced with an additional problem in this situation because we are a community property state. It is not necessary for us to address that particular problem at this time inasmuch as the mobile home in question was . . . separate property . . .”).

331. See *Kizer*, 943 S.W.2d at 953.

Texas community property law is problematic in these circumstances. Generally, fire insurance proceeds . . . take the place of the destroyed property Thus, any payment of insurance proceeds under a policy issued to the community, providing coverage for community property, and paid for by community assets, can only be characterized as community property. Accordingly, if an innocent spouse is paid a “share” for destroyed community property, absent any severance of the estate, that payment itself must be characterized as community property in which the guilty spouse necessarily has an interest.³³²

Once more, *Kulubis* was decided eleven years before *Kizer*, and in the former case, the Texas Supreme Court stated the following:

We are not to be understood as holding that an innocent spouse is barred from recovering under an insurance policy covering community property. We do not have that fact situation before us and therefore do not address the problem of how to compensate the innocent spouse and yet not permit benefit to the wrongdoing spouse. That problem will be addressed when and if it is presented to us.³³³

Thus, the conflicting innocent spouse decisions continued.³³⁴ However, the Texas Supreme Court received an excellent opportunity to settle the conflict, finally and totally, a decade after its separate property decision in *Kulubis*.³³⁵

In 1999, the Supreme Court of Texas decided *Texas Farmers Insurance Co. v. Murphy*.³³⁶ The underlying facts in *Murphy* are simple.³³⁷ Texas Farmers insured Robert and Daisy Murphy’s home against specific perils under a standard temporary insurance binder.³³⁸ Seven days later, the Murphys’ home burned down.³³⁹ After the fire, Robert sued the insurer to collect insurance proceeds, Daisy filed for divorce, and she and Robert executed a partition agreement to divide their community interests if they received proceeds under the insurance binder.³⁴⁰ Ultimately, Robert and Daisy divorced, and Daisy filed her own claim for the insurance benefits.³⁴¹

Texas Farmers investigated the claim and concluded that Robert intentionally caused the fire.³⁴² Reserving its rights, the insurer filed a

332. See *id.* at 952-53.

333. See *Kulubis*, 706 S.W.2d at 955.

334. See discussion *infra* Part VII.A.

335. See *Tex. Farmers Ins. Co. v. Murphy*, 996 S.W.2d 873 (Tex. 1999).

336. *Id.* at 882.

337. See *id.*

338. See *id.* at 875.

339. *Id.*

340. *Id.*

341. See *id.*

342. *Id.*

declaratory judgment suit.³⁴³ In the complaint, Texas Farmers asserted that it had no duty to indemnify Robert and Daisy.³⁴⁴ “Farmers alleged that public policy prohibits arsonists from recovering for their losses.”³⁴⁵ A jury found that Robert burned down the home.³⁴⁶ The same jury also found that Daisy was innocent because she did not have prior knowledge of Robert’s deviant intentions, and she did not participate in the arson.³⁴⁷

However, notwithstanding the jury’s innocent spouse finding, the trial court issued a take-nothing judgment against both Robert and Daisy.³⁴⁸ Innocent Daisy appealed.³⁴⁹ Applying the traditional rules of contract construction that govern the interpretation of insurance policies, the Texas Supreme Court declared that Texas’s longstanding public policy against allowing insureds to benefit from fraud does not prevent an innocent co-insured spouse from recovering her share of property-insurance benefits.³⁵⁰ Did the supreme court clearly decide whether property insurers always have a duty to indemnify innocent co-insured spouses after deviant spouses destroy community, separate, or partition property? The answer is no.³⁵¹

Therefore, conflicting innocent-spouse decisions remain among Texas’s courts.³⁵² Differences also exist between the Texas Supreme Court’s ruling in *Murphy* and the Fifth Circuit Court of Appeals’ decisions in diversity cases.³⁵³ To be sure, these continuing conflicts among Texas’

343. *Id.*

344. *Id.*

345. *Id.* “Farmers further alleged that Robert misstated and willfully concealed material facts, vitiating coverage under the insurance policy’s concealment clause. Robert counterclaimed for breach of contract and violations of the Texas Insurance Code.” *Id.*

346. *Id.*

347. *Id.*

348. *Id.*

349. *Id.*

350. *Id.* at 881.

351. *See id.*

352. Compare *McEwin v. Allstate Tex. Lloyds*, 118 S.W.3d 811, 815-16 (Tex. App.—Amarillo 2003 no pet.) (citing *Kulubis*, 706 S.W.2d at 955) (“Kathy’s status as an innocent spouse . . . does not determine her right to recover from Allstate The series of events encompassing James’ intentionally causing loss of the insured home and turning in a loss report without disclosing that the loss was due to his intentional acts comprised perpetration of a fraud on Allstate relating to the insurance, even had James not made false statements in his later examinations under oath Because of James’ fraud, the Concealment or Fraud clause voided the policy as to both James and Kathy”), with *Murphy*, 996 S.W.2d at 881 (“We reaffirm our longstanding public policy [of] preventing an arsonist from benefitting from fraud by denying recovery of his or her own one-half interest in the claim against the insurer. We conclude, however, that such public policy does not overcome an innocent spouse’s contractual right to recover her or his one-half interest in the policy benefits.”).

353. Compare *Webster v. State Farm Fire & Cas. Co.*, 953 F.2d 222, 223 (5th Cir.1992) (concluding that a post-fire divorce between the innocent and deviant co-insured spouses—which awarded half of the insurance proceeds on the destroyed community property to the innocent spouse as separate property—still did not permit the innocent spouse to recover insurance proceeds for a pre-divorce arson fire), and *Norman v. State Farm Fire & Cas. Co.*, 804 F.2d 1365,1366 (5th Cir. 1986) (stressing that denying deviant co-insureds a benefit is the single most important consideration, and declaring that the co-insured innocent spouse could not recover any insurance proceeds because there was a possibility that the deviant co-insured spouse might benefit), and *Cal. Ins. Co. v. Allen*, 235 F.2d

courts and between the Fifth Circuit and Texas' courts, are problematic. Arguably, there should be no conflicts because section 2002.003 of the Texas Insurance Code is rather clear:

A homeowners' insurance policy or fire insurance policy . . . may not be delivered, issued for delivery, or renewed in this state unless the policy contains the following language: It is understood and agreed that this policy, subject to all other terms and conditions contained in this policy, when *covering residential community property*, as defined by state law, shall remain in full force and effect as to the interest of each spouse covered, irrespective of divorce or change of ownership between the spouses *unless excluded by endorsement* attached to this policy until the expiration of the policy or until canceled in accordance with the terms and conditions of this policy.³⁵⁴

Of course, whether innocent co-insured spouses may recover benefits under property insurance contracts also generates a considerable number of conflicting rulings in other community property states.³⁵⁵ Generally, for a variety of reasons, other state courts embraced the proposition that innocent spouses may recover insurance earnings after deviant co-insured spouses destroy community property.³⁵⁶ Other courts in community property jurisdictions have found a variety of different reasons to rule against innocent co-insured spouses.³⁵⁷

In particular, whether innocent co-insured spouses may receive all or half of the insurance proceeds has produced conflicting judicial rulings in community property states.³⁵⁸ For example, in *Felder v. North River Insurance Co.*, the deviant co-insured spouse died as he was destroying jointly owned property.³⁵⁹ The Wisconsin Court of Appeals allowed the innocent spouse to recover all of the insurance money to cover the full

178, 180 (5th Cir. 1956) (concluding that an innocent co-insured spouse may not recover insurance proceeds if the deviant spouse torches community property); *with Murphy*, 996 S.W.2d at 881 (allowing an innocent co-insured to recover insurance money when a deviant co-insured spouse intentionally destroys community property).

354. TEX. INS. CODE ANN. § 2002.003 (Vernon 2007) (emphasis added).

355. See discussion *infra* Part VII.A.2.

356. See *State Farm Auto. Ins. Co. v. Raymer*, 977 P.2d 706, 711 (Alaska 1999); *Atlas Assur. Co. of Am. v. Mystic*, 822 P.2d 897, 901 (Alaska 1991); *Nangle v. Farmers Ins. Co. of Ariz.*, 73 P.3d 1252, 1257 (Ariz. Ct. App. 2003); *Trinity Universal Ins. Co. v. Kirsling*, 73 P.3d 102, 106 (Idaho 2003); *Guillot v. Travelers Indem. Co.*, 338 So. 2d 334, 337 (La. Ct. App. 1976); *Williams v. Fire Ass'n of Phila.*, 193 So. 202, 204 (La. Ct. App. 1939); *Delph v. Potomac Ins. Co.*, 620 P.2d 1282, 1285 (N.M. 1980).

357. See, e.g., *Crumpler v. State Farm Fire & Cas. Co.*, No. 95-31300, 1996 WL 512065, at *2 (5th Cir. 1986) (citing Louisiana's law); *Brown v. U.S. Fid. & Guar. Co.*, 977 P.2d 807, 817 (Ariz. Ct. App. 1998).

358. See discussion *infra* Part VII.A.2.

359. *Felder v. N. River Ins. Co.*, 435 N.W.2d 263, 264 (Wis. Ct. App. 1988).

amount of the innocent spouse's losses.³⁶⁰ To justify its ruling, the *Felder* court stressed that the deviant spouse died in the fire; consequently, the deviant spouse could never benefit from his destruction of the insured and jointly owned property.³⁶¹

However, in *Atlas Assurance Co. of America v. Mistic*, the Supreme Court of Alaska reached a decidedly different conclusion.³⁶² In *Mistic*, the husband and wife jointly owned their house as tenants in common.³⁶³ In addition, the spouses were co-insureds under a property insurance contract.³⁶⁴ Briefly put, the husband set fire to and totally destroyed the house.³⁶⁵ Shortly thereafter, the innocent wife filed for divorce.³⁶⁶ A probate judge granted the divorce and concluded:

While there is a presumption that an equal division of marital property is a just division . . . [the husband in this case] willfully destroyed and wasted substantial marital property and [the wife] is entitled to one-half the value of the property destroyed in addition to her share of the marital estate under an equitable distribution.³⁶⁷

The insurer refused to compensate the innocent co-insured wife for her interest in the demolished house.³⁶⁸ Therefore, she sued the insurer, asserting that she had a contractual right to receive half of the policy limits under the insurance contract.³⁶⁹ A different lower court in Alaska found the following: (1) the estranged husband intentionally caused the fire and destroyed the jointly owned house; (2) the property insurer had no contractual duty to indemnify the deviant husband for his losses, since he intentionally destroyed the insured property; (3) the first-party insurer had a contractual duty to indemnify the innocent co-insured wife *Mistic*; and (4) the innocent spouse was entitled to half the policy limits under the insurance contract.³⁷⁰ The insurer appealed.³⁷¹

First, the Alaska Supreme Court observed that the insurance contract's policy limit was \$42,000.³⁷² However, the innocent co-insured wife's property losses exceeded that amount.³⁷³ Her estimated damages were

360. *Id.* at 266.

361. *Id.*

362. *Atlas Assur. Co. of Am. v. Mistic*, 822 P.2d 897, 901 (Alaska 1991).

363. *Id.* at 898.

364. *Id.*

365. *Id.*

366. *Id.*

367. *Id.*

368. *Id.* at 899.

369. *Id.* at 900.

370. *Id.* at 899.

371. *Id.*

372. *Id.* at 898.

373. *Id.*

\$100,000.³⁷⁴ Did the insurer have a contractual duty to compensate the innocent wife for all of her losses? The supreme court said no.³⁷⁵ To reach that conclusion, the Supreme Court of Alaska examined the “insurable interests” clause in the insurance contract.³⁷⁶ It read:

Insurable Interest and Limit of Liability. Even if more than one person has an insurable interest in the property covered, we shall not be liable:

- a. for an amount greater than the interest of a person insured under this policy; or
- b. for more than the limit of liability that applies.³⁷⁷

The insurance contract clearly limited a co-insured’s payment “to the lesser of the person’s interest or the contract limits.”³⁷⁸ When the innocent spouse submitted her claim to the insurer, her property interest was greater than the contract limits: \$100,000 versus \$42,000.³⁷⁹ Therefore, arguably, she should have received \$42,000 from the insurer.³⁸⁰ However, the Supreme Court of Alaska declared that the innocent co-insured spouse could recover only *one-half* of her total damages or *one-half* of the contract limits, whichever was less.³⁸¹

Consequently, in *Mistic*, the innocent spouse recovered only \$21,000, rather than the full amount under the insurance contract.³⁸² Recognizing a split among courts, the Alaska Supreme Court justified its declaration this way: “The vast majority of courts which have reached this issue, and . . . allowed recovery at all, have held that the innocent coinsured may only recover one-half of the insurance proceeds, up to the policy limits.”³⁸³ Clearly, to resolve the dispute, the *Mistic* court did not carefully apply any traditional rules of contract construction and interpretation, such as the doctrine of plain meaning or the ambiguity doctrine.³⁸⁴ Arguably, that omission should raise some concern, because the term “one-half” does not appear in the “insurable interest” clause.³⁸⁵

374. *Id.*

375. *Id.*

376. *Id.*

377. *Id.* at 901.

378. *Id.*

379. *Id.* at 898.

380. *Id.*

381. *Id.* at 901.

382. *Id.*

383. *Id.* See also *Delph v. Potomac Ins. Co.*, 620 P.2d 1282, 1234 (N.M. 1980) (another community property state’s supreme court holding that the innocent spouse may collect only one-half of the insurance proceeds).

384. See *Mistic*, 822 P.2d at 901.

385. *Id.*

2. *Conflicting Declarations and Rulings in Separate Property States*

To be sure, courts in separate property states are seriously divided over whether first-party insurers must indemnify blameless co-insured spouses after deviant spouses destroy jointly owned residential or commercial property.³⁸⁶ A large group of courts have forced insurers to compensate innocent co-insured spouses for the latter's share of losses.³⁸⁷ However, an equally large number of courts in separate property states have declared that insurers have no contractual duty to indemnify innocent co-insured spouses.³⁸⁸ Significantly, the totality of several minor splits has produced the major split among courts in separate property jurisdictions.³⁸⁹

386. See discussion *infra* Part VII.A.2.

387. See *Hosey v. Seibels Bruce Group*, S.C. Ins. Co., 363 So. 2d 751, 754 (Ala. 1978); *Home Ins. Co. v. Pugh*, 286 So. 2d 49, 51-52 (Ala. Civ. App. 1973); *Republic Ins. Co. v. Jernigan*, 719 P.2d 331, 333-34 (Colo. Ct. App. 1985); *Steigler v. Ins. Co. of N. Am.*, 384 A.2d 398, 402 (Del. 1978); *Overton v. Progressive Ins. Co.*, 585 So. 2d 445, 449 (Fla. Dist. Ct. App. 1991); *Auto-Owners Ins. Co. v. Eddinger*, 366 So. 2d 123, 124 (Fla. Dist. Ct. App. 1979); *Fittje v. Calhoun County Mut. County Fire Ins. Co.*, 552 N.E.2d 353, 357 (Ill. App. Ct. 1990); *Econ. Fire & Cas. Co. v. Warren*, 390 N.E.2d 361, 363-64 (Ill. App. Ct. 1979); *Fuston v. Nat'l Mut. Ins. Co.*, 440 N.E.2d 751, 753-54 (Ind. Ct. App. 1982); *Am. Econ. Ins. Co. v. Liggett*, 426 N.E.2d 136, 140 (Ind. Ct. App. 1981); *Sager v. Farm Bureau Mut. Ins. Co.*, 680 N.W.2d 8, 16 (Iowa 2004); *Jensen v. Jefferson County Mut. Ins. Ass'n*, 510 N.W.2d 870, 872 (Iowa 1994); *Am. Hardware Mut. Ins. Co. v. Mitchell*, 870 S.W.2d 783, 785 (Ky. 1993); *Baker v. Commercial Union Ins. Co.*, 416 N.E.2d 187, 190 (Mass. 1981); *Hildebrand v. Holyoke Mut. Fire Ins. Co.*, 386 A.2d 329, 331 (Me. 1978); *Morgan v. Cincinnati Ins. Co.*, 307 N.W.2d 53, 60-61 (Mich. 1981); *Williams v. Auto Club Group Ins. Co.*, 569 N.W.2d 403, 405-06 (Mich. Ct. App. 1997); *Brown v. Frankenmuth Mut. Ins. Co.*, 468 N.W.2d 243, 247 (Mich. Ct. App. 1991); *Ramon v. Farm Bureau Ins. Co.*, 457 N.W.2d 90, 95 (Mich. Ct. App. 1990); *Lewis v. Homeowners Ins. Co.*, 432 N.W.2d 334, 337 (Mich. Ct. App. 1988); *Watson v. United Servs. Auto. Ass'n*, 566 N.W.2d 683, 692 (Minn. 1997); *McGory v. Allstate Ins. Co.*, 527 So. 2d 632, 640 (Miss. 1988); *DePalma v. Bates County Mut. Ins. Co.*, 24 S.W.3d 766, 770 (Mo. Ct. App. 2000); *Howell v. Ohio Cas. Ins. Co.*, 327 A.2d 240, 244 (N.J. Super. Ct. Div. 1974); *Goldner v. Kemper Ins. Co.*, 544 N.Y.S.2d 396, 397 (N.Y. App. Div. 1989); *Krupp v. Aetna Life & Cas. Co.*, 479 N.Y.S.2d 992, 998 (N.Y. App. Div. 1984); *Nationwide Mut. Fire Ins. Co. v. Pittman*, 348 S.E.2d 350, 351 (N.C. Ct. App., 1986); *Maravich v. Aetna Life & Cas. Co.*, 504 A.2d 896, 907-08 (Pa. Super. Ct. 1986); *McCracken v. Gov't Employees Ins. Co.*, 325 S.E.2d 62, 64 (S.C. 1985); *Ryan v. MFA Mut. Ins. Co.*, 610 S.W.2d 428, 437 (Tenn. Ct. App. 1980); *Error v. W. Home Ins. Co.*, 762 P.2d 1077, 1080 (Utah 1988); *Rockingham Mut. Ins. Co. v. Hummel*, 250 S.E.2d 774, 806-07 (Va. 1979); see also, *McFarland v. Utica Fire Ins. Co. of Oneida County, N.Y.*, No. 93-7936, 1994 WL 16464174, at *7 (5th Cir. 1994) (citing Mississippi's law); *Mich. Millers Mut. Ins. Corp. v. Benfield*, 140 F.3d 915, 926 (11th Cir. 1998); *Haynes v. Hanover Ins. Cos.*, 783 F.2d 136, 138 (8th Cir. 1986).

388. See *Am. Family Mut. Ins. Co. v. Bowser*, 779 P.2d 1376, 1382 (Colo. Ct. App. 1989); *Richards v. Hanover Ins. Co.*, 299 S.E.2d 561, 563-64 (Ga. 1983); *Aurelius v. State Farm Fire & Cas. Co.*, 894 N.E.2d 765, 772-73 (Ill. App. Ct. 2008); *Vance v. Pekin Ins. Co.*, 457 N.W.2d 589, 593 (Iowa 1990); *St. Paul Fire & Marine Ins. Co. v. Molloy*, 433 A.2d 1135, 1142 (Md. 1981); *Kosior v. Cont'l Ins. Co.*, 13 N.E.2d 423, 425 (Mass. 1938); *Simon v. Sec. Ins. Co.*, 210 N.W.2d 322, 327 (Mich. 1973); *Ijames v. Republic Ins. Co.*, 190 N.W.2d 366, 369-70 (Mich. Ct. App. 1971); *Childers v. State Farm Fire & Cas. Co.*, 799 S.W. 2d 138, 141-42 (Mo. Ct. App. 1990); *Woodhouse v. Farmers Union Mut. Ins. Co.*, 785 P.2d 192, 194 (Mont. 1990); *Fernandez v. Cigna Prop. & Cas. Ins. Co.*, 590 N.Y.S.2d 925, 928 (N.Y. App. Div. 1992); *Samhammer v. Home Mut. Ins. Co. of Binghamton*, 507 N.Y.S.2d 499, 503 (N.Y. App. Div. 1986); *Short v. Okla. Farmers Union Ins. Co.*, 619 P.2d 588, 591 (Okla. 1980); *Knauber v. Cont'l Ins. Cos.*, 435 A.2d 217, 218-19 (Pa. Super. Ct. 1981); *Dolcy v. R.I. Joint Reinsurance Ass'n*, 589 A.2d 313, 316 (R.I. 1991); *Coop. Fire Ins. Ass'n of Vt. v. Domina*, 399 A.2d 502, 503 (Vt. 1979); *Utah Farm Bureau Ins. Co. v. Crook*, 980 P.2d 685, 689 (Utah 1999); see also *Hall*

For example, some courts in separate property jurisdictions decide in favor of the innocent spouse or indemnity insurers depending on the types of property interests insured under the contract.³⁹⁰ Consider, for example, cases in which spouses jointly owned their insured property as “tenants by the entirety.”³⁹¹ The supreme courts of Virginia, Vermont, and Oklahoma have declared that an innocent co-insured spouse may not recover under a first-party property insurance contract if a deviant spouse destroys property of tenancy by the entirety.³⁹² Conversely, in other tenancy by the entirety cases, appellate courts in New Jersey and Indiana have decided differently, ruling in favor of innocent co-insured spouses.³⁹³

In addition, courts in separate property states are also divided over whether insurers must compensate innocent co-insured spouses after deviant spouses destroy tenancy in common property.³⁹⁴ This type of property interest allows one to sell one’s share or leave it in a will without the consent of other owners.³⁹⁵ As an example, if an individual dies without a will, his share goes to his heirs rather than to the other owners.³⁹⁶ Of course, deviant husbands or wives may destroy, and have destroyed,

v. State Farm Fire & Cas. Co., 937 F.2d 210, 214-15 (5th Cir. 1991) (citing Mississippi’s law); Sales v. State Farm Fire & Cas. Co., 849 F.2d 1383, 1385 (11th Cir. 1988) (citing Georgia’s law.); Spezialetti v. Pac. Employers Ins. Co., 759 F.2d 1139, 1140 (3d Cir. 1985) (citing Pennsylvania’s law).

389. See *supra* text accompanying notes 386-88.

390. See *infra* text accompanying notes 391-407.

391. See, e.g., Lunnan v. Hunter, 35 A.2d 292, 294 (Pa. 1944) “Tenancy by entireties is a venerable institution of the common law: it rests upon instincts which form the very warp and woof of our domestic and social fabric. In such a tenancy each spouse is seized per tout et non per my. There is but one legal estate, which, by a long course of judicial decisions, has been buttressed against inroads attempted either by the parties themselves or by their individual creditors.” *Id.*

392. See Short v. Okla. Farmer’s Union Ins. Co., 619 P.2d 588, 589 (Okla. 1980) (observing that the husband and wife owned the fire-damage house “in joint tenancy” and concluding that fraud or false swearing by either party voids the entire insurance contract); Coop. Fire Ins. Assoc. of Vt. v. Domina, 399 A.2d 502, 503 (Vt. 1979) (“One tenant by entirety cannot sever the tenancy by deed, as a joint tenant can”); Rockingham Mut. Ins. Co. v. Hummel, 250 S.E.2d 774, 776 (Va. 1979) (noting that the legal interest of a married couple with a tenancy by the entirety under the insurance contract was not severable, but joint).

393. See Am. Econ. Ins. Co. v. Liggett, 426 N.E.2d 136, 140 (Ind. Ct. App. 1981) (“The legal fiction of the entireties’ estate in real estate is designed for the protection of the spouses and the marriage. It was initially designed to prevent the individual creditors of either spouse from taking the marital home. The courts generally, and divorce courts in particular, find no difficulty in dividing an entireties estate. I find it a perversion of this legal fiction, designed to protect the spouses’ rights and marital property, to use it to destroy the property rights of an innocent spouse.”); Howell v. Ohio Cas. Ins. Co., 327 A.2d 240, 242 (N.J. Super. Ct. App. Div. 1974) (concluding that the husband’s fraud was no bar to the innocent wife’s recovery under the policy, but reaching that “result irrespective of whether the interests of the wife and husband in the tenancy by the entirety, in the personal property, or in the contract rights under the policy are deemed to be joint or several. The significant factor is that the responsibility or liability for the fraud—here, the arson—is several and separate rather than joint, and the husband’s fraud cannot be attributed or imputed to the wife who is not implicated therein.”).

394. See generally Burbach v. Sussex County Mun. Utils. Auth., 723 A.2d 137, 140 (N.J. Super. Ct. App. Div. 1999) (stating that a “tenant in common by definition has an undivided interest in the whole, that is, an interest that encompasses the entire property.”).

395. See *id.*

396. See *id.*

tenancy in common property before death.³⁹⁷ When such destruction has occurred, some courts in separate property states have allowed innocent spouses to collect insurance proceeds.³⁹⁸ Other courts have not.³⁹⁹

In addition, whether innocent co-insured spouses may recover all or just half of the proceeds under property insurance contracts also generates a considerable number of conflicting rulings among courts in separate property states.⁴⁰⁰ Reconsider the holding in *Mistic*: An innocent co-insured spouse may only recover one-half of the insurance proceeds, up to the policy limit, after a deviant co-insured spouse destroys jointly owned property.⁴⁰¹ A significant number of courts in separate property states embraced the *Mistic* rule.⁴⁰² But other state courts in those jurisdictions have permitted innocent spouses to receive a full recovery up to the policy limits.⁴⁰³ Like their counterparts in community property states, courts in separate property states give all sorts of explanations for compelling

397. See *Hoyt v. N.H. Fire Ins. Co.*, 29 A.2d 121, 122-23 (N. H. 1942).

398. See *id.* The tenants in common have individual interests in the insurance policy because courts construe an insurance contract according to what a reasonable person would have thought, "not what the insurance company intended the words of the policy to mean." *Id.*

399. See, e.g., *Monaghan v. Agric. Fire Ins. Co.*, 18 N.W. 797, 804 (Mich. 1884) (concluding that a deviant co-insured's attempt to defraud the insurance company by making false affidavits in relation to loss property is a complete bar to innocent co-insureds' recovery under the policy); see also *Klemens v. Badger Mut. Ins. Co.*, 99 N.W.2d 865, 866 (Wis. 1959) (a supreme court in a community property state embracing the proposition that an innocent joint tenant may not recover proceeds under a fire insurance contract if a deviant co-insured joint tenant set fire to the property). But see *Watts v. Farmers Ins. Exch.*, 120 Cal. Rptr. 2d 694, 705-06 (Cal. Ct. App. 2002) ("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.") (emphasis added).

400. See, e.g., *Atlas Assur. Co. of Am. v. Mistic*, 822 P.2d 897, 901 (Alaska 1991).

401. *Id.*

402. See, e.g., *Commercial Union Ins. Co. v. State Farm Fire & Cas. Co.*, 546 F. Supp. 543, 547 (D. Colo. 1982) (applying Colorado's law); *Republic Ins. Co. v. Jernigan*, 719 P.2d 331, 333 (Colo. Ct. App. 1985); *Steigler v. Ins. Co. of N. Am.*, 384 A.2d 398, 402 (Del. 1978); *Econ. Fire & Casualty Co. v. Warren*, 390 N.E.2d 361, 364 (Ill. App. Ct. 1979); *Fuston v. Nat'l Mut. Ins. Co.*, 440 N.E.2d 751, 754 (Ind. Ct. App. 1982); *St. Paul Fire & Marine Ins. Co. v. Molloy*, 433 A.2d 1135, 1144 (Md. 1981); *Lewis v. Homeowners Ins. Co.*, 432 N.W.2d 334, 337 (Mich. Ct. App. 1988); *Krupp v. Aetna Life & Casualty Co.*, 479 N.Y.S.2d 992, 998 (N.Y. App. Div. 1984); *Winter v. Aetna Cas. & Sur. Co.*, 409 N.Y.S.2d 85, 88 (N.Y. App. Div. 1978); *Lovell v. Rowan Mut. Fire Ins. Co.*, 274 S.E.2d 170, 174 (N.C. 1981); *Nationwide Mut. Fire Ins. Co. v. Pittman*, 348 S.E.2d 350, 351 (N.C. Ct. App. 1986); *Maravich v. Aetna Life & Cas. Co.*, 504 A.2d 896, 907 (Pa. Super. Ct. 1986).

403. See, e.g., *Am. Econ. Ins. Co. v. Liggett*, 426 N.E.2d 136, 145 (Ind. Ct. App. 1981); *Hildebrand v. Holyoke Mut. Fire Ins. Co.*, 386 A.2d 329, 332 (Me. 1978) (allowing the innocent wife to recover fully after co-insured husband set the house on fire because public policy against permitting a wrongdoer to benefit was not violated by making the insurer pay); *Howell v. Ohio Cas. Ins. Co.*, 327 A.2d 240, 244 (N.J. Super. Ct. App. Div. 1974) (concluding that the wife was entitled to recover one-half of the loss of personal property and the entire additional living expenses).

insurers to pay only one-half or all insurance proceeds within the policy limits.⁴⁰⁴

Finally, split decisions also appear between innocent spouse rulings that originate, respectively, in separate property and community property state courts.⁴⁰⁵ Those “between jurisdictions” splits have occurred, even when (1) the probative facts in the respective controversies were fairly similar; (2) courts in separate and community states performed reasonably similar analyses; and (3) community and separate property state courts applied the same equitable doctrines.⁴⁰⁶ To illustrate, consider the facts and outcomes in innocent spouse controversies that were decided in Wisconsin and Massachusetts.⁴⁰⁷

Hedtcke v. Sentry Insurance Co. was decided in Wisconsin, a community property jurisdiction.⁴⁰⁸ In *Hedtcke*, Judith and Ronald Hedtcke were married and jointly owned the residential property.⁴⁰⁹ Sentry insured the property and promised to indemnify if and when fire, the peril insured against, damaged or destroyed the house.⁴¹⁰ During the policy’s period, a fire destroyed the property.⁴¹¹ Robert was the culprit, and he torched the property when Judith did not occupy the house.⁴¹² Judith asked the insurer to indemnify, the insurer refused, and Judith sued. Ultimately, the Wisconsin Supreme Court ruled in her favor.⁴¹³ To reach its conclusion, the supreme court declared that permitting an innocent co-insured spouse to recovery when a deviant co-insured destroys jointly owned property “preserves the essence of the legal principles . . . and produces an equitable result.”⁴¹⁴

Now, consider the brief facts and ruling *Kosior v. Continental Insurance Co.*⁴¹⁵ John and Tofeld Kosior were husband and wife, and they

404. See, e.g., *Republic Ins. Co. v. Jernigan*, 719 P.2d 331, 333-34 (Colo. Ct. App. 1985) (“Exclusionary clauses in insurance contracts must be interpreted in favor of the insured. . . . [The innocent co-insured] may recover up to a one-half interest in the property, i.e., one-half of the value of the damaged dwelling, other structures, and personal property; limited of course by the total policy limits.”); *Steigler v. Ins. Co. of N. Am.*, 384 A.2d 398, 402 (Del. 1978) (“[T]he rights of husband and wife [are] separate under the contract and, . . . both logic and justice require that the amount recoverable be likewise allocated. . . . [The innocent co-insured wife could recover only] one-half of the damages within the limits of the contract.”); *Am. Econ. Ins. Co. v. Liggett*, 426 N.E.2d 136, 140 (Ind. Ct. App. 1981) (citing public policy and permitting the innocent co-insured spouse full recovery under the policy since her husband died in the fire and there was no way to prove he caused it).

405. See discussion *supra* Part II.

406. See discussion *supra* Part II.

407. See *Kosior v. Cont’l Ins. Co.*, 13 N.E.2d 423 (Mass. 1938); *Hedtcke v. Sentry Ins. Co.*, 326 N.W.2d 727 (Wis. 1982).

408. *Hedtcke*, 326 N.W.2d at 729.

409. *Id.*

410. *Id.*

411. *Id.* at 729-30.

412. *Id.* at 729.

413. *Id.* at 738-40.

414. *Id.* at 738.

415. *Kosior v. Cont’l Ins. Co.*, 13 N.E.2d 423 (Mass. 1938).

owned buildings as tenants in common.⁴¹⁶ Continental Insurance Company (Continental) and two other insurers insured the buildings against fire.⁴¹⁷ The Kosiors were co-insured spouses under each insurance contract.⁴¹⁸ After securing the insurance, John intentionally burned the buildings.⁴¹⁹ Although conceding that her husband's deviant act voided the fire insurance policies, Tofeld still asked Continental to reimburse her for her share of the loss.⁴²⁰ Like the insurer in *Hedtcke*, Continental refused.⁴²¹

In response, the innocent co-insured Tofeld commenced an action in equity "to recover the amount [that Continental] justly and equitably [owed her under the first-party, property insurance contract]."⁴²² Stated slightly differently, citing the court's equity powers, she asked the lower court to declare that the insurers had a duty to indemnify her.⁴²³ The Supreme Judicial Court of Massachusetts rejected Tofeld's claim and reinforced the lower court's equitable powers and ruling.⁴²⁴ The Massachusetts Supreme Judicial Court concluded that the deviant husband's "burning the insured buildings was an act of the 'insured,' and as such it was fraud upon the [insurer and] . . . rendered the policies void in accordance with their terms."⁴²⁵

B. Whether Property Insurers Have a Duty to Indemnify Other Innocent Co-insured Fiduciaries

Like many innocent co-insured spouses, other fiduciaries also submit claims to property insurers after their deviant co-owners intentionally destroy or diminish the market value of jointly owned tangible or intangible property. Quite often, indemnity insurers refuse to compensate those innocent co-insureds: partnerships, partners, joint venturers, executors and administrators of estates, corporations, corporate officials, and corporate directors.⁴²⁶ As a consequence, "commercial" fiduciaries must spend out-of-pocket dollars to cover destroyed or diminished property interests under their control or supervision.⁴²⁷ Whether first-party property insurers have a contractual duty to indemnify innocent co-insured "commercial" fiduciaries generates a considerable amount of disagreement among state courts

416. *Id.* at 424.

417. *Id.* at 423-24.

418. *Id.* at 423.

419. *Id.* at 424.

420. *Id.*

421. *Id.*; *Hedtcke v. Sentry Ins. Co.*, 326 N.W. 2d 727, 729 (Wis. 1982).

422. *Kosior*, 13 N.E.2d at 424.

423. *Id.*

424. *Id.* at 425.

425. *Id.* (emphasis added).

426. *Id.*

427. *Id.*

located within and beyond both community and separate property states.⁴²⁸ To illustrate this point, a review of a few cases in which co-insured corporations asked insurers to indemnify them after various deviant co-insureds destroyed corporate interests might be helpful.⁴²⁹

First, consider the controversy in *Hoosier Insurance Co. v. North South Trucking Supplies, Inc.*⁴³⁰ Lisa Shoemaker's husband died in an automobile accident, and she received approximately \$160,000 from the insurer.⁴³¹ Later, Scott Casey (Lisa's boyfriend) and Scott's parents (John Norman (Norman) and Carol Casey), decided to purchase and operate a business that sold supplies to truck stops.⁴³² Lisa invested \$70,000 in the enterprise.⁴³³ Norman did not have cash to invest in the business so he supplied a building.⁴³⁴ They named the new company North South Trucking Company (North South).

Respectively, Lisa and Norman were president and secretary of North South.⁴³⁵ Lisa owned 100 percent of the company's shares, leaving no other party with any property interest in the corporation.⁴³⁶ Lisa knew very little about the supply business.⁴³⁷ Even more relevant, Norman never sought Lisa's approval or informed consent before making important corporate decisions.⁴³⁸ He wrote most of the checks, performed the accounting for the business, monitored the accounts payable and receivable, determined the types and amount of inventory that North South would order, and insured North South's inventory for \$95,000 under a property insurance contract.⁴³⁹ Hoosier Insurance Company (Hoosier) was the insurer.⁴⁴⁰

Less than a month after purchasing the property insurance on behalf of the corporation, a fire damaged a large portion of the building that contained North South's inventory.⁴⁴¹ The fire damaged a large portion of the house and the attached block warehouse as well.⁴⁴² Norman was the suspected arsonist.⁴⁴³ He submitted a proof-of-loss form, claiming that the actual cash value of the property at the time of the loss was \$101,124.86.⁴⁴⁴

428. *Id.*

429. *Id.*

430. *Hoosier Ins. Co. v. N.S. Trucking Supplies, Inc.*, 684 N.E.2d 1164 (Ind. Ct. App. 1997).

431. *Id.* at 1166.

432. *Id.*

433. *Id.*

434. *Id.*

435. *Id.*

436. *Id.*

437. *Id.*

438. *Id.*

439. *Id.* at 1166-67.

440. *Id.* at 1167.

441. *Id.*

442. *Id.*

443. *Id.*

444. *Id.*

After an investigation, a certified public account (CPA) concluded that the inventory's fair market value was \$36,000.⁴⁴⁵ Hoosier denied the claim, asserting that Norman intentionally set the fire.⁴⁴⁶ Additionally, the insurer concluded that Norman and Lisa breached a condition subsequent by misrepresenting the actual value of the destroyed property.⁴⁴⁷

Ultimately, the case went to trial and a jury returned a verdict in favor of North South.⁴⁴⁸ They awarded the innocent co-insured corporation \$36,175.⁴⁴⁹ After the judge entered the judgment and denied Hoosier's motion for judgment on the evidence, Hoosier appealed.⁴⁵⁰ Before the Indiana Court of Appeals, the insurer argued that the trial court committed reversible error.⁴⁵¹ To reach a just result, the court of appeals had to determine whether the actual or presumed arsonist, Norman, exercised absolute control over the corporation or whether he would benefit after torching North South's inventory.⁴⁵²

Based on the evidence, the appellate court concluded that "North South as a corporation neither explicitly authorized Norman's acts nor implicitly ratified them by allowing him to dominate corporate affairs."⁴⁵³ The Appellate Court of Indiana also embraced the jury's finding that Norman would "not benefit in any way from North South's recovery of the insurance proceeds."⁴⁵⁴ Thus, in light of the jury's findings, the court affirmed the lower court's ruling, concluding that the property insurer had a duty to indemnify the co-insured corporation for its deviant co-fiduciary's destructive act.⁴⁵⁵ Also, in *Fidelity-Phenix Fire Insurance Co. of N.Y. v. Queen City Bus & Transfer Co.* and in *Erlin-Lawler Enters., Inc. v. Fire Insurance Exchange*, the Fourth Circuit Court of Appeals and a California's appellate court also have embraced the reasoning and holding in *Hoosier*.⁴⁵⁶

445. *Id.*

446. *Id.*

447. *Id.* The insurer concluded that Norman and Lisa violated the "Concealment, Misrepresentation or Fraud" clause in the North South's insurance contract policy. *Id.* That clause read: "We will not pay for any loss or damage in any case of: (1) Concealment or misrepresentation of a material fact or, (2) Fraud committed by an insured at any time and relating to a claim under this policy." *Id.*

448. *Id.*

449. *Id.*

450. *Id.*

451. *Id.* at 1167-68.

452. *Id.* at 1169.

453. *Id.* at 1172.

454. *Id.* ("Lisa was the sole stockholder of the corporation. Norman owned no ownership interest in the corporation. Moreover, Norman was terminated as secretary of the corporation Thus, Norman will receive no direct or indirect benefit from his wrongdoing.").

455. *Id.*

456. *Fidelity-Phenix Fire Ins. Co. of N.Y. v. Queen City Bus & Transfer Co.*, 3 F.2d 784 (4th Cir. 1925). A co-insured corporation challenged the trial court's conclusion that it was precluded from recovering under a fire insurance contract, since the deviant fiduciary, the arsonist and a 50% stockholder, was the corporation's "alter ego." *Erlin-Lawler Enters., Inc. v. Fire Ins. Exch.*, 73 Cal. Rptr. 182, 186-87 (1968). The appellate court did not embrace that conclusion. *Id.* Even though the

On the other hand, courts in Georgia, Delaware, Illinois, Michigan, Nebraska, New Jersey, and Oregon have performed a fairly similar “dominance and control” analysis like the one appearing in *Hoosier*.⁴⁵⁷ Those tribunals have concluded that innocent co-insured corporations may not recover property insurance proceeds after co-insured fiduciaries—shareholders, officers and directors—destroy or diminish the value of corporate property.⁴⁵⁸ To underscore the severity of this particular split involving the rights of innocent and co-insured corporations, the Fourth Circuit’s holding in *Fidelity-Phenix* conflicts with its holding in *Kimball Ice Co. v. Hartford Fire Insurance Co.*⁴⁵⁹

As discussed earlier, trustees, executors, administrators, and partners are fiduciaries; they have a collective duty to protect and preserve assets on behalf of other persons or fiduciaries.⁴⁶⁰ Frequently, they are co-insureds

arsonist stood to benefit up to 50% of the recovery, that single fact apparently was not determinative. *Id.*

457. See *Sandersville Oil Mill Co. v. Globe & Rutgers Fire Ins. Co.*, 124 S.E. 728, 728-29 (Ga. App. 1924) (concluding that the insurer is liable under a property insurance contract if negligence rather than fraud produced a fire that destroyed corporate property, but barring a corporation’s recovery if its innocent stockholders will not actually realize any benefit because of the insolvent state of the corporation); *N. Assurance Co. v. Rachlin Clothes Shop Inc.*, 125 A. 184, 187-88, 190 (Del. 1924) (concluding that if an officer or stockholder has absolute control in the conduct of the business of a corporation, his acts, if he acts on behalf of the corporation, become the acts of the corporation barring it from recovery even though he is not the dominant shareholder); see also *Felsenthal Co. v. N. Assurance Co.*, 120 N.E. 268, 271 (Ill. 1918) (“When . . . the beneficial owner of practically all of the stock in a corporation, and who has the absolute management and control of its affairs and its property, . . . sets fire to the property of a corporation or causes it to be done, there is no sound reason to support the contention . . . that the corporation should be allowed to recover on a policy for the destruction of the corporate property by a fire . . .”); *United Gratiot Furniture Mart, Inc. v. Mich. Basic Prop. Ins.*, 406 N.W.2d 239, 242 (Mich. Ct. App. 1987) (finding no reversible error, the court concluded that the jury properly applied the “dominance and control” test and embraced the jury’s finding that a deviant co-insured shareholder destroyed corporate property, thus precluding the innocent corporation’s receiving of insurance proceeds); *Cont’l Ins. Co. v. Gustav’s Stable Club Inc.*, 317 N.W.2d 734, 740 (Neb. 1982) (declaring that an innocent co-insured corporation may not recover under a fire insurance contract if the co-fiduciary incendiary or arsonist owned half of the stocks and was the dominant manager of corporate property); *Miller & Dobrin Furniture Co. v. Camden Fire Ins. Co. Assn.*, 150 A.2d 276, 284 (N.J. Super. 1959) (holding that the corporation could not recover where a 50% shareholder, the secretary-treasurer and director, exercised dominant control over and management of the corporation. In addition, although the business was being conducted under the guise of a corporation, the court declared that it was in fact a partnership, and applied partnership rule to reach its conclusion.); *Minn. Bond Ltd. v. St. Paul Mercury Ins. Co.*, 706 P.2d 942, 944 (Or. 1985) (holding that the innocent co-insured corporation may not recover for arson, which 50% shareholder officer committed, because the co-fiduciary’s deviant act was excluded under the property-insurance contract and the coverage provision for employee dishonesty did not apply).

458. See *supra* note 457.

459. Compare *Fidelity-Phenix Fire Ins. Co. of N. Y. v. Queen City Bus & Transfer Co.*, 3 F.2d 784, 785 (4th Cir. 1925) (allowing the innocent co-insured corporation to recover proceeds), with *Kimball Ice Co. v. Hartford Ins. Co.*, 18 F.2d 563, 564-66 (4th Cir. 1927) (concluding that the innocent corporation could not recover proceeds under a fire insurance contract where the allegedly deviant corporate manager owned one-fourth of the corporate stock and had complete control and management of the corporation).

460. See *supra* Part II.

under property insurance contracts.⁴⁶¹ As a consequence, judicial conflicts have arisen over whether property insurers have a duty to indemnify blameless trusts/trustees and partnerships/partners after deviant co-fiduciaries intentionally destroy or waste various property interests.⁴⁶² A brief consideration of multiple rulings involving trusts and partnerships should illustrate the extent of the conflicts on several dimensions.⁴⁶³

First, consider the facts and holding in *Giacobetti v. Insurance Placement Facility of Pennsylvania*.⁴⁶⁴ Louis Manusov owned a building which was a combination of a home and a grocery store.⁴⁶⁵ He conveyed the building along with the land on which it was situated to seven named trustees: himself, his sister Freda Kracoff, his brother-in-law Charles Kracoff, and four nieces and nephews—Harry Kracoff, Doris Kracoff, Sara Stark, and Nathan Petrushansky (the Manusov Family Trust).⁴⁶⁶ Under the terms of a deed of trust, “the Trust [would] terminate upon the death of the last survivor of the designated trustees, at which time title [would] ‘vest absolutely in fee simple to the children or issue of said designated Trustees, share and share alike, per capita, and not per stirpes.’”⁴⁶⁷

When the deed of trust was executed, Manusov’s brother-in-law, Charles Kracoff, operated the grocery store under a lease agreement with Manusov.⁴⁶⁸ About twenty years after the formation of the trust, Louis Manusov, Freda Kracoff, and Charles Kracoff died.⁴⁶⁹ Therefore, Harry Kracoff, Manusov’s nephew, assumed all responsibilities and began to operate the grocery store.⁴⁷⁰ Harry Kracoff’s father and prior lessee, Charles Kracoff, owned part of the contents in the grocery store, including equipment and improvements.⁴⁷¹ The trustees of the trust that Charles Kracoff identified in his will owned the title to those contents.⁴⁷² Harry

461. See *supra* Part II.

462. See *infra* text accompanying notes 464-547.

463. See *infra* text accompanying notes 464-547.

464. *Giacobetti v. Ins. Placement of Pa.*, 457 A.2d 853 (Pa. 1983).

465. *Id.* at 854.

466. *Id.* Under the terms of the trust, Manusov personally received \$200 per month for the rest of his life. *Id.* The trust paid \$300 per year “[t]o each of the Grantees or their survivors and successors.” *Id.* The trust also paid up to \$50 per week to ‘Grantees, Trustees, or their issue or any member of their respective families . . . in the event of sickness or need’ . . . \$1,000 as a wedding gift to each trustee’s child who should marry.” *Id.* (quoting the Manusov Family Trust agreement).

467. *Id.* “Manusov also directed that ‘rent, income and profits’ from the premises were to be applied to ‘taxes, insurance, cost of maintenance and other expenses in connection with the management of said property.’” *Id.* (quoting the Manusov Family Trust agreement).

468. *Id.*

469. *Id.*

470. *Id.*

471. *Id.*

472. *Id.* “The trustees were Harry Kracoff, Dora Kracoff, Sara Stark, and Nathan Petrushansky, the four remaining co-trustees of the Manusov Family Trust.” *Id.*

Kracoff owned the remainder of the grocery store's contents and inventories.⁴⁷³

After he began to operate the store, Harry Kracoff purchased a fire insurance contract from Insurance Placement Facility of Philadelphia (IPFP).⁴⁷⁴ The policy covered the building which housed the grocery store, and the policy limit was \$50,000.⁴⁷⁵ A separate clause in the insurance contract covered the contents of the food market.⁴⁷⁶ Under the latter clause, IPFP's maximum exposure would be \$100,000 if a loss occurred.⁴⁷⁷

A fire destroyed the building and its contents, and Harry Kracoff submitted timely, sworn proofs of loss.⁴⁷⁸ Although Kracoff reported that the fire's origin was "unknown to insured," IPFP determined that Harry Kracoff started the fire.⁴⁷⁹ Consequently, the property insurer refused to indemnify.⁴⁸⁰ Responding to the insurer's rejection, Harry Kracoff, Doris Kracoff, Sara Stark, and Nathan Petrushansky sued IPFP.⁴⁸¹ Two claims appeared in their complaint.⁴⁸² First, as "Trustees of [the] Manusov Family Trust," the four complainants asserted that IPFP had a duty to pay \$50,000 to cover the destroyed building.⁴⁸³ Also, as "Trustees Under the Will of Charles Kracoff," they argued that IPFP had a contractual obligation to pay \$100,000 to cover the building's destroyed contents.⁴⁸⁴ Harry Kracoff also sued individually and on behalf of himself "in his own right."⁴⁸⁵

Shortly before trial, Nathan Petrushansky, one of the co-trustees, died.⁴⁸⁶ Even more significant, before the trial commenced, Harry Kracoff resigned as a trustee of the Manusov Family Trust.⁴⁸⁷ His resignation was "effective immediately."⁴⁸⁸ Additionally, Harry Kracoff executed a "Release and Disclaimer" that read as follows: "[I renounce and disclaim]

473. *Id.*

474. *Id.*

475. *Id.*

476. *Id.*

477. *Id.*

478. *Id.* at 855.

479. *Id.*

480. *Id.*

IPFP] filed an answer and new matter, the latter of which averred that in the sworn proofs of loss Harry Kracoff had deliberately concealed the true origin of the fire with intent to defraud [IPFP], in violation of the "Concealment, Fraud" provision of the insurance policy. [IPFP] further averred that it was not liable for the losses under the "Perils Not Included" clause, and added that plaintiffs had, "in fact, intentionally and deliberately caused or contributed to the cause of such fire and any consequent loss."

Id.

481. *Id.*

482. *Id.*

483. *Id.*

484. *Id.*

485. *Id.*

486. *Id.* at 856.

487. *Id.* at 855-56.

488. *Id.* at 856.

'all right[s], title and interest of any kind which I ever had, now have or may have in the future in said Trust as a beneficiary thereof.'"489 In the end, Doris Kracoff and Sara Stark were the only remaining and innocent co-trustees of the Manusov Family Trust.⁴⁹⁰

During the bench trial, the court of common pleas rejected Harry Kracoff's assertion that "an angry outside person" started the fire.⁴⁹¹ Instead, the lower court found that Harry Kracoff started the fire.⁴⁹² Therefore, imputing Harry Kracoff's deviance to the innocent co-trustees under the Manusov Family Trust, the court of common pleas declared that IPFP did not have to indemnify the innocent co-insured trustees.⁴⁹³

After they did not prevail, the remaining trustees, Doris Kracoff and Sara Stark, resigned as trustees.⁴⁹⁴ As a consequence, the Orphans' Court Division of the Court of Common Pleas of Philadelphia "granted a petition for the appointment of a substituted trustee to prosecute an appeal."⁴⁹⁵ The substituted trustee was Attorney Alexander B. Giacobetti.⁴⁹⁶ After an appellate court affirmed the trial court's ruling, Giacobetti appealed to the Pennsylvania Supreme Court.⁴⁹⁷

At the outset, Pennsylvania's highest court embraced the lower court's finding that Harry Kracoff's deviance prevented him "from sharing in the proceeds of the fire insurance policy."⁴⁹⁸ Harry's criminal act also prevented his "children or issue," beneficiaries under the Manusov Family Trust, from receiving any insurance proceeds because Harry would benefit from their bounty.⁴⁹⁹ On the other hand, the Pennsylvania Supreme rejected the lower court's conclusion that IPFP had no duty to indemnify the remaining innocent co-insured trustees and beneficiaries under the Manusov Family Trust.⁵⁰⁰

489. *Id.*

490. *Id.*

491. *Id.*

492. *Id.*

493. *See id.*

494. *Id.*

495. *Id.* "The petition was filed by John D. Lucey, Jr., Esquire, who had been appointed as guardian and trustee ad litem to represent minor and unascertained interests in proceedings initiated by the former co-trustees to terminate the Manusov Family Trust. The record makes no mention of the status of the proceedings to terminate the Trust." *Id.* at n.6.

496. *Id.* at 856.

497. *Id.*

498. *Id.*

499. *Id.* at 856-57. "[IPFP's] right to retain the shares of Harry Kracoff and his 'children or issue' is in no respect dependent upon [Harry Kracoff's] 'Release and Disclaimer' . . . [on the day] . . . he resigned as trustee. Rather, [IPFP's] right to retain these shares gives full effect to 'the common law principle that a person will not be permitted to profit by his own wrong, particularly his own crime.'" *Id.* at 857 (quoting Greifer Estate, 5 A.2d 118, 119 (Pa. 1939)).

500. *Id.* at 857.

The *Giacobetti* court's own words are instructive and they cogently summarize the court's reason for ruling in favor of the innocent trustees and beneficiary.⁵⁰¹ The Pennsylvania Supreme Court wrote:

[T]he wrongful conduct of Harry Kracoff may not fairly be imputed to the entire Trust, as nothing in the trust instrument even remotely contemplated that any portion of the corpus might be deliberately destroyed by fire. Nor may Harry Kracoff's wrongful conduct fairly be imputed to the other beneficiaries on the theory that they acquiesced in his assumption of control over the family's business affairs Although over the years of the administration of the Trust the other trustee-beneficiaries permitted Harry Kracoff to assume progressively more responsibilities under the Deed of Trust, including the responsibility to procure insurance on the trust property, . . . [IPFP] has failed to establish that Harry Kracoff became the agent of any of the other beneficiaries for all purposes The conduct of Harry Kracoff was wholly unilateral and in no way may be deemed to be an act of the Trust itself.⁵⁰²

Now, consider the facts and holding in *Mercantile Trust Co. v. New York Underwriters Insurance Co.*⁵⁰³ Herman Luer and his wife established a real estate trust comprising of two lots, a residential house, and other structures.⁵⁰⁴ Under the terms of the trust, the residential house was held for "Mrs. Luer's use during her life and then for the benefit of their son Edward D. Luer."⁵⁰⁵ Upon the death of Edward D. Luer, the trust estate was to go to his descendants.⁵⁰⁶ In addition, Herman Luer also created an income trust, under which Edward Luer was the sole intended beneficiary.⁵⁰⁷ The Mercantile Trust Company (Mercantile) was the trustee.⁵⁰⁸

After the Luers created the trusts, Edward Luer purchased a homeowner's insurance contract from New York Underwriters Insurance Company (Underwriters).⁵⁰⁹ The contract of insurance covered only the residential house and appurtenances.⁵¹⁰ Both Edward Luer and Mercantile, the trustee, were listed as the "named insureds."⁵¹¹ The policy limits under the contract were \$20,000 and \$8,000 for the house and its contents, respectively.⁵¹² Less than a year after purchasing the insurance, Edward

501. *See id.*

502. *Id.* at 857.

503. *Mercantile Trust Co. v. N.Y. Underwriters Ins. Co.*, 376 F.2d 502 (7th Cir. 1967).

504. *Id.* at 503.

505. *Id.*

506. *Id.*

507. *Id.*

508. *Id.*

509. *Id.*

510. *Id.*

511. *Id.* "On the face of the policy, the insured were shown as 'Mercantile Trust Company, trustee, under indenture of trust . . . and Edward D. Luer.'" *Id.*

512. *Id.* "Edward Luer (or his wife) purchased the homeowner's policy and paid the premiums . . .

Luers moved 75% of his household goods to a storage company in Illinois and drove to Golden, Colorado.⁵¹³ A few days later, a loud explosion occurred in his house and it burned to the ground.⁵¹⁴

The trustee, Mercantile, asked Underwriters to pay \$20,000 to cover the destroyed house.⁵¹⁵ Luer submitted a claim for \$8,000, and he asked Underwriters to cover the household contents which were not transferred to storage.⁵¹⁶ The insurer denied both claims after discovering that Edward Luer had misrepresented the actual value of the inventory that he moved to storage before the fire.⁵¹⁷ Mercantile sued Underwriters.⁵¹⁸ After a bench trial, the United States District Court for the Northern District of Illinois decided in favor of Mercantile, and the Underwriters appealed.⁵¹⁹

Before the Seven Circuit Court of Appeals, Underwriters argued that the district court erroneously entered judgment for Mercantile.⁵²⁰ Conversely, the trustee stressed that the co-insured fiduciaries' rights and obligations under the property insurance contract were divisible.⁵²¹ The trustee admitted that Edward Luer was a deviant co-insured fiduciary.⁵²² But the trustee insisted that Edward's deviancy, fraudulently misrepresenting the true value of the stored furnishings, should not bar the trustee's recovery of the \$20,000.⁵²³ The Seventh Circuit accepted Mercantile's argument and ordered Underwriters to indemnify the trustee.⁵²⁴ Applying Illinois's law and citing the New Hampshire Supreme Court's language in *Hoyt v. New Hampshire Fire Insurance Co.*, the federal court of appeals wrote:

Mercantile's rights should not be defeated by any wrongful acts of Edward Luer 'The ordinary person owning an undivided interest in property, not versed in the nice distinctions of insurance law, would naturally

Mercantile . . . never paid any of the insurance costs." *Id.*

513. *Id.*

514. *Id.*

515. *Id.*

516. *Id.* at 503-04.

517. *Id.*

Luer presented an \$8,000 claim to Underwriters, enclosing a detailed, handwritten household inventory showing the total contents of the house as worth \$32,105.35. During the course of investigation of the origin of the fire, Edward Luer told Underwriters' arson investigator that the only object moved out of the residence before the fire was his son Frank D. Luer's bed. In an ensuing deposition in California, where Edward Luer [resided], he repeated the statement that only his son's bed had been moved out of the residence. His deposition was signed and sworn to before a notary public.

Id.

518. *Id.* at 503.

519. *Id.*

520. *Id.* at 504.

521. *Id.*

522. *Id.*

523. *Id.*

524. *Id.* at 506.

suppose that his individual interest in the property was covered by a policy which named him without qualification as one of the persons insured.' . . . Mercantile had no control over the property and was unaware of Edward Luer's misconduct Edward Luer had only a beneficial life interest in the property. We do not think that the Illinois courts would impute his fraud to the trustee or to his son Frank D. Luer, the innocent remainderman. Accordingly, the judgment of the district court is affirmed with the qualification that none of the proceeds of this policy on the dwelling house be expended for the benefit of Edward Luer.⁵²⁵

That the *Mercantile* court cited excerpts from the New Hampshire Supreme Court's decision in *Hoyt* is significant.⁵²⁶ In *Hoyt*, the complaining innocent fiduciaries were partners rather than trustees.⁵²⁷ Among partnership cases, *Hoyt*'s innocent fiduciary ruling is the minority rather than the majority position. Ernest E. Hoyt, Ernest L. Hoyt, and Walter J. Jacobsen were apparently co-partners and they owned a certain property as tenants in common.⁵²⁸

Six fire insurance contracts listed each partner as a named insured.⁵²⁹ The insurers were several other companies and New Hampshire Fire Insurance Company, collectively, NHFIC.⁵³⁰ While the policies were current, Ernest L. Hoyt intentionally set fire to the insured property, and the structure was completely destroyed.⁵³¹ An indictment charged him with arson and he pleaded guilty.⁵³² The other two co-insured partners did not participate in nor had any knowledge of the property destruction.⁵³³ The innocent co-insured fiduciaries filed a notice of loss, asking NHFIC to compensate the innocent partners for their share of the losses.⁵³⁴ The insurers declined.⁵³⁵

Eventually, the case reached the New Hampshire Supreme Court.⁵³⁶ Before that tribunal, the property insurers admitted that the innocent partners could have insured their respective separate insurable interests in

525. *Id.* at 505-06 (citing language in *Hoyt v. N. H. Fire Ins. Co.*, 29 A.2d 121, 122 (N.H. 1942). See *Borman v. State Farm Fire and Cas. Co.*, 499 N.W.2d 419, 421 (Mich. App., 1993) (A conservator/administrator of one insured's estate sued the property insurer to recover proceeds under a homeowner's policy after a deviant co-insured set fire to the property. The court of appeals adopted the administrator's argument and concluded that—despite the deviant co-insured's fraud or intentional misconduct—the insurer still had a duty to indemnify the innocent co-insured.).

526. See *Mercantile*, 376 F.2d at 505-06.

527. See *Hoyt*, 29 A.2d at 122.

528. *Id.*

529. *Id.*

530. *Id.*

531. *Id.*

532. *Id.*

533. *Id.*

534. *Id.* at 122-23.

535. *Id.*

536. See *id.* at 122.

the “common property.”⁵³⁷ The insurers stressed, however, that the innocent partners did not.⁵³⁸ Therefore, from the insurers’ collective perspective, they had no duty to indemnify for several reasons: (1) The allegedly innocent partners did not insure their individual interests; (2) The complaining partners were “jointly named” under each policy; and (3) if one “jointly named” partner breaches a condition subsequent in a policy, that violation prevents all partners from recovering under the first-party property insurance contract.⁵³⁹

The Supreme Court of New Hampshire, however, did not embrace the insurers’ argument.⁵⁴⁰ First, the supreme court observed that the “named insured” or coverage provision in a property insurance contract creates a “joint covenant” and is not conclusive.⁵⁴¹ Second, the court stated, “There is a presumption in this jurisdiction against an intention to create joint interests . . . and if the defendants intended the policies . . . to be joint, that intention should have been clearly expressed.”⁵⁴² Third, the supreme court stressed that the innocent co-insured partners insurable interests under the insurance contract comported with the view that “[A] a contract may be divisible in some respects and indivisible in others.”⁵⁴³

Therefore, in light of those considerations, the *Hoyt* court concluded that deviant co-partner’s incendiarism did not prevent the innocent partners from collecting proceeds under the property insurance contracts.⁵⁴⁴ But, to repeat, there is a split in authorities, and the decision in *Hoyt* is a minority position among partners and partnership cases.⁵⁴⁵ For example, *McCullough v. State Farm Fire & Casualty Co.*, the Court of Appeals for the Eighth Circuit applied Nebraska’s law and concluded that the insurer had no duty to indemnify the innocent father-partner after the deviant son-partner intentionally torched the partnership’s videotape rental business.⁵⁴⁶

537. *Id.* at 122-23.

538. *Id.*

539. *Id.* at 123.

540. *Id.*

541. *Id.*

While it is essential to the existence of a fire insurance policy that the party insured should have some interest in the subject matter of the insurance and cases cited. . . , it is not necessary that the extent of the insured’s interest be set forth in the policy Thus, ‘One who holds an undivided interest need not specifically describe his share . . . but may effect insurance . . . in general terms. If it appears that the description was intended to cover and apply exclusively to the individual interest of the assured, he will recover for such interest as he has.’

Id. at 122 (citing 3 Joyce, Insurance, 2d Ed., § 1691).

542. *Id.* at 123.

543. *Id.*

544. *Id.*

545. *See id.*

546. *McCullough v. State Farm Fire & Cas. Co.*, 80 F.3d 269, 272 (8th Cir. 1996).

Furthermore, Oklahoma and Wisconsin Supreme Courts as well as an appellate court in California have reached the same conclusion.⁵⁴⁷

VI. CONFLICTING STATE AND FEDERAL COURT'S DECLARATORY
JUDGMENTS—WHETHER LIABILITY INSURERS HAVE A DUTY TO PAY
THIRD-PARTY CLAIMS ON BEHALF OF INNOCENT
CO-INSURED FIDUCIARIES

Once more, fiduciaries' dealings, along with their corresponding obligations, may be categorized as strictly *familial* or strictly *business-related* fiduciary relationships. Thus, at this juncture, it is necessary to repeat a few general principles: "All fiduciaries are held to a duty of fairness, good faith and fidelity."⁵⁴⁸ Spouses, parents, and adult children have a mutual obligation to act in good faith, exercise prudence, and be fair when their transactions evolve from and are based on familial confidential relations.⁵⁴⁹ Similarly, business-related fiduciaries must act in good faith

547. See *Travelers Fire Ins. Co. v. Wright*, 322 P.2d 417, 422 (Okla. 1958) (embracing the rule that "an innocent partner cannot recover on an insurance policy upon partnership property willfully burned by his copartner, especially where the policy provides that the insured shall use all reasonable means at and after a fire to preserve the property"); *Bellman v. Home Ins. Co.*, 189 N.W. 1028, 1028 (Wis. 1922) ("To permit a recovery by either the partnership or the unoffending partner upon a policy of insurance issued to a partnership, insuring partnership property, where one of the partners has willfully fired the insured property, is . . . repugnant to an intuitive sense of justice."); *Zemelman v. Boston Ins. Co.*, 84 Cal. Rptr. 206, 208 (Cal. App. 1970) (In this case, a partner—acting on behalf of the partnership—filed a claims under the fire insurance contract and fraudulently misrepresented a material fact. The contract expressly voided the entire policy if—either before or after a loss—the insured willfully misrepresented a material fact. Accepting the insurers defenses, the court concluding that as a matter of law, the deviant partner's filing a false claim triggered a denial of coverage for both deviant and innocent co-insured partners under a fire insurance contracts, because the fraud was a direct fraud upon the insurance company and a violation of the contract).

548. See *In re Honig*, 89 A.2d 411, 413 (1952).

549. *Nobles v. Hutton*, 7 Cal. App. 14, 20-21 (1907) ("[T]he relation of parent and child, where business transactions are carried on between them, is the source of the very highest considerations of confidence and trust. Confidence in such a case originates in and proceeds from natural laws, and, generally speaking, is innate and an essential part of the nature of both, for in whom could a parent repose a greater degree of confidence than in him to whom has been directly transmitted his own blood, and over whom he has exercised parental dominion and discipline from infancy to matured manhood. So, when a son, dealing with his parent with regard to the latter's property, gains an advantage or obtains title to such property without adequate or any consideration, the transaction should, upon principles of equity and fair dealing, be scanned with the strictest scrutiny. . . . The books are full of cases illustrating the application of the principle as thus stated[.]."). See, e.g., *In re Marriage of Young*, No. A114989, 2007 WL 2143007, at*5 (Cal. Ct. App. 2007) (CAL. FAM. CODE § 721 reads: "[I]n transactions between themselves, a husband and wife are subject to the general rules governing fiduciary relationships which control the actions of persons occupying confidential relations with each other. This confidential relationship imposes a duty of the highest good faith and fair dealing on each spouse, and neither shall take any unfair advantage of the other"); *Mizrahi v. Mizrahi*, B 191300, 2007 WL 2728329, at*5 (Cal. Ct. App. 2007) ("Families are held together by mutual trust and rely on that trust when transacting business with one another. Except in unusual circumstances, adult children owe a debt and thus a special fiduciary duty toward their elderly parents[.]"); *In re Guardianship of Willbanks*, 588 P.2d 118, 120 (Or. Ct. App. 1978) ("Family relationships cannot excuse fiduciary's duty to account for the estate's assets.").

and protect co-fiduciaries' interest, even if family members or no family members participate in those confidential and commercial enterprises.⁵⁵⁰

In light of those principles, courts in separate and community property states have to address three very different but highly related questions: (1) whether innocent fiduciaries may purchase liability or indemnity insurance to insure themselves against the perils of a vicarious liability action or judgment; (2) whether innocent fiduciaries are vicariously liable for their deviant co-fiduciaries intentional and negligent acts; and (3) whether innocent co-insured fiduciaries' may recover proceeds under third-party insurance contracts after triers of fact conclude that innocent fiduciaries are vicariously liable for deviant fiduciaries' negligent or intentional acts.⁵⁵¹

Put simply, there is no serious debate or conflict regarding the first and second questions. Generally, innocent fiduciaries may purchase liability or indemnity insurance to cover third-party, personal-injury, or property-damage claims when innocent fiduciaries become vicariously liable for their co-fiduciaries' wrongful acts.⁵⁵² In fact, general contractors often require subcontractors to purchase third-party liability or indemnity insurance which covers general contractors if they become vicariously liable for workers' injuries.⁵⁵³

550. *Best Buy Stores, L.P. v. Developers Diversified Realty Corp.*, 636 F. Supp. 3d 869, 888 (D. Minn. 2009) ("Under Minnesota law, whether a fiduciary relationship exists is a question of fact. 'A fiduciary relationship exists 'when confidence is reposed on one side and there is resulting superiority and influence on the other.' Evidence of business experience disparities, financial control, repeated assurances and invited confidences may suffice to show a fiduciary relationship") (quoting *Toombs v. Daniels*, 361 N.W.2d 801, 809 (Minn.1985); *Stark v. Equitable Life Assurance Soc'y*, 285 N.W. 466, 470 (Minn. 1939); *Kennedy v. Flo-Tronics, Inc.*, 143 N.W.2d 827, 830 (Minn. 1966). *See, e.g., DiSabatino v. Farrar*, No. Civ. A. 95C-02-183-WTQ, 1998 WL 730322, at *5 (Del. Super. 1998).

The court finds there is a valid equitable claim; on the totality of the circumstances, Alfred reasonably relied upon and trusted his brother Michael to establish somehow a retirement contribution for him and further that such trust was supported by Alfred's labor for the family corporations, Alfred's ownership status in Debro, and . . . by the clear representations of Michael. There existed both a personal confidential relationship, enhanced by a blood relationship, and a family business fiduciary relationship between manager-employer and shareholder-employee.

Id.

551. *See infra* text accompanying notes 552-56.

552. *See, e.g., Frontline Processing Corp. v. Am. Econ. Ins. Co.*, 149 P.3d 906, 909 (Mont. 2006).

[T]he policy before us insures Frontline against direct losses caused by the dishonesty of its employees. Many jurisdictions have construed 'direct loss' or similar language in a fidelity bond or insurance policy. A fidelity policy, also known as an employee dishonesty policy, is a form of insurance in which the insurer agrees 'to indemnify an employer against a loss arising from the lack of integrity or honesty of an employee. . . .' Under a liability policy, by contrast, the policy holder is insured against or indemnified for, vicarious liability to a third-party claimant.

Id. (citation omitted).

553. *See, e.g., Seren Innovations, Inc. v. Transcontinental Ins. Co.*, No. A05-917, 2006 WL 1390262, at *1 (Minn. Ct. App. 2006).

Seren Innovations, Inc. Seren was the contractor on a fiber optic cable installation project in St. Cloud. Seren hired Cable Constructors, Inc. (CCI) to perform the construction and

Second, courts generally agree that fiduciaries are vicariously liable for their co-fiduciaries' negligent conduct.⁵⁵⁴ Under the "single business enterprise theory," two corporations are vicariously liable for the each other's obligations if a single business enterprise exists factually and they both participate in the enterprise.⁵⁵⁵ Members of joint ventures are vicariously liable for each other's acts, since a voluntary relationship exists between or among the members.⁵⁵⁶ Trustees, executors, administrators, or conservators may be vicariously liable.⁵⁵⁷ Additionally, even insurance carriers are vicariously liable for their local recording agents' affirmative misrepresentations.⁵⁵⁸

On the other hand, whether fiduciaries are liable for their co-fiduciaries' intentional acts depends on the types of fiduciary relationships that exist among or between fiduciaries.⁵⁵⁹ For example, under the doctrine of respondeat superior, employers are vicariously liable for employees' tortious acts when employees latter act within their scope of employment.⁵⁶⁰

installation of the cable. Although Seren had a primary insurance carrier, [with] respondent Western National Mutual Insurance Company Western National, the construction contract between Seren and CCI required CCI to purchase additional insurance to indemnify Seren. In satisfaction of this requirement, CCI purchased policies from . . . Transcontinental Insurance Company (Transcontinental) and Continental Casualty Co. (Continental). CCI purchased from Transcontinental a commercial general-liability policy with coverage of \$1 million. CCI purchased from Continental a commercial umbrella policy with coverage of \$25 million.

Id.

554. *Cf.* St. Anthony's Hosp. v. Whitfield, 946 S.W.2d 174, 177 (Tex. App.—Amarillo 1997, writ denied) ("Vicarious liability is liability placed upon one for the conduct of another, based solely upon the relationship between the two.").

555. *See* S. Union Co. v. City of Edinburg, 129 S.W.3d 74, 86-90 (Tex. 2003).

556. *See* Adams v. Johnston, 860 P.2d 423, 429 (Wash. Ct. App. 1993).

557. *Cf.* Reynolds v. Schrock, 107 P.3d 52, 57 (Or. Ct. App. 2005) (embracing the view that "a trustee's attorney may be liable for a trustee's breach of the trust if the attorney 'knew or should have known that he was assisting the trustee to commit a breach of trust'"). *But see* Murdock v. Murdock, 370 So. 2d 290, 292-93 (Ala. 1979).

The law . . . is well settled. 'An executor who is a layman has the right to rely upon the advice and counsel of an attorney If due care is exercised in the selection and employment of an attorney or agent, the executor is not absolutely bound by dereliction of the attorney or agent. . . [A] representative is ordinarily not personally liable for loss chargeable to his lawyer's negligence, misconduct, or nonfeasance, if due prudence was exercised in the selection of the lawyer. But the representative may not surrender all the duties of his trust or delegate all his functions to the attorney without becoming responsible to the distributees for losses caused by the attorney's conduct. . . .' This rule, by its very terms, precludes the administrator's vicarious liability under the doctrine of *respondeat superior*. Liability is not to be imposed upon an imputed negligence or no-fault concept. . . . With the possible exception of Louisiana, this personal fault-based rule of an administrator's or executor's liability for dereliction of the fiduciary's lawyer appears to be universally recognized throughout the United States.

Id. (quoting 31 AM. JUR. 2D EXECUTORS AND ADMINISTRATORS § 219).

558. *See, e.g.,* Royal Globe Ins. Co. v. Bar Consultants, Inc., 577 S.W.2d 688, 694 (Tex. 1979).

559. *See, e.g.,* Haney v. Kitchen, 690 N.W.2d 675, 677 (Iowa 2005) (providing a list of situations in which a fiduciary will be held liable).

560. *See* Baptist Mem'l Hosp. Sys. v. Sampson, 969 S.W.2d 945, 947 (Tex. 1998).

However, employers may not be vicariously liable when employees commit intentional torts on or off the business premises during working hours.⁵⁶¹ Furthermore, married people are not vicariously liable for each other's intentional acts simply because they are married.⁵⁶² Generally, the law recognizes that spouses are "are still individuals and responsible for their own acts."⁵⁶³

Courts in community and separate property states continue to deliver conflicting rulings surrounding the third question: whether third-party insurers must reimburse innocent co-insured fiduciaries after the latter become vicariously liable for their co-fiduciaries' negligent or intentional acts and the innocent fiduciaries pay third-party claims or judgments.⁵⁶⁴ To be sure, judicial splits appear among decisions in which both familial and business fiduciaries have asked insurance companies to reimburse out-of-pocket expenditures.⁵⁶⁵ Therefore, this latter question and its ancillary issues are discussed in this part.⁵⁶⁶

A. Whether Liability Insurers Have a Duty to Pay Third-party Claims On Behalf of Vicariously Liable, Innocent, and Co-Insured Familial Fiduciaries

To begin the discussion, assume that familial fiduciaries are factually innocent co-insured, and vicariously liable for another familial fiduciary's wrongful conduct. What factors do courts consider before determining whether third-party insurers have an obligation to indemnify innocent fiduciaries after the latter use personal funds to cover third-party victims' personal injuries or property damage? To help answer this fundamental question, consider the facts and the courts' conflicting analyses in two, fairly similar controversies.⁵⁶⁷

In *American States Insurance Co. v. Borbor by Borbor*, James and Isabel Meacham were residents of California where they owned and operated Isabel's Nursery School.⁵⁶⁸ Put simply, they were familial and business fiduciaries. American States Insurance Company (American) is an Indiana corporation.⁵⁶⁹ Under a comprehensive liability policy, American

561. See *Scott v. Commercial Union Ins. Co.*, 415 So. 2d 327, 329 (La. Ct. App. 1982); see also *Enserch Corp. v. Parker*, 794 S.W.2d 2, 6 (Tex. 1990) (concluding that a party is not ordinarily vicariously liable for an independent contractor's actions, because the latter has sole control over the means and methods to accomplish a bargained-for-exchange task).

562. See *Shearer v. Dunn County Farmers Mut. Ins. Co.*, 159 N.W.2d 89, 93 (Wis. 1968).

563. *Id.*

564. See *infra* Part VI.A.

565. See *infra* Part VI.A.

566. See *infra* Part VI.A.

567. See *infra* text accompanying notes 568-641.

568. *Am. States Ins. Co. v. Borbor by Borbor*, 826 F.2d 888, 889 (9th Cir. 1987).

569. *Id.* at 890.

insured James and Isabel Meacham d/b/a: Isabel's Nursery School."⁵⁷⁰ James was a pedophile.⁵⁷¹ He took "over 2,000 photographs" of children who attended the school and "catalogued the slides in a meticulous filing system."⁵⁷² James photographed the children while they were undressing, touching themselves, and posing in various sexual positions.⁵⁷³

James's deviant activities and his conviction occurred while the liability insurance contract was in force.⁵⁷⁴ Also, during that same period, at least twenty-three children and their parents sued James and Isabel Meacham for the intentional and negligent infliction of emotional distress, assault, battery, and fraud.⁵⁷⁵ The Meachams asked American to defend and indemnify them.⁵⁷⁶ The liability insurer began a defense under a reservation of rights.⁵⁷⁷

Shortly thereafter, American filed a declaratory judgment action in the United States District Court for the Central District of California.⁵⁷⁸ The insurer asked the federal district court to determine its rights and obligations under the Meachams' liability insurance policy.⁵⁷⁹ After a bench trial, the district court found the following: (1) The Meachams were partners in the nursery school business; (2) James' molestation of the children was intentional; and (3) as a partner, Isabel was vicariously liable for James' intentional acts.⁵⁸⁰

Even more relevant, section 533 of the California Insurance Code states that "[a]n insurer is not liable for a loss caused by the willful act of the insured; but he is not exonerated by the negligence of the insured, or of the insured's agents or others."⁵⁸¹ Citing section 533, the federal district court concluded that James' intentional acts "occurred 'in the ordinary course of business,'" and those violations precluded insurance coverage for both James and Isabel.⁵⁸² Therefore, American did not have to indemnify or defend Isabel.⁵⁸³ To help reach that conclusion, the district court suggested that Isabel might have been slightly acquiescent as a wife and

570. *Id.* at 889.

571. *Id.*

572. *Id.* at 889-90.

573. *Id.* at 889.

574. *Id.*

575. *Id.* at 890.

576. *Id.*

577. *Id.*

578. *Id.*

579. *Id.*

580. *Id.*

581. CAL. INS. CODE § 533 (West 1987).

582. *Am. States Ins. Co.*, 826 F.2d at 892 (citing CAL. CORP. CODE § 15013) (finding that James and Isabel had equal control over the operation of the nursery school, and that James had apparent and ostensible authority to be with the children and take them off school premises, the court concluded that his wrongful acts occurred "in the ordinary course of the business").

583. *Id.* at 895.

partner when James was molesting children.⁵⁸⁴ Asserting that she was the innocent wife, partner, and co-insured fiduciary, Isabel Meacham appealed.⁵⁸⁵

Before the Ninth Circuit Court of Appeals, Isabel admitted that she was a partner in the nursery school enterprise.⁵⁸⁶ Additionally, citing partnership rules, Isabel admitted that she was vicariously liable for James' conduct.⁵⁸⁷ However, she stressed that she was separately insured under the American liability insurance contract.⁵⁸⁸ Therefore, in light of her individual coverage, Isabel insisted that American had a duty to indemnify and defend her against the underlying third-party lawsuit.⁵⁸⁹ The court of appeals agreed with Isabel, rejecting the district court's conclusion that section 533 of the California Insurance Code barred her recovery under the third-party insurance contract.⁵⁹⁰

First, the Ninth Circuit observed that the federal district court mistakenly and inappropriately "collapsed two separate considerations into one."⁵⁹¹ More specifically, the Ninth Circuit emphasized that whether a partner may be vicariously liable for co-partner's intentional acts is very different from whether California Insurance Code § 533 requires a liability insurer to defend or indemnify a totally innocent co-insured partner who is vicariously liable for a co-partner's conduct.⁵⁹² In the end, Court of Appeals for the Ninth Circuit declared that American had a duty to indemnify Isabel.⁵⁹³ The federal appellate stressed that "Isabel's liability for James' acts [must] be distinguished from her ability to insure against

584. *Id.* at 891-92 ("American States argued at trial that Isabel had aided, abetted, participated in, or ratified James' criminal acts, the district court found she had not. The court stated: 'I find that at most, she *may* have been a knowing bystander. More likely, she closed her eyes to certain facts to deliberately avoid learning the whole truth.'").

585. *Id.*

586. *Id.*

587. *Id.* at 892.

[T]he court concluded that Isabel committed no wrongful act which would deprive her of the policy's coverage. The court determined, however, that Isabel was nonetheless vicariously liable for James' acts of child molestation because the Meachams operated the nursery school as a partnership. 'This is true even if Isabel is regarded as innocent as to his wrongdoings, or merely negligent in her supervision.'

Id. (citations omitted).

588. *Id.* at 893.

589. *Id.* at 890.

590. *Id.* at 892.

591. *Id.*

592. *Id.*

593. *Id.* at 894. "To conclude that Isabel may be indemnified under the American States policy does no violence to this public policy. . . . [N]either Isabel's negligence if any, nor her vicarious liability for James' willful acts precludes insurance coverage under California Insurance Code § 533." *Id.*

that liability.”⁵⁹⁴ In addition, the Ninth Circuit embraced Isabel’s argument that she was insured separately under the liability insurance contract.⁵⁹⁵

In *Taryn E.F. by Grunewald v. Joshua M.C.*, innocent parents were co-insured fiduciaries along with their child.⁵⁹⁶ However, the insurer did not have to indemnify the parents after they became vicariously liable for their child’s intentional act.⁵⁹⁷ Here, Dan and Dawn F. are the parents of Taryn F., and Michael and Beverly C. are the parents of Joshua C.⁵⁹⁸ On two occasions, Taryn’s parents employed Joshua, then twelve years old, to babysit three-year-old Taryn and her brother.⁵⁹⁹ On both occasions, Joshua sexually assaulted and battered Taryn in various ways.⁶⁰⁰ Taryn’s parents commenced a third-party lawsuit against Joshua and his parents seeking damages for Joshua’s torts.⁶⁰¹

The complaint alleged that Joshua intentionally, willfully, maliciously, and wantonly sexually molested a female infant.⁶⁰² Dan and Dawn also alleged that Joshua’s parents were vicariously liable for Joshua’s act.⁶⁰³ A Wisconsin statute allows third-party victims to impute a deviant child’s intentional acts to the child’s innocent parents.⁶⁰⁴ More specifically, Section 895.035(2)(a) of the Wisconsin Statute reads in pertinent part:

The parent or parents with custody of a minor child, in any circumstances where he, she, or they may not be liable under the common law, are liable for damages to property, for the cost of repairing or replacing property or removing the marking, drawing, writing, or etching from property . . . for the value of unrecovered stolen property, or *for personal injury attributable to a willful, malicious, or wanton act of the child.*⁶⁰⁵

Dan and Dawn amended their third-party complaint and listed Michael and Beverly’s homeowners’ insurer, Little Black Mutual Insurance Company (Little Black), as another defendant.⁶⁰⁶

Little Black filed a motion for summary judgment, asking the trial court to dismiss Dan and Dawn’s third-party lawsuit.⁶⁰⁷ The insurer argued

594. *Id.* at 892.

595. *Id.* at 893. “[Isabel argued that California Insurance Code § 533] does not preclude insurance coverage for an innocent, albeit perhaps a negligent, co-partner who is a separate insured under a comprehensive liability policy.” *Id.*

596. *Taryn E.F. by Grunewald v. Joshua M.C.*, 505 N.W.2d 418 (Wis. Ct. App. 1993).

597. *Id.* at 419.

598. *Id.*

599. *Id.*

600. *Id.*

601. *Id.*

602. *Id.* at 420.

603. *Id.* at 419.

604. *Id.* at 422.

605. WIS. STAT. ANN. § 895.035(2)(a) (West 2009) (emphasis added).

606. *Taryn E.F.*, 505 N.W.2d at 419.

607. *Id.*

that the insurance contract excluded coverage for “any insured’s intentional, wanton malicious acts.”⁶⁰⁸ Also citing the exclusion clause, Little Black maintained that it had no duty to indemnify or defend Joshua and his parents.⁶⁰⁹ Little Black asserted that Joshua’s liability and his parents’ vicarious liability evolved “directly or indirectly from the actual, alleged or threatened sexual molestation [of baby Taryn].”⁶¹⁰

After reviewing the exclusion clause, the trial court granted the insurer’s motion.⁶¹¹ The court concluded that Little Black had no duty to indemnify or defend Beverly and Michael.⁶¹² More enlightening, the trial court found that (1) Joshua was a “named insured” under the insurance contract; (2) the exclusions clause precluded coverage for “any insured”; and (3) coverage for Joshua’s alleged acts were excluded under the intentional-acts and sexual-molestation exclusion clauses.⁶¹³ Although finding that Michael and Beverly were innocent co-insureds, the trial court concluded that the contract’s severability-of-interests clause did not apply.⁶¹⁴

On appeal before the Wisconsin Court of Appeals, Taryn’s parents argued that Little Black had a duty to indemnify Michael and Beverly, so the latter could secure and transfer the insurance proceeds to Taryn.⁶¹⁵ In particular, they argued that the trial court erred because Michael and Beverly were innocent co-insureds who did not participate in or encourage Joshua’s acts.⁶¹⁶ Furthermore, Taryn’s parents asserted that Little Black had a duty to indemnify because Michael and Beverly were insured separately under the insurance contract’s severability-of-interest clause.⁶¹⁷

First, the court of appeals concluded that the exclusion clause excluded coverage for Michael and Beverly’s vicarious liability because Joshua’s

608. *Id.* at 420.

609. *Id.*

610. *Id.*

611. The policy exclusions clause read:

INTENTIONAL ACT EXCLUSION

* * *

The insurance afforded by this policy shall not apply to any damages to property or for bodily injury attributable to a willful, malicious, wanton or otherwise intentional act of the “insured” or performed at an “insured’s” direction or for any outrageous conduct on the part of any “insured” consisting of any intentional, wanton, malicious acts, or, in addition, any act that would constitute wanton disregard for the rights of others.

* * *

SEXUAL MOLESTATION EXCLUSION

This policy does not apply to liability which results directly or indirectly from the actual, alleged or threatened sexual molestation of a person.

612. *Id.* at 420.

613. *Id.*

614. *Id.*

615. *See id.* at 421.

616. *See id.*

617. *See id.* at 420.

tortious acts were excluded.⁶¹⁸ Second, the insurance contract's severability-of-interest clause stated: "Each person listed above is a separate insured under this policy, but this does not increase *our* limit of liability under this policy."⁶¹⁹ Yet Taryn's parents argued that ambiguity arises when one reads the language in the severability clause in conjunction with the terms and phrases in the exclusionary clauses.⁶²⁰ Rejecting this argument, the Wisconsin Court of Appeals stated: "Language [in the exclusion clause] unambiguously denies coverage for all liability incurred by each and any insured as a result of certain conduct by any of the persons insured by the policy."⁶²¹

Without a doubt, the conflicting decisions in *Borbor* and *Taryn* are excellent examples of widespread disagreement among state and federal courts over the question of whether insurers must indemnify innocent co-insured and vicariously liable fiduciaries when their deviant co-familial fiduciaries injure third-party victims' persons and property. Many courts have forced insurers to indemnify innocent but vicariously liable familial fiduciaries.⁶²² Numerous other courts have not.⁶²³

618. *Id.* at 422. "Under this insurance contract, coverage for liability resulting from Joshua's acts is precluded because the contract expressly denies coverage (1) if *any* insured engages in intentional, wanton, malicious acts and (2) if liability directly or indirectly results from a sexual molestation." *Id.*

619. *Id.* at 420 (emphasis in original).

620. *Id.* at 420.

621. *Id.* at 420-21.

Assuming, without deciding, that the severability clause creates separate policies for each insured, that clause does not render the exclusionary clauses in the policy ambiguous. The intentional acts exclusion expressly states that "[t]he insurance afforded by this policy shall not apply to *any damages . . . attributable to . . . any outrageous conduct on the part of any "insured" consisting of any intentional, wanton, malicious acts. . . .*

Id.

622. See, e.g., *Armstrong v. Sec. Ins. Group*, 288 So. 2d 134, 137 (Ala. 1973) (The named insureds under a liability policy were "Mary Ann and William Cofield d/b/a Lakeview Sandwich Shop." William shot a patron during a scuffle at the shop. The court held that where innocent co-insured did not authorize, direct, or commit the assault, the liability policy's intentional injury exclusion did not apply); *Arenson v. Nat'l Auto. & Cas. Ins. Co.*, 286 P.2d 816, 818 (Cal. 1955) (Arenson's minor son intentionally burned down school property. A state statute imposed liability on a parent for a child's "willfully" caused damages. The school district secured a judgment against Arenson. Although Arenson, his spouse, and minor children were all insured under a general liability policy, the insurer refused to indemnify Arenson because the damage was "caused intentionally by or at the direction of the insured." The California Supreme Court reversed and stated: "Section 533 of the Insurance Code—which codifies the general rule that an insurance policy indemnifying the insured against liability due to his own willful wrong is void as against public policy—has no application to a situation where the plaintiff is not personally at fault."); *Nat'l Union Fire Ins. Co. v. Lynette C.*, 279 Cal. Rptr. 394, 402 (Cal. Ct. App. 1991) (concluding that the foster parents' liability policy—which excluded from coverage liability for sexual misconduct if insured acted with actual lasciviousness or immoral purpose and intent—covered an innocent co-insured foster mother who negligently failed to protect foster child from the foster father's sexual molestation); *Safe Auto Ins. Co. v. Farm Bureau Ins. Co.*, 856 N.E.2d 156, 162 (Ind. App. 2006) ("Although Badillo is excluded from coverage under the terms of Duran's insurance policy, Indiana Code section 27-1-13-7 requires Safe Auto to insure Duran for vicarious liability arising from the negligence of a permissive user, even those otherwise excluded. In addition, Duran's misrepresentation at the time of her application for the policy does not affect Safe Auto's obligation to provide coverage for vicarious liability arising from the permissive use of the insured vehicle.");

But there is more. In *Taryn*, Joshua's parents stressed that the insurance contract contained a "severability of interests" clause.⁶²⁴ Under such clauses, the named insureds' insurable interests are severable and not joint.⁶²⁵ Therefore, before refusing to indemnify, insurers have a duty to read an exclusion clause in light of the "separation of insureds" clause.⁶²⁶ Essentially, the "separation of the insureds doctrine" requires insurers to apply an exclusion clause to each insured separately.⁶²⁷

Arguably, when courts compare severability and exclusion clauses, those tribunals must decide which clause is superior.⁶²⁸ There is no universal test to determine which clause controls.⁶²⁹ However, courts have fashioned some generally severability rules to govern disputes involving property insurance contracts. First, innocent co-insured fiduciaries may not recover proceeds under a property insurance contract if the innocent and

Shearer v. Dunn County Farmers Mut. Ins. Co., 159 N.W.2d 89, 93 (Wis. 1968) (rejecting an invitation to fashion a vicariously liability doctrine that imputes an insured deviant spouse's action to the insured innocent spouse and prevent the innocent spouse from recovering the insurance contract. "The marriage relationship should not be used as a basis for such a law. Married people are still individuals and responsible for their own acts. Vicarious liability is not an attribute of marriage."); Smith v. State Farm Fire & Cas. Co., 531 N.W.2d 376, 382 (Wis. Ct. App. 1995) (concluding that the insurer had to indemnify the innocent co-insured fiduciary because the deviant co-insured's negligence could not be imputed to the innocent fiduciary); Chacon v. Am. Family Mut. Ins. Co., 788 P.2d 748, 752 (Colo. 1990) (declining to follow the minority of jurisdictions, holding that "any insured" denies coverage only to the culpable party, and recognizing that "an insurance policy is a contract between the parties which should be enforced in a manner consistent with the intentions expressed therein"); Nw. Nat'l Ins. Co. v. Nemetz, 135 Wis. 2d 245, 400 N.W.2d 33, 38 (Wis. Ct. App. 1986) (concluding that the exclusionary clauses precluded coverage for the insured who committed the excludable acts, but not for the innocent insured because the insurers did not adequately draft the policy to exclude coverage for both insureds based on the excludable acts of one insured).

623. *George v. White Consol. Indus., Inc.*, 721 So. 2d 573, 575-77 (La. Ct. App. 1998) (concluding that household exclusion bars a tort-based indemnity claim against an insured who is vicariously liable); *Worcester Mut. Ins. Co. v. Marnell*, 496 N.E.2d 158, 161 (Mass. 1986) (concluding that the insurer had no duty to indemnify innocent co-insured and vicariously liable familial fiduciaries); *McPhee v. Tufty*, 623 N.W.2d 390, 394, 409 (N.D. 2001) (concluding that evidence supported the lower court's application of the family car doctrine which made the father vicariously liable for the driver's negligence but also concluding that the policy did not cover the third-party, vicarious-liability claim since the car was not "used"); *Knoblock v. Prudential Prop. & Cas. Ins. Co.*, 615 A.2d 644, 646-47 (N.J. Super. Ct. App. Div. 1992) (declaring that the insurance contract's exclusion clause bars third-party tort-based indemnity claim against an insured who is vicariously liable because the claim was derived solely from the third-party's bodily injury claim); see *J.G. & R.G. v. Wangard*, 753 N.W.2d 475, 495-96 (Wis. 2008) (Butler, J., dissenting) ("[T]o the extent that the majority appears to view the intentional acts exclusion clause as unambiguously imputing Steven's intentional acts to his wife's negligent acts, such an imposition of vicarious liability violates the rule of law we have generally established against imputing one spouse's conduct to another in an insurance coverage contract"). (citing *Shearer v. Dunn County Farmers Mut. Ins. Co.*, 159 N.W.2d 89, 93 (Wis. 1968)).

624. *Taryn E.F. v. Joshua M.C.*, 505 N.W.2d 418, 420 (Wis. Ct. App. 1993).

625. *Id.*

626. See, e.g., *Michael Carbone, Inc., v. Gen. Accident Ins. Co.*, 937 F. Supp. 413, 416 (E.D. Pa. 1996).

627. *Id.*

628. See *id.*

629. See *id.* at 417.

deviant co-insureds interests in tangible or intangible property are joint or inseparable.⁶³⁰ On the other hand, if the innocent and offending co-insureds' interests in the property are divisible or severable, innocent co-insureds may recover under a property-insurance contract.⁶³¹

However, it is important to stress: In *Borbor* and *Taryn* the respective controversies concerned whether innocent and co-insured fiduciaries, although vicariously liable, could recover under liability insurance contracts.⁶³² Therefore, courts must perform a slightly different analysis.⁶³³ A court must determine whether the co-insureds' contractual obligations are joint or severable under the liability insurance contracts.⁶³⁴ Arguably, liability insurers should indemnify innocent co-insured fiduciaries if the latter's contractual obligations are severable and if innocent co-insured fiduciaries factually breached coverage, exclusions, or conditions clauses.⁶³⁵

Furthermore, this arguably sound rule should apply even when innocent fiduciaries are vicariously liable for their co-fiduciaries' intentional, criminal, or negligent acts.⁶³⁶ However, courts are also seriously divided over this "severability of obligation" issue.⁶³⁷ Some courts do not force liability insurers to indemnify vicariously liable, innocent co-insured fiduciaries.⁶³⁸ Generally, those courts conclude that the "any insured" language in an exclusion clause bars coverage for deviant, innocent, or vicariously liable co-insured fiduciaries if "any insured" violates the exclusion clause, and those tribunals apply this arguably draconian rule even if liability policies contain severability clauses.⁶³⁹

630. See, e.g., *Short v. Okla. Farmers Union Ins.*, 619 P.2d 588, 590 (Okla. 1980); see also *Morgan v. Cincinnati Ins. Co.*, 282 N.W.2d 829, 830 (Mich. Ct. App. 1979).

631. See, e.g., *Hosey v. Seibels Bruce Group, S.C. Ins. Co.*, 363 So. 2d 751, 754 (Ala. 1978); and *Hoyt v. N.H. Fire Ins. Co.*, 29 A.2d 121, 123 (N.H. 1942).

632. See discussion *supra* Part VI.A.

633. See discussion *supra* Part VI.A.

634. See discussion *supra* Part VI.A.

635. See discussion *supra* Part VI.A.

636. See discussion *supra* Part VI.A.

637. See *infra* notes 630-40.

638. See *id.*

639. *Michael Carbone, Inc. v. Gen. Accident Ins. Co.*, 937 F. Supp. 413, 423 (E.D. Pa. 1996) (holding that an exclusion phrased "any insured" precluded coverage despite a severability clause); see *McCauley Enters. v. N.H. Ins. Co.*, 716 F. Supp. 718, 721 (D. Conn. 1989) (holding that an exclusion referencing "any insured" barred recovery of losses by an innocent co-insured); *Chacon v. Am. Family Mut. Ins. Co.*, 788 P.2d 748, 752 (Colo. 1990) (holding that an exclusion for the intentional acts of "any insured" precluded a negligent supervision claim despite a severability clause); *Oaks v. Dupuy*, 653 So. 2d 165, 168 (La. Ct. App. 1995) (concluding that a severability clause did not alter the scope of an exclusion clause phrased in terms of "any insured"); *Am. Family Mut. Ins. Co. v. Copeland-Williams*, 941 S.W.2d 625, 629 (Mo. Ct. App. 1997) ("The use of the phrase 'any insured' makes the exclusionary clause unambiguous even in light of the severability clause."); *Am. Family Mut. Ins. Co. v. Moore*, 912 S.W.2d 531, 533-35 (Mo. Ct. App. 1995) (holding that a severability clause did not negate an exclusion for damages "arising out of business pursuits of any insured . . . by an insured"); *Nw. G.F. Mut. Ins. Co. v. Norgard*, 518 N.W.2d 179, 180, 184 (N.D. 1994) (holding that an exclusion for sexual molestation by "an insured, an insured's employee or any other person involved" precluded coverage for a negligent supervision claim against another insured, notwithstanding a severability clause); *Great Cent. Ins. Co. v.*

Conversely, other federal and state courts forced insurers to indemnify even vicariously liable and innocent co-fiduciaries when insurance contracts contained severability-of-obligation clauses.⁶⁴⁰

*B. Whether Liability Insurers Have a Duty to Indemnify or Defend
Vicariously Liable, Innocent, and Co-Insured Business Fiduciaries Against
Third-party Claims*

Finally, liability insurers and business fiduciaries also frequently litigate whether insurers have a contractual duty to indemnify or defend factually innocent, yet vicariously liable, co-insured fiduciaries.⁶⁴¹ Generally, liability insurers argue that they have no obligation to indemnify or defend innocent co-insured commercial fiduciaries, when deviant co-fiduciaries negligently or intentionally destroy third-parties' lives and/or property interests.⁶⁴² That this disagreement persists among innocent commercial fiduciaries and liability insurers is somewhat puzzling for one major reason: Commercial or business fiduciaries know they will, or might be, vicariously liable for their deviant partners' conduct; therefore, they purchase liability insurance.⁶⁴³

Roemmich, 291 N.W.2d 772, 774 (S.D. 1980) (finding no ambiguity in the term "any insured" in an exclusionary clause, even when interpreted with a severability of insurance provision); Caroff v. Farmers Ins. Co. of Wash., 989 P.2d 1233, 1236-37 (Wash. Ct. App. 1999) (holding that exclusions of coverage for injury arising out of child molestation by "any insured" precluded coverage despite general severability clauses); Taryn E.F. v. Joshua M.C., 505 N.W.2d 418, 421 (Wis. Ct. App. 1993) (holding that an exclusionary clause referencing "any insured" precluded coverage even when read with a severability clause); see, e.g., Am. Family Mut. Ins. Co. v. White, 65 P.3d 449, 457 (Ariz. App. [Div. 1] 2003) (concluding that the exclusion for conviction of "any insured" applied to claims made solely against parents, regardless of policy's severability clause).

640. W. Am. Ins. Co. v. AV & S, 145 F.3d 1224, 1229 (10th Cir.1998) ("[T]he term 'any insured' in an exclusion clause in a policy that also contains a severability clause does not exclude coverage for all insureds when only one insured is at fault."); Transp. Indem. Co. v. Wyatt, 417 So. 2d 568, 571 (Ala. 1982) (applying a severability clause and finding the term "any insured" in an exclusion ambiguous); Premier Ins. Co. v. Adams, 632 So. 2d 1054, 1057 (Fla. Dist. Ct. App. 1994) (holding that a severability clause limited an exclusion for intentional acts by "any insured" to exclude coverage only for the insured who intentionally caused the injury); Brumley v. Lee, 963 P.2d 1224, 1227-28 (Kan. 1998) (holding that a severability clause afforded each insured his or her own policy despite an exclusionary intentional act clause referencing "any insured"); Worcester Mut. Ins. Co. v. Marnell, 496 N.E.2d 158, 161 (Mass. 1986) (interpreting a severability clause to nullify a motor vehicle exclusion despite the exclusion's "any insured" language); Am. Nat'l Fire Ins. Co. v. Estate of Fournelle, 472 N.W.2d 292, 295 (Minn. 1991) (stating that a severability clause provided for separate coverage to named insureds despite a household exclusion applying to "any insured").

641. See, e.g., Selander v. Erie Ins. Group, 709 N.E.2d 11661, 1162-1163 (Ohio 1999) ("Glenn and Eugene Selander were electricians involved in a partnership known as Twin Electric and were working in the course and scope of their business activities. . . . The policy included uninsured/underinsured motorist coverage in the amount of \$300,000 per accident. . . . Under the specific language of the policy, 'if you are a partnership a non-owned automobile does include any automobile owned by or registered in the name of a partner, but only while such automobile is being used in your business.'").

642. See *id.*

643. See *id.*

Potentially vicariously liable employers also accept the same realization and purchase third-party insurance.⁶⁴⁴ But even more importantly, federal and state courts recognize that commercial or business fiduciaries are acting prudently and responsibly when they purchase liability insurance to cover imputed negligence. Yet, conflicting judicial rulings and declarations continue to arise over whether third-party insurers have a duty to indemnify or defend vicariously liable co-insured, business fiduciaries.⁶⁴⁵

To illustrate, consider a few decisions in which federal and state courts decided whether liability insurers had a duty to indemnify or defend presumably vicariously liable corporations, partners, and employers.⁶⁴⁶ In *Northern Assurance Co. v. Rachlin Clothes Shop*, the Delaware Supreme Court declared that when officers or stockholders act on behalf of the corporation, those fiduciaries' conduct become acts of the corporation.⁶⁴⁷ Therefore, an insurer does not have to indemnify the innocent corporation when deviant directors and officers exercise absolute control over corporate business and harm corporate interests.⁶⁴⁸ In *Western Casualty & Surety Co. v. Aponaug Manufacturing Co.*, the Fifth Circuit Court of Appeals declared that the liability insurer had a duty to indemnify the innocent corporation after the president and agent of the corporation injured a third-party and the latter sued the corporation.⁶⁴⁹

A split in rulings also exists among partners-partnership decisions. The Supreme Courts of New Jersey, New York, and Oklahoma have declared that liability insurers have a duty to indemnify and defend innocent partners when deviant partners injure a third-party and the victim commences a vicarious liability action against the innocent partners.⁶⁵⁰ The

644. Cf. *Baumeister v. Plunkett*, 673 So. 2d 994, 996 (La. 1996). "An employer is not vicariously liable merely because his employee commits an intentional tort on the business premises during working hours. Vicarious liability will attach in such a case only if the employee is acting within the ambit of his assigned duties and also in furtherance of his employer's objective." *Id.* (quoting *Scott v. Commercial Union Ins. Co.*, 415 So. 2d 327, 329 (La. Ct. App. 1982)).

645. See *infra* text accompanying notes 647-71.

646. See *infra* text accompanying notes 647-71.

647. *N. Assurance Co. v. Rachlin Clothes Shop*, 125 A. 184, 187-88, 190 (Del. 1924).

648. *Id.*

649. *W. C. & Sur. Co. v. Aponaug Mfg. Co.*, 197 F.2d 673, 674 (5th Cir.1952). The exclusionary clause provided that 'Assault and battery shall be deemed an accident unless committed by or at the direction of the Insured;' the court stated: "The clause is without effect as to other persons insured who neither committed nor directed the commission of the assault and battery." *Id.*

650. See *Malanga v. Mfrs. Cas. Ins. Co.*, 146 A.2d 105, 110 (N.J. 1958) (finding that although all partners were liable when one partner committed an assault and battery, the assault and battery exclusory clause in liability policy did not diminish the other partners rights); *Morgan v. Greater New York Taxpayers Mut. Ins. Ass'n*, 112 N.E.2d 273, 275 (N.Y. 1953) ("Where liability is imposed upon one of the insureds for an assault by another assured in which he took no part, the [innocent partner's right of indemnity] should be no different for that which would obtain where the assault was committed by a person who is not an assured . . ."); see also *Nassau Ins. Co. v. Mel Jo-Jo Cab Corp.*, 423 N.Y.S.2d 813, 815 (N.Y. Sup. Ct. 1980) ("Notwithstanding the fact that coverage may, . . . withheld from the named insured or an omnibus insured actually responsible for the commission of the assault or directing

Ninth Circuit Court of Appeals embraced the same rule, even though one general partnership rule is very clear: “[A]ll partners in a partnership are bound by the fraud of one or any of them acting within the scope of his authority in a partnership transaction with an innocent third-party and for all responsible for the injury occasioned thereby.”⁶⁵¹

On the other hand, the decision in *Miele v. Zurich U.S.* presents the counterview among partnership cases.⁶⁵² In *Miele*, John and Catherine Murray filed a complaint against Timothy and Linda Miele.⁶⁵³ The Miele’s couple formed a husband-and-wife partnership in Tennessee, doing business as Miele Homes.⁶⁵⁴ The third-party complaint alleged that the Mieles poorly constructed the Murrays’ house.⁶⁵⁵ Several causes of action also appeared in the complaint.⁶⁵⁶ A jury found that the Mieles breached the construction contract by refusing to make the repairs.⁶⁵⁷ In addition, the jury found that John Miele was negligent and that his actions were deceptive, unfair, and willful.⁶⁵⁸ Citing the Tennessee Consumer Protection Act, the trial court trebled the actual damages and awarded \$295,500 to the third-party complainants.⁶⁵⁹

Maryland Insurance Group (Maryland Insurance) insured the partnership and the Mieles under a commercial general liability insurance contract.⁶⁶⁰ The Mieles submitted the Murrays’ complaint to Maryland Insurance.⁶⁶¹ Maryland Insurance paid only \$40,254.45 of the judgment

it to be committed, . . . , it is illogical to indiscriminately exclude from coverage all insureds whenever an assault is committed, without distinguishing the responsibility, if any, of the particular insured for that specific assault.”), aff’d, 78 A.D.2d 549, 432 N.Y.S.2d 29 (N.Y. App. Div. 1980); *Employers Surplus Lines v. Stone*, 388 P.2d 295, 298 (Okla.1963) (partner who personally committed the assault is precluded from recovering under a liability policy, but co-partner who did not commit the assault should be indemnified.).

651. Cf. *Dart Indus., Inc. v. Liberty Mut. Ins. Co.*, 484 F.2d 1295, 1297 (9th Cir. 1973) (stressing that § 533 does not bar coverage where a corporation’s liability is based upon respondeat superior.). See *Stout v. Turney*, 586 P. 2d 1228, 1231 n. 6 (Cal. 1978); see also *Hallett v. St. Paul Fire and Marine Ins. Co.*, 749 P.2d 196, 199 (Wash. Ct. App. 1988) (“Given its clear meaning, the provision is not unreasonable. It provides coverage for the firm and the partners in those situations where the firm and individual partners are found vicariously liable for the tort of one of the partners while driving his own auto. It avoids the obviously increased risk of providing individual coverage for the partner who is the tortfeasor. To construe the policy as providing personal liability coverage for the tortfeasor partner would amount to providing excess liability insurance coverage for the personal automobile liability of all of the partners in the firm for \$547 per year. The policy language makes it clear that Willhite’s personal liability to Hallett is not covered by the St. Paul policy).

652. *Miele v. Zurich U.S.*, 98 S.W.3d 670, 670 (Tenn. Ct. App. 2002).

653. *Id.* at 674.

654. *Id.* at 672.

655. *Id.* at 671.

656. *Id.* (claiming that plaintiffs were negligent, breached their contract, violated the Tennessee Consumer Protection Act, used deceptive or unfair practices, and failed to repair poor workmanship).

657. *Id.*

658. *Id.* at 674.

659. *Id.* at 672.

660. *Id.*

661. *Id.*

and refused to pay the additional \$254,745.55.⁶⁶² Shortly thereafter, the Mieles sued Zurich U.S., the successor-in-interest to Maryland Insurance.⁶⁶³ The Mieles alleged that Maryland Insurance breached its duty to fully indemnify the Mieles.⁶⁶⁴

“Under Tennessee’s law, partners are liable for the wrongful acts of their co-partners.”⁶⁶⁵ As a consequence, Mr. Miele’s liability is imputed to Ms. Miele’s and both are responsible for the personal injuries of John and Catherine Murray.⁶⁶⁶ In light of that rule, the Tennessee Court of Appeals concluded that Linda Miele “was not an innocent co-insured because the liability imposed on [John] Miele was imputed to [her] as a partner in Miele Homes.”⁶⁶⁷ Therefore, the appellate court declared that Zurich U.S. did not have to indemnify Linda Miele.⁶⁶⁸

Finally, in employer-employee cases, the Ninth Circuit and the Texas and Louisiana Courts of Appeals have declared that liability insurers do not have to indemnify or defend innocent employers who might be vicariously liable for their deviant employees’ intentional or negligent acts.⁶⁶⁹ Another group of courts have embraced or fashioned a pro-employers rule.⁶⁷⁰ In particular, the Seventh and Eighth Circuits, one federal district court, and appellate courts in North Carolina and Oregon, forced insurers to indemnify and/or defend factually innocent employers that are vicariously liable.⁶⁷¹

662. *Id.*

663. *Id.*

664. *Id.*

665. *Id.* at 675.

666. *Id.*

667. *Id.*

668. *Id.* at 675.

669. *See Vons Companies, Inc. v. Fed. Ins. Co.*, 212 F.3d 489, 492-93 (9th Cir. 2000) (“Vons’s policy did not provide coverage for third-party claims. We hold that ‘direct’ means ‘direct’ and that in the absence of a third-party claims clause, Vons’s policy did not provide indemnity for vicarious liability for tortious acts of its employee.”) (citations omitted); *King v. Dallas Fire Ins. Co.*, 27 S.W.3d 117, 130 (Tex. App.—Houston [1st Dist.] 2000) (concluding that the insurer had no duty to defend the vicariously liable employer after finding: (1) the employee’s victimization of a third-party was not an “accident” or and “occurrence” under the policy; and (2) the third-party vicarious liability claim and the employer’s allegedly negligent hiring, training, and supervision of the employee were inextricably related to the employee’s intentional tort); *McNamara v. Augustino Bros., Inc.*, 13 So.3d 736, 743, *6 (La. Ct. App. 2009) (declaring that employees’ criminal acts exclusion in policy excluded coverage for employees’ alleged theft; insurer was not required to indemnify contractor under theory of vicarious liability; and the breach-of-contract exclusion provision in the insurance contract barred coverage from the third-party victim’s negligent breach-of-contract claim).

670. *See cases cited infra* note 671.

671. *See Roman Catholic Diocese of Springfield v. Maryland Cas. Co.*, 139 F.3d 561, 567 (7th Cir. 1998) (concluding that the liability insurer had a duty to defend Roman Catholic Diocese against the parent’s allegations that a former priest abused their children); *Silverball Amusement, Inc. v. Utah Home Fire Ins. Co.*, 33 F.3d 1476, 1476 (8th Cir.1994) (concluding that under Arkansas the insurer had a duty to indemnify the employer and defend the employer’s allegedly negligent hiring and supervision, even though the employee intentionally sexually molested a child); *Lutheran Benevolent Ins. Co. v. Nat. Catholic Risk Retention Group, Inc.*, 939 F. Supp. 1506, 1514 (N.D. Okla. 1995) (concluding that under Oklahoma law the insurer had a duty to indemnify and that the church’s alleged negligence in retaining a priest, after learning the priest had sexually molested a child, was covered event under the church’s

VII. A PLAUSIBLE STRATEGY TO HARMONIZE CONFLICTING
DECLARATORY JUDGMENTS AND RULINGS REGARDING INNOCENT AND
CO-INSURED FIDUCIARIES' RIGHTS UNDER PROPERTY AND LIABILITY
INSURANCE CONTRACTS

As discussed in this article, federal and state courts have employed a variety of equitable and legal doctrines to decide whether insurers have a duty to indemnify innocent co-insured fiduciaries.⁶⁷² Some courts based their decisions on whether the fiduciaries' insured property interest was community property, a tenancy in common, or a tenancy in the entirety.⁶⁷³ Many courts consider whether innocent and deviant co-insured fiduciaries formed a principal-agency relationship.⁶⁷⁴ A third group of federal and state courts consider whether innocent fiduciaries had a contractual obligation to prevent deviant co-insured fiduciaries from destroying insured property interests.⁶⁷⁵ Several tribunals asked whether the co-insured fiduciaries' insurable interests and general obligations were joint or severable under first and third-party insurance contracts.⁶⁷⁶ Another group of tribunals wanted to know whether the exclusion or the severability clause in the insurance policy was superior or inferior.⁶⁷⁷ Still, other courts wanted

liability policy that defined "occurrence" as an accident); *Edwards v. Akion*, 279 S.E.2d 894, 897 (N.C. App. 1981) (finding that a city's employee's intentional torts, while acting within the scope of his duties, were "occurrences" within the meaning of the church's liability policy and the insurer had a duty to defend the city against the third-party); *Albertson's Inc. v. Great Sw. Fire Ins. Co.*, 732 P.2d 916, 918 (Or. App. 1987) (declaring that under Oregon law the insurer had a duty to defend a retail store against customer's allegations of tortious conduct because such conduct, when viewed from the standpoint of the insured employer, could reasonably fall within the definition of "accident" and "occurrence" for purposes of policy coverage).

672. See discussion *supra* Parts II-IV.

673. See, e.g., *Kosior v. Cont'l. Ins. Co.* 13 N.E.2d 423, 424-25 (Mass. 1938); *Klemens v. Badger Mut. Ins. Co. of Milwaukee*, 99 N.W.2d at 867; *Cooperative Fire Ins. Ass'n of Vermont v. Domina*, 399 A.2d 502, 503 (Vt. 1979); *Rockingham Mut. Ins. Co. v. Hummel*, 250 S.E.2d 774, 776 (Va. 1979).

674. Cf. *Mut. Life Ins. Co. of New York v. Estate of Wesson*, 517 So. 2d 521, 535 (Miss. 1987) (unless otherwise agreed, a principal is subject to a duty to exonerate an agent who is not barred by the illegality of his conduct to indemnify him for . . . expenses of defending actions by third persons brought because of the agent's authorized conduct, such actions being unfounded but not brought in bad faith . . .").

675. See *Hummel*, 250 S.E.2d 774, 776 (Va. 1979) (concluding that under joint insurance each spouse had a "joint obligation to use all reasonable means to save and preserve the property [and that] "each spouse had the joint duty to refrain from defrauding the insurer"); see also *Matyuf v. Phoenix Ins. Co.*, 27 Pa. D. & C. 2d 351, 361-63 (1933) (declaring that if either insured spouse violated any contractual duties, the breach was chargeable to the Named Insured and prevented either spouse from recovering any amount under the policy).

676. See *Ponder v. Allstate Ins. Co.*, 729 F. Supp. 60, 61 (E.D. Mich. 1990) (concluding that a policy is void only for the deviant insured and that an innocent insured may still recover); *Chacon v. Am. Family Mut. Ins. Co.*, 788 P.2d 748, 750 (Colo. 1990) (concluding that the innocent fiduciary could not recover because contract obligation was joint); see also *Morgan v. Cincinnati Ins. Co.*, 307 N.W.2d 53, 54-55 (Mich. 1981) (declaring that a statutory standard concealment/fraud clause created separate obligations).

677. Compare *J.G. v. Wangard*, 753 N.W.2d 475, 489 (Wis. 2008) (concluding that the exclusionary clause excluded the innocent spouses recovery even though the severability clause stated

to determine whether innocent co-insured fiduciaries were vicariously liable for their co-fiduciaries' intentional or criminal acts.⁶⁷⁸

Yet, as reported throughout this article, judicial conflicts over whether insurers have a duty to indemnify innocent co-insured fiduciaries are continual and widespread.⁶⁷⁹ Therefore, it is reasonable to conclude that the aforementioned equitable and legal doctrines do not explain those conflicts.⁶⁸⁰ In fact, one could argue that those theories and accompanying legal analyses serve as nurseries for, if not the exact sources of, the persistent conflicting declaratory judgments.⁶⁸¹ Therefore, the author hypothesized that extralegal factors might be producing these major and confusing splits among state and federal courts.

Of course, the author based his hypothesis on a curious and wholly unexpected discovery during an initial and cursory review of co-insured fiduciary decisions. Briefly stated, among community property cases, state and federal courts were more likely force property insurers to indemnify co-insured fiduciaries when the latter were innocent wives.⁶⁸² However, when co-insured fiduciaries were innocent husbands, courts were more likely to conclude that property insurers did not have to indemnify the co-insured.⁶⁸³

Therefore, in light of that cursory examination and unexpected finding, the author decided to conduct a full empirical study to determine whether federal and state courts were allowing extralegal factors, i.e. spouses' gender, types of insurance contracts, types of innocent and co-insured fiduciaries, types of insured property interests, fiduciaries' geographic locations, etc. to influence statistically and significantly, courts' dispositions on duty-to-indemnify cases. Thus, this part of the article discusses the empirical study's methodology, reports the statistical findings

that "[c]overage applies separately to each covered person"), with *Gulmire v. St. Paul Fire & Marine Ins. Co.*, 674 N.W.2d 629, 640 (Wis. Ct. App. 2003) (concluding that a severability clause required coverage despite the presence of an exclusionary clause in the policy). See also *Michael Carbone, Inc. v. Gen. Accident Ins. Co.*, 937 F. Supp. 413, 418 (E.D. Pa. 1996) ("[T]he vast majority of jurisdictions which have addressed the issue . . . hold that the severability doctrine or a separation of insureds clause modifies the meaning of an exclusion phrased in terms of 'the insured.' These cases hold that the exclusion will only be effective if it applies with respect to the specific insured seeking coverage.") (citing *Float-Away Door Co. v. Continental Casualty Co.*, 372 F.2d 701, 708 (5th Cir.), cert. denied, 389 U.S. 823 (1967); *Phoenix Assur. Co. v. Hartford Ins. Co.*, 488 P.2d 206, 208 (Colo. App. 1971); *Shelby Mut. Ins. Co. v. Schuitema*, 183 So. 2d 571, 574 (Fla. Dist. Ct. App. 1966), *aff'd per curiam*, 193 So. 2d 435 (Fla. 1967); *Pennsylvania Nat'l Mut. Casualty Ins. Co. v. Bierman*, 292 A.2d 674, 678-79 (Md. 1972); *American Nat'l Fire Ins. Co. v. Estate of Fournelle*, 472 N.W.2d 292, 294 (Minn. 1991); *Travelers Ins. Co. v. Auto-Owners Ins. Co.*, 203 N.E.2d 846, 850 (Ohio App. 1964); *Commercial Standard Ins. Co. v. American General Ins. Co.*, 455 S.W.2d 714, 721 (Tex. 1970); and *Bankers & Shippers Ins. Co. v. United States Fire Ins. Co.*, 224 S.E.2d 312, 317 (Va. 1976)).

678. See discussion *supra* Part V.

679. See discussion *supra* Part V.

680. See discussion *supra* Parts II-IV.

681. See *supra* Part V.

682. See Table 3, *infra* at note 738.

683. See *id.*

in several tables, and discusses the relevance of those findings for courts, practitioners, and co-insured fiduciaries.⁶⁸⁴

A. Source of Data, Sampling Procedures, and Background Characteristics of Co-Insured Fiduciaries and Insurers

Again, the general hypothesis that propelled this study is simple: No statistically significant relationship exists between innocent co-insured fiduciaries' likelihood of winning duty-to-indemnify actions in declaratory judgment hearing and those fiduciaries background attributes.⁶⁸⁵ Therefore, combing reporters and other legal sources as well as using Lexis-Nexis and Westlaw, efforts were made to find and read every reported and unreported duty-to-indemnify and innocent co-insured fiduciary case. Those efforts produced 201 innocent co-insured fiduciaries decisions.⁶⁸⁶ Furthermore, a stratified random sampling generated an additional 329 non-coinsured fiduciary duty-to-indemnify cases. Therefore, the case study is based on 530 state and federal declaratory judgments and rulings which were decided between 1845 and 2009.⁶⁸⁷

1. Demographic Characteristics and Bivariate Relationships Between the Disposition of Duty-to-Indemnify Actions and the Attributes of Co-Insured Fiduciaries and Other Insured Persons

TABLE 1 illustrates some demographic characteristics of co-insured fiduciaries and other insured persons.⁶⁸⁸ There are six columns of statistics. The two far-left columns appear under the heading, *Innocent Spouses* (N = 115).⁶⁸⁹ The two middle columns appear under the heading, *Innocent Co-Insureds* (N = 86).⁶⁹⁰ The two far-right columns of statistics appear under the heading, *Other Insured Persons* (N = 329).⁶⁹¹

684. See *infra* Part VII.A.

685. See *supra* Part I.

686. See Table 1, *infra* note 692.

687. The findings and discussion presented in Part VII are derived from and based on the statistical analysis of 530 declaratory judgments and rulings. See Willy E. Rice, *Destroyed Community Property, Damaged Persons and Insurers' Duty to Indemnify Innocent Spouses and Co-Insured Fiduciaries—An Attempt to Harmonize Conflicting Federal and State Courts' Declaratory Judgments* (an unpublished working paper and statistical reports—on file with the author). All statistical procedures, reports, databases and results associated with this presentation are on file with the author.

688. See Table 1, *infra* note 692.

689. *Id.*

690. *Id.*

691. *Id.*

TABLE 1. SELECTED DEMOGRAPHIC CHARACTERISTICS OF INNOCENT CO-INSURED AND INSURED-INNOCENT SPOUSES WHO COMMENCED DECLARATORY-JUDGMENT SUITS AGAINST INSURERS IN STATE AND FEDERAL COURTS — 1845-2009 (N = 530)

Demographics	Innocent Spouses (N = 115)		Innocent Co-Insureds (N = 86)		Other Insured Persons (N = 329)	
	N	Per cent	N	Per cent	N	Per cent
Types of States:						
Community-Property						
California	5	4.5	6	7.0	19	5.8
Louisiana	4	3.5	38	44.2 ***	24	7.3
Texas	16	13.9 ***	2	2.3	26	7.9
Wisconsin	13	11.3	3	3.5	11	3.3
Other	8	7.0	9	10.5	15	4.5
Separate-Property	69	60.0 ***	28	32.6	234	71.1 ***
Federal Circuits:						
Fifth Circuit	23	20.0	43	50.0 ***	57	17.3
Ninth Circuit	14	12.2	11	12.8	41	12.6
Other Circuits	78	67.8 ***	32	37.2 ***	231	70.2 ***
Types of Insurance Contracts:						
Fire Insurance	102	88.7 ***	30	34.8 ***	1	.3
Homeowners' Insurance	6	5.2	4	4.6	22	6.7
Auto Insurance	3	2.6	44	51.2 ***	14	4.3
Liability Insurance	3	2.6	6	7.0	258	78.4 ***
Other	1	.9	2	2.3	34	10.3
Types Insurable Interests:						
Property Interests						
Jointly-Owned Property	44	38.3	24	27.9	-0-	-0-
Tenants Entirety & Common	29	25.2	1	1.2	-0-	-0-
Community Property	32	27.8	-0-	-0-	-0-	-0-
Other Insurable Interests	10	8.7	61	70.9	329	100.0
Types of Plaintiffs:						
Insured Innocent Wives	95	82.6	-0-	-0-	-0-	-0-
Insured Innocent Husbands	20	17.4	-0-	-0-	-0-	-0-
Partnerships & Joint Ventures	1	.9	11	12.8	5	1.5
Corporations/Small Business	-0-	-0-	13	15.1	208	63.2
Trustees & Administratrix	-0-	-0-	5	5.8	2	.6
Third-Party Plaintiffs	-0-	-0-	31	36.0	10	4.4
Lenders & Mortgagees	-0-	-0-	31	36.0	10	4.4
Excess Insurers	-0-	-0-	-0-	-0-	25	7.6
Professions & Associations	-0-	-0-	-0-	-0-	11	3.3
Educational Institutions	-0-	-0-	31	36.0	10	4.4
Municipal Governments	-0-	-0-	-0-	-0-	15	4.6
Various Other Insureds	-0-	-0-	19	22.1	35	10.6

*** Chi square test statistically significant at $p \leq .0001$

692. Willy E. Rice, SELECTED DEMOGRAPHIC CHARACTERISTICS OF INNOCENT CO-INSURED AND INSURED-INNOCENT SPOUSES WHO COMMENCED DECLARATORY JUDGMENT SUITS AGAINST INSURERS IN STATE AND FEDERAL COURTS — 1845-2009 [hereinafter Table 1].

Comparing the three columns of percentages reveals some notable findings. The percentages illustrate the distributions of the three groups of litigants by *Types of States*, by *Federal Circuits*, by *Types of Insurance Contracts*, by *Types of Insurable Interests* and by *Types of Plaintiffs*.⁶⁹³ First, among the *innocent-spouses* and *other-insureds* cases, the largest proportion of duty-to-indemnify disputes originated in separate property states. The reported percentages are 60% and 71.1%, respectively.⁶⁹⁴ On the other hand, among *innocent-coinsureds* cases, only 32.6% of the cases originated in separate property states.⁶⁹⁵ Instead, the overwhelming majority of *innocent-coinsureds* disputes evolved in community property states.⁶⁹⁶ Of that number, a significant percentage (44.2%) commenced in Louisiana.⁶⁹⁷

Second, among the three groups of litigants, the largest numbers of disputes involve disputed rights and obligations under very different insurance contracts.⁶⁹⁸ Respectively, *innocent spouses*, *innocent co-insureds*, and *other insureds* were significantly more likely to ask courts to interpret their rights under fire/property, automobile, and liability insurance contracts.⁶⁹⁹ The respective percentages are 88.7%, 51.2%, and 78.4%.⁷⁰⁰

Third, Table 1 also illustrates the *types of insurable interests* under the various insurance contracts.⁷⁰¹ There are two large categories: "property interests" and "other insurable interests."⁷⁰² *Innocent co-insured fiduciaries* and *other insured persons* were more likely to purchase insurance contracts to cover non-property interests.⁷⁰³ The percentages are 70.9% and 100% respectively.⁷⁰⁴ Conversely, *innocent spouses* were more likely to insure their property interests.⁷⁰⁵ More specifically, innocent spouses insured *jointly owned tenancies in common and/or by the entirety*, and *community property* in greater numbers than the other two groups of complainants.⁷⁰⁶ The reported percentages are 38.3%, 25.2%, and 27.8% respectively.⁷⁰⁷

Finally, Table 1 also presents specific descriptions of plaintiffs within the three large groups of complainants.⁷⁰⁸ Among *innocent spouses* cases, *co-insured wives* and *husbands* comprised 82.6% and 17.4% of the

693. *See id.*

694. *Id.*

695. *Id.*

696. *Id.*

697. *Id.*

698. *Id.*

699. *Id.*

700. *Id.*

701. *See id.*

702. *See id.*

703. *See id.*

704. *Id.*

705. *Id.*

706. *Id.*

707. *Id.*

708. *See id.*

plaintiffs, respectively.⁷⁰⁹ Among *innocent co-insureds* cases, *third-parties*, *lenders/mortgagees*, and *educational institutions* comprised the bulk of those cases.⁷¹⁰ Individually, those subcategories of plaintiffs comprised 36.0% of the total.⁷¹¹ The reported percentages for *partnerships*, *corporations*, and *trustees* are 12.8%, 15.1%, and 5.8%, respectively.⁷¹² Among *other insured persons, corporations and small businesses* were the largest category comprising 63.2% of plaintiffs.⁷¹³

Table 2 displays co-insured fiduciaries' and other insureds' pleadings and theories of recovery as well as insurers' affirmative defenses.⁷¹⁴ In addition, Table 2 identifies the courts where litigants initiated their actions and reports the disposition of the cases in those courts.⁷¹⁵

709.

710.

711.

712.

713. *Id.*

714. *See infra* Table 2, note 716.

715. *Id.*

TABLE 2 INNOCENT CO-INSURED AND INNOCENT SPOUSE LITIGANTS PLEADINGS, THEORIES OF RECOVERY AND SUCCESS RATES IN COURTS — 1845-2009 (N = 530)

Demographics	Innocent Spouses (N = 115)		Innocent Co-Insured (N = 86)		Other Insured Persons (N = 329)	
	N	Per cent	N	Per cent	N	Per cent
Declaratory-Judgments Venues:						
State Courts	96	83.5 ***	71	82.6 ***	107	32.5
Federal Courts	19	16.5	15	17.4	222	67.5 ***
Litigants' Proffered Doctrines of Contract Interpretation						
Insureds' Theories:						
Ambiguity Rule	17	14.8	3	3.5	211	64.1 ***
Reasonable-Expectation Rule	14	12.1	9	10.5	6	1.8
Public Policy	41	35.6 ***	32	37.2 ***	34	10.3
Insurers' Theories:						
Plain-Meaning Rule	4	3.5	5	5.8	48	14.6
Traditional Contract Rules	39	33.9 ***	37	43.0 ***	30	9.1
Insurers' Contract-Based Affirmative Defenses:						
"Intentional Acts"	96	83.5 ***	28	32.6 ***	15	4.6
"Exclusions"	12	10.4	9	10.5	113	34.3 ***
"Breach of Conditions"	4	3.3	8	9.3	24	7.3
An Assortment of Others	3	2.6	41	47.6 ***	177	53.8 ***
Disposition of Actions Across All Trial & District Courts:						
Insureds' "Favorable" Outcomes	44	38.3	36	41.9	135	41.0
Insurers' "Favorable" Outcomes	71	61.7	50	58.1	194	59.0
Disposition of Actions Across All Appellate Courts:						
Insureds' "Favorable" Outcomes	56	54.4	43	51.8	142	49.7
Insurers' "Favorable" Outcomes	47	45.6	40	48.2	144	50.3

*** Chi square test statistically significant at $p \leq .0001$

Of the 530 litigants, some decided to appeal trial and district courts' adverse ruling. Others did not. Thus the percentages for appellate-court outcomes are based on 472 cases — the number of litigants who decided to appeal.

First, *innocent spouses* and *innocent co-insured fiduciaries* were significantly more likely to initiate their complaints in state courts.⁷¹⁷ The percentages are 83.5% and 82.6%, respectively.⁷¹⁸ On the other hand, *other insured persons* were more likely to file their complaints in federal courts.⁷¹⁹ The percentage is 67.5%.⁷²⁰

Second, it is important to remember that both insureds and insurers may commence declaratory judgment suits and ask courts for relief. Therefore, by citing public policy as well as the ambiguity and/or reasonable expectation doctrine, insureds often encourage courts to interpret duty-to-indemnify clauses in favor of the insureds. Conversely, citing the doctrine of plain meaning and/or traditional rules of contract construction and interpretation, insurers make a similar request.

Table 2 presents insureds and insurers' theories of recovery among the three broad categories of cases.⁷²¹ Among *innocent spouses* and *innocent co-insured* cases, *insured petitioners* were more likely to use a *public policy* argument to secure favorable declarations.⁷²² The respective percentages are 35.6% and 37.2%.⁷²³ However, among the same two groups of cases, *insurer-petitioners* were significantly more likely to cite *traditional rules of contract construction and interpretation* to ensure favorable rulings.⁷²⁴ The reported percentages are 33.9% and 43.0%, respectively.⁷²⁵ Among cases entitled "Other Insured Persons," *insured petitioners* commenced the largest number of actions (64.1%)—listing the *ambiguity doctrine* as their theory of recovery.⁷²⁶ *Insurers-petitioners* were more likely to cite the plain meaning doctrine (14.6%) as their theory of recovery.⁷²⁷

Arguably, the *disposition-of-actions* or *outcomes* percentages are the most interesting statistics in Table 2.⁷²⁸ Put simply, those statistics provide a rudimentary answer to this very general question: Who is more likely to prevail in declaratory judgment trials—insureds or insurers? The percentages in Table 2 are clear and consistent. In lower federal and state courts, *insurers* are significantly more likely to win among "*innocent spouses*," "*innocent co-insureds*" and "*other insured persons*" cases.⁷²⁹

717. *See id.*

718. *Id.*

719. *Id.*

720. *Id.*

721. *See id.*

722. *See id.*

723. *Id.*

724. *Id.*

725. *Id.*

726. *Id.*

727. *Id.*

728. *See id.*

729. *Id.*

Insurers' respective percentages across the three groups are 61.7%, 58.1% and 59.0%.⁷³⁰

However, a review of outcomes in federal and state appellate courts reveals significant reversals.⁷³¹ Overall, insureds won more decisions.⁷³² Among "innocent spouses," insureds won 54.4% of the decisions, and among "innocent co-insureds" cases, insureds prevailed in 51.8% of the actions.⁷³³ Furthermore, among cases entitled "other insured person," insureds and insurers won an equal number of cases in federal and state appellate courts.⁷³⁴ The reported percentages in Table 2 are 49.7% and 50.3%, respectively.⁷³⁵

Again, a simple hypothesis was the impetus for this study: No statistically significant relationship exists between innocent co-insured fiduciaries' likelihood of winning duty-to-indemnify disputes and those fiduciaries' background attributes.⁷³⁶ To test that very general hypothesis, several statistics were generated to uncover the bivariate relationship between *five predictor variables* and the *disposition of cases*—win-loss percentages—in state and federal courts.⁷³⁷

Among other features, Table 3 presents four columns of percentages that illustrate the bivariate relationships between innocent fiduciaries' *likelihood of winning/losing* a case and five background attributes.⁷³⁸ The latter variables are (1) *types of insureds*; (2) *locations of federal appellate courts in which all cases originated*; (3) *locations of federal appellate courts in which third-party cases originated*; (4) *names of states—community or separate property—in which all disputes originated*; and (5) *types of insurable interests among fiduciaries who resided in just community property states*.⁷³⁹

730. *Id.*

731. *Id.*

732. *Id.*

733. *Id.*

734. *Id.*

735. *Id.*

736. *See supra* note 687.

737. *See supra* note 687.

738. *See* Willy E. Rice, THE DISPOSITION OF SEPARATELY INSURED AND INNOCENT CO-INSURED'S DUTY-TO-INDEMNIFY ACTIONS BY SELECTED DEMOGRAPHIC CHARACTERISTICS OF THE LITIGANTS [hereinafter Table 3].

739. *Id.*

TABLE 3. THE DISPOSITION OF SEPARATELY INSURED AND INNOCENT CO-INSURED'S DUTY-TO-INDEMNIFY ACTIONS BY SELECTED DEMOGRAPHIC CHARACTERISTICS OF THE LITIGANTS (N = 530)

Selected Demographics	Subcategories	Disposition of Actions From the Perspectives of All Insured Persons			Disposition of Actions From the Perspectives of ONLY Insured Innocent Spouses & Fiduciaries		
		Favorable	Unfavorable	Number (N = 530)	Favorable	Unfavorable	Number (N = 201)
Types of Insureds	Insured Wives	43.7	56.3	(N = 96) **	43.8	56.2	(N = 96) **
	Insured Husbands	15.0	85.0	(N = 20) **	15.0	85.0	(N = 20) **
	Other Insured Persons	41.1	58.9	(N = 414)	41.2	58.8	(N = 85)
Federal Circuits: Pleadings Among All Insureds	Fifth Circuit	43.9	56.1	(N = 123)	39.4	60.4	(N = 66)
	Ninth Circuit	31.8	68.2	(N = 66)	32.0	68.0	(N = 25)
	Other Circuits	41.1	58.9	(N = 341)	41.8	58.2	(N = 110)
Federal Circuits: Pleadings by Various Third Parties & Victims	Fifth Circuit	45.2	54.8	(N = 93)	47.7	52.3	(N = 44)
	Ninth Circuit	26.4	73.6	(N = 87) ***	26.9	73.1	(N = 26)
	Other Circuits	44.6	55.4	(N = 296) ***	46.0	54.0	(N = 87)
Community & Separate Property States' Filings	Louisiana	51.5	48.5	(N = 66)	50.0	50.0	(N = 42)
	Texas	36.4	63.6	(N = 44)	16.7	83.3	(N = 18) **
	Other States	33.3	60.7	(N = 420)	39.7	60.3	(N = 141) **
Insured Interests In ONLY Community Property States	Community Property	25.0	75.0	(N = 32) **	25.0	75.0	(N = 32)
	Other Insurable Interests	44.3	55.7	(N = 167) **	43.1	56.9	(N = 72)

*** Chi square test statistically significant at $p \leq .01$

** Chi square test statistically significant at $p \leq .05$

There were 476 persons comprising this group. These third parties were primarily administrators, estates as legal entities, executors, trustees, assignees, judgment creditors, intended beneficiaries", as well as employees, automobile passengers and other persons whom insureds actually or allegedly victimized.

Once more, there are four columns of percentages in Table 3.⁷⁴⁰ The two far-left columns of percentages appear under the heading, DISPOSITION OF ACTIONS FROM THE PERSPECTIVES OF ALL INSURED PERSONS.⁷⁴¹ Even a cursory review of the two far-left columns of percentages indicates that generally, insureds were more likely to receive unfavorable rather than favorable declarations or rulings.⁷⁴² However, do percentages and reported statistics at the bottom of Table 3 allow one to reject the null hypothesis? The answer is yes. A review of the two far-left columns of percentages show that *types of insureds, the locations of federal appellate courts in which the third-party cases originated, and the types of insurable interests among fiduciaries who resided in just community property states*, “predict” insureds’ likelihood of success.⁷⁴³

Again consider the percentages under the heading, DISPOSITION OF ACTIONS FROM THE PERSPECTIVES OF ALL INSURED PERSONS. The results indicate that: (1) Insured husbands are significantly more likely to receive unfavorable rulings than insured wives, 85% versus 56.3%; and (2) Ninth Circuit plaintiffs who commenced third-party actions against insurers are significantly more likely to lose (73.6%) than those who sued insurers in the Fifth Circuit (54.8%) or in other federal circuits (55.4%).⁷⁴⁴ Also, in community property states, insureds may insure either community property or other types of property interests.⁷⁴⁵ The percentages show that those who insured community property were significantly more likely to receive unfavorable rulings than those who insured other types of property interests, 75% versus 55.7%.⁷⁴⁶

Of course, the distribution of percentages under the heading, DISPOSITION OF ACTIONS FROM THE PERSPECTIVES OF ONLY INNOCENT SPOUSES AND FIDUCIARIES, shows a very similar pattern.⁷⁴⁷ Generally, innocent co-insured spouses and other fiduciaries were significantly more likely to receive unfavorable rather than favorable outcomes.⁷⁴⁸ However, among the five predictor variables, two variables produced more unfavorable outcomes for innocent fiduciaries: (1) innocent co-insured husbands were significantly more likely to receive unfavorable rulings than innocent co-insured wives, 85% versus 56.2%; and (2) innocent co-insured fiduciaries who commenced actions against insurers in Texas were significantly more likely to receive unfavorable declarations (83.3%) than

740. *See id.*

741. *See id.*

742. *See id.*

743. *See id.*

744. *Id.*

745. *Id.*

746. *Id.*

747. *See id.*

748. *See id.*

innocent fiduciaries who sued insurers in Louisiana (50.0%) or in other states (60.3%).⁷⁴⁹

Clearly, these findings answer the general question as to whether federal and state courts allow extralegal variables to influence the disposition of duty-to-indemnify cases when innocent co-insured spouses and fiduciaries sue for declaratory relief. Yes, extralegal factors influence courts' decisions and some variables are likely to produce significantly more unfavorable than favorable results for innocent spouses and other fiduciaries. However, as these bivariate statistics confirm and as discussed throughout this article, federal and state courts appear to be forever divided over whether insurers have a duty to indemnify all sorts of innocent co-insured fiduciaries. Therefore, a second question remains: Whether an analysis of the empirical findings in this study can help jurists to understand or harmonize contradictory, and apparently unexplainable, duty-to-indemnify declarations.

To help answer this final question, consider the percentages and simple statistics appearing in Table 4.⁷⁵⁰ That table illustrates the disposition of separately insured's and innocent co-insured fiduciaries' duty-to-indemnify actions by insurers' affirmative defenses and by various doctrines of contract construction and interpretation.

749. *Id.*

750. See Willy E. Rice, THE DISPOSITION OF SEPARATELY INSURED'S AND INNOCENT CO-INSURED'S DUTY-TO-INDEMNIFY ACTIONS BY INSURERS' AFFIRMATIVE DEFENSES AND DOCTRINES OF CONTRACT CONSTRUCTION AND INTERPRETATION [hereinafter Table 4].

TABLE 4. THE DISPOSITION OF SEPARATELY INSURED AND INNOCENT CO-INSURED'S DUTY-TO-INDEMNIFY ACTIONS BY INSURERS' AFFIRMATIVE DEFENSES AND DOCTRINES OF CONTRACT CONSTRUCTION AND INTERPRETATION (N = 530)

Selected Favorable	Unfavorable (N = 201)	Disposition of Actions From the Perspectives of				Disposition of Actions From the			
		Demographics		Subcategories		ONLY Insured		Innocent Spouses & Fiduciaries	
		Percent	Number	Percent	Number	Favorable	Unfavorable	Favorable	Unfavorable
Insurers' Contract-Based Affirmative Defenses	"No Coverage"	48.7	51.3	(N = 154) **	40.9	59.1	(N = 44) **		
	"An Intentional Act"	37.9	62.1	(N = 174)	38.4	61.6	(N = 146)		
	Other Defenses	36.6	63.4	(N = 202) **	54.5	45.5	(N = 11) **		
Disposition of Declaratory Judgments By Doctrines Applied In State & Federal Trial & District Courts	Reasonable Expectation Rule	55.2	44.8	(N = 29)	52.2	47.8	(N = 23)		
	Ambiguity Rule	41.6	58.4	(N = 231)	35.0	65.0	(N = 20)		
	Plain Meaning Rule	30.0	70.0	(N = 57)	22.2	77.8	(N = 9)		
	General Contract Rules	36.8	63.2	(N = 106)	40.8	59.2	(N = 76)		
Disposition of Declaratory Judgments By Doctrines Applied In State & Federal Courts of Appeals	Public Policy	43.9	56.1	(N = 107)	38.4	61.6	(N = 73)		
	Reasonable Expectation Rule	81.5	18.5	(N = 27) ***	81.8	18.2	(N = 22) **		
	Ambiguity Rule	54.6	45.4	(N = 207) ***	58.8	41.2	(N = 17) **		
	Plain Meaning Rule	21.2	78.8	(N = 52) ***	11.1	88.9	(N = 9)		
	General Contract Rules	46.1	53.9	(N = 89)	44.1	55.9	(N = 68) **		
	Public Policy	55.7	43.3	(N = 97) ***	57.1	42.9	(N = 70) **		

*** Chi square test statistically significant at $p \leq .01$

** Chi square test statistically significant at $p \leq .05$

Of 530 cases in the total sample, litigants appealed 472 to state and federal appellate courts. Of this latter number, there are 186 appellate cases for insured innocent spouses and innocent co-insured persons.

Like Table 3, the two far-left columns of percentages in Table 4 appear under the heading, "DISPOSITION OF ACTIONS FROM THE PERSPECTIVES OF ALL INSURED PERSONS", and the two far-right columns of percentages appear under the heading "DISPOSITION OF ACTIONS FROM THE PERSPECTIVES OF ONLY INNOCENT SPOUSES AND FIDUCIARIES."⁷⁵¹

First, consider the doctrines of interpretation that state trial courts and federal district courts employed to decide whether insurers had a duty to indemnify. Significantly, when those lower state and federal courts applied the *doctrine of ambiguity*, the *plain meaning rule*, and *general rules of contract interpretation* or cited *public policy*, the insureds under the heading of "All Insured Persons" were more likely to receive unfavorable, rather than favorable, declarations.⁷⁵² The percentages for unfavorable outcomes are 58.4%, 70.0%, 63.2%, and 56.1%, respectively.⁷⁵³

A close examination of the distribution of percentages for "Innocent Spouses and Fiduciaries" reveals similar outcomes.⁷⁵⁴ Innocent co-insured fiduciaries are significantly more likely to receive unfavorable rulings and declarations when state trial courts and federal district courts apply the *doctrine of ambiguity*, the *plain meaning rule*, and *general rules of contract interpretation*, or when those lower courts cite *public policy*.⁷⁵⁵ The respective percentages are 65.0%, 77.8%, 59.2% and 61.6%.⁷⁵⁶ On the other hand, *insureds generally* and *innocent co-insured fiduciaries specifically* are more likely to received *favorable* declarations when lower state and federal courts apply the *reasonable expectation doctrine*.⁷⁵⁷ The percentages for the two groups of insureds are 55.2% and 52.2% respectively.⁷⁵⁸

Without a doubt, that co-insured fiduciaries and insureds generally are more likely to receive unfavorable decisions when state trial courts and federal district courts apply the doctrine of ambiguity is somewhat surprising.⁷⁵⁹ Briefly put, the rule is clear: A dispute arises about the meaning of ambiguous terms in an insurance contract's duty-to-pay or duty-to-indemnify clause, courts must construe the language against the insurer and in favor of the insureds.⁷⁶⁰ Arguably, the greater majority of lower courts in this study did not embrace and apply that rule in favor of the

751. See Table 3, *supra* note 738; Table 4, *supra* note 750.

752. Table 4, *supra* note 750.

753. *Id.*

754. *Id.*

755. *Id.*

756. *Id.*

757. *Id.*

758. *Id.*

759. See *id.*

760. See *id.*

insureds.⁷⁶¹ Perhaps that failure generated or contributed to the number of conflicting decisions overall.

However, the last five rows of percentages in Table 4 strongly suggest that the documented duty-to-indemnify splits among or between state and federal courts of appeals may be attributed to those tribunals properly and consistently applying various doctrines of interpretation.⁷⁶² The evidence in TABLE 4 is rather compelling. First, consider the doctrines of interpretation that state and federal appellate courts used to declare whether insurers had a duty to indemnify. Specifically, when *state and federal courts of appeals* applied the *doctrine of reasonable expectation*, the *doctrine of ambiguity*, and cited *public policy*, “all insured persons” were more likely to receive favorable, rather than unfavorable declarations.⁷⁶³ The percentages for favorable outcomes are 81.5%, 54.6.0%, and 55.7%, respectively.⁷⁶⁴ Of course, when those appellate courts applied the *doctrine of plain meaning* and *traditional rules of contract construction and interpretations*, “all insured persons” were significantly more likely to lose. The respective percentages are 78.8% and 53.9%.⁷⁶⁵

Furthermore, a close analysis the distribution of percentages for “Innocent Spouses and Fiduciaries” discloses very similar win/loss patterns.⁷⁶⁶ To illustrate, innocent co-insured fiduciaries are significantly more likely to receive *favorable* declarations when state and federal appellate courts applied the *doctrine of reasonable expectation*, the *doctrine of ambiguity*, and cited *public policy*.⁷⁶⁷ The percentages for innocent fiduciaries’ *favorable* outcomes are 81.8%, 58.8.%, and 57.1% respectively.⁷⁶⁸ Conversely, innocent co-insured fiduciaries and spouses were significantly more likely to receive *unfavorable* declarations when state and federal courts of appeals again applied the *doctrine of plain meaning* and *traditional rules of contract construction and interpretations*.⁷⁶⁹ The respective percentages are 88.9% and 55.9%.⁷⁷⁰

761. *See id.*

762. *See id.*

763. *Id.*

764. *Id.*

765. *Id.*

766. *See id.*

767. *See id.*

768. *Id.*

769. *See id.*

770. *Id.*

2. *A Multivariate, Two-Stage Probit Analysis—A Review of the Concurrent Relationships Between Several Predictors and the Disposition of Duty-to-Indemnify Cases in State and Federal Declaratory Judgment Trials*

Certainly, Tables 3 and 4 presented some statistically significant, bivariate relationships between the disposition of controversies and background variables.⁷⁷¹ However, although those simple statistical findings are meaningful, they are only descriptive and not predictive. In addition, simple bivariate statistical procedures do not test for “selectivity bias,” a potential source of error in sample data.⁷⁷² Also, simple descriptive statistics do not measure the simultaneous effects of each individual variable on the disposition of declaratory judgment actions.

Therefore, if a researcher does not employ a statistical procedure to *control for the simultaneous influences of multiple factors* on the disposition of cases, the investigator is precluded from saying anything conclusive about each variable’s unique predictive power. Consequently, a more powerful or robust statistical procedure is required. A multivariate, two-staged probit analysis is one statistical procedure that a researcher can use to measure the simultaneous influences of multiple factors; that procedure was employed in this study.⁷⁷³

771. See Table 3, *supra* note 738; Table 4, *supra* note 750.

772. See Willy E. Rice, *Judicial and Administrative Enforcement of Individual Rights Under the National Labor Relations Act and Under the Labor-Management Relations Act Between 1935 and 1990—An Historical and Empirical Analysis of Unsettled Intercircuit and Intracircuit Conflicts*, 40 DEPAUL L. REV. 653, 730-34 (1991); Willy E. Rice, *Race, Gender, “Redlining,” and The Discriminatory Access to Loans, Credit, and Insurance: An Historical and Empirical Analysis of Consumers Who Sued Lenders and Insurers in Federal and State Courts, 1950-1995*, 33 SAN DIEGO L. REV. 583, 692-93 (1996). After insurers refuse to indemnify innocent co-insured fiduciaries or any insured person, some insured fiduciaries might *decide not to secure a declaratory judgment* in a federal district court or in a state trial court. On the other hand, other insured persons or co-insured fiduciaries might *decide to commence* an action. Also, among those deciding to petition a lower court for relief, some insureds will be successful, but other insureds will not prevail. It is very likely the unsuccessful insureds would appeal their adverse declarations to a state or a federal appellate court. Briefly stated, a co-insured fiduciary or any insured person’s decision to file the initial action—as well as that person’s decision to appeal an adverse ruling—is called “self selection.” Therefore, the statistical error that “self selection” might produce is called “selectivity bias.” A prudent investigator must use a more powerful statistical procedure that tests for selectivity bias in the sample data. Here is another brief example of potential selectivity bias: A researcher discovers that courts of appeals are significantly less likely to award declaratory relief to innocent co-insured husbands and more likely to award relief to innocent co-insured wives. At that point, the researcher might conclude that judges are biased against innocent co-insured husbands. However, the investigator must be certain that the population of innocent co-insured husbands, *those who appealed an adverse declaration*, is not statistically different from the population of innocent co-insured husbands *who decided not to appeal an adverse declaration*. Just maybe there could be something extremely “deficient” about the unsuccessful innocent co-insured husbands or about the merits of their complaints. Judicial bias or prejudice, therefore, would not be the correct explanation of innocent co-insured husbands’ lack of success in courts of appeals or in district or trial courts. In other articles, the author discusses and presents examples of selectivity bias.

773. The author has discussed and used this statistical procedure to analyze multiple sets of sample data, and those statistical findings and analyses appear in several published articles. See Willy E. Rice, *Insurance Contracts and Judicial Discord Over Whether Liability Insurers Must Defend Insureds*,

Table 5 presents the results of a single multivariate model.⁷⁷⁴ It includes fifteen predictor variables: *Types of Insured Person*—two categories; *Types of Insurable Interests*—two categories; *Types of Property Insurance Contracts*—two categories; *Location of State Appellate Courts*—two categories; *Location of Federal Courts of Appeals*—two categories; *Affirmative Defense*—“No Coverage”; *Types of Legal Doctrines*—three categories; and a *Lambda Term*—the test for selectivity bias.⁷⁷⁵

Allegedly Intentional and Immoral Conduct: A Historical and Empirical Review of Federal and State Courts, Declaratory Judgments—1900-1997, 47 AM. U.L. 1131, 1212 nn.386-87 (1998); Willy E. Rice, *Federal Courts and the Regulation of the Insurance Industry: An Empirical and Historical Analysis of Courts, Ineffectual Attempts to Harmonize Federal Antitrust, Arbitration, and Insolvency Statutes with the McCarran-Ferguson Act—1941-1993*, 43 CATH. U. L. REV. 399, 445-49 nn. 212-19 (1994); Willy E. Rice, *Judicial Bias, the Insurance Industry and Consumer Protection: An Empirical Analysis of State Supreme Courts, Bad-Faith, Breach-of-Contract, Breach-of-Covenant-of-Good-Faith and Excess-Judgment Decisions, 1900-1991*, 41 CATH. U. L. REV. 325, 369-77 nn. 157-60 (1992).

774. See Table 5, *infra* note 776.

775. See Table 5, *infra* note 776.

TABLE 5. INSURERS' DUTY TO INDEMNIFY CO-INSURED & SEPARATELY INSURED PERSONS: THE SIMULTANEOUS EFFECTS OF SELECTED PREDICTOR VARIABLES ON LITIGANTS' DECISIONS TO INITIATE DECLARATORY-JUDGMENT ACTIONS IN STATE AND FEDERAL COURTS AND ON THE CASES' DISPOSITION (N=472)

PREDICTOR VARIABLES	Decision to Appeal to State & Federal Appellate Courts		Disposition of Declaratory- Judgment Actions On Appeal	
	Probit Coefficients (Standard Errors)	Absolute Values of z-Statistics	Probit Coefficients (Standard Errors)	Absolute Values of z-Statistics
Types of Insured Persons:				
Innocent Co-Insureds	.0067 (.0342)	.02	-.0634 (.2346)	.27
Innocent Spouses	.0254 (.0502)	.51	.1650 (.3169)	.52
Types of Insurable Interests:				
Community Property	-.0395 (.0912)	.43	-.3889 (.3359)	1.16
Jointly Owned Property	-.1457 (.0456)	.32	-.1813 (.2519)	.72
Property Insurance Contracts:				
Homeowners' Insurance	-.0625 (.2285)	.27	-1.0218 (.3789)	2.70 **
Fire Insurance	.0315 (.0467)	.67	.1264 (.3111)	.41
State Courts of Appeals:				
New Mexico	.0839 (.2187)	.38	-1.1551 (.6371)	1.81 *
Texas	-.0349 (.0823)	.42	-.3186 (.2835)	1.12
Federal Courts of Appeals:				
Fifth Circuit	.0139 (.0278)	.50	-.0468 (.2025)	.23
Ninth Circuit	.0114 (.0265)	.43	-.0285 (.2011)	.14
Affirmative Defense:				
"No Coverage"	.0256 (.0319)	.08	.1225 (.1456)	.84
Legal Doctrines Applied:				
Reasonable Expectation Rule	.0047 (.1481)	.03	.8414 (.3110)	2.71 **
Plain-Meaning Rule	-.0720 (.2255)	.32	-.9182 (.2139)	4.29 ***
General Contract Rules	-.0206 (.0519)	.40	-.2186 (.1728)	-1.26
Lambda Term (Test for Selectivity Bias)	—	—	.1366 (.3512)	.40
CONSTANT	.8783 (.2511)	3.50 ***	.1375 (.1086)	1.27
Levels of statistical significance: *** p < .0001 ** p < .01 * p = .07				

776. Willy E. Rice, INSURERS' DUTY TO INDEMNIFY CO-INSURED & SEPARATELY INSURED PERSONS: THE SIMULTANEOUS EFFECTS OF SELECTED PREDICTOR VARIABLES ON LITIGANTS' DECISIONS TO INITIATE DECLARATORY JUDGMENT ACTIONS IN STATE AND FEDERAL COURTS AND ON THE CASES' DISPOSITION [hereinafter Table 5].

First, the following is worth repeating: The total sample size for this study is 530 *declaratory judgments and rulings* (N = 530).⁷⁷⁷ Initially, state trial courts or federal district courts decided these controversies. However, 472 *litigants* were dissatisfied with the lower courts' declarations and rulings (N= 472).⁷⁷⁸ As a consequence, those unsuccessful insureds and insurers appealed their adverse declarations and rulings to a federal or a state court of appeals.⁷⁷⁹ Fifty-eight (N = 58) litigants *decided not to appeal*, for reasons unknown.⁷⁸⁰ Most likely, those insureds and insurers were satisfied with the relief that they received in the state trial courts or in the federal district courts.⁷⁸¹

Four distributions of probit coefficients, along with standard errors, and z-statistics are illustrated in Table 5.⁷⁸² The probit values and z-statistics appearing under the heading, *Decision to Appeal to State and Federal Appellate Courts*, answer this question: Whether the multiple and simultaneous effects of the fifteen variables significantly influence insureds' or insurers' respective *decisions to appeal* their adverse declarations and rulings to state and federal courts of appeals.⁷⁸³ The answer is no, because the corresponding z-statistics indicate that *none of the probit values are statistically significant*.⁷⁸⁴ Stated differently, neither of the fifteen predictors had any significant influence on litigants' *decision to appeal or not to appeal* lower courts' rulings.⁷⁸⁵

Of course, there is a more important question: Whether the simultaneous and multiple effects of the fifteen variables are more likely or less likely to influence the disposition of duty-to-indemnify disputes in federal and state courts of appeals.⁷⁸⁶ The answer to that question may be found in Table 5 among the distributions of probit values and z-statistics appearing under *Disposition of Declaratory Judgment Actions On Appeal*.⁷⁸⁷ A careful observation discloses that the *Lambda term* (.1366) is not statistically significant, *suggesting* the absence of selectivity bias in the sample data.⁷⁸⁸ On the other hand, there are *four statistically significant* probit values; three of which are *negative* and one is *positive*.⁷⁸⁹

777. See *supra* note 687.

778. See *supra* note 687.

779. See *supra* note 687.

780. See *supra* note 687.

781. Shelly J. White, A .1, Critique of Texas Rule of Appellate Procedure 25.1, 57 BAYLOR L. REV. 937, 938 (2005) (explaining that people generally do not seek appeal because they are satisfied with the judgment of the trial court).

782. Table 5, *supra* note 776.

783. See *id.*

784. See *id.*

785. See *id.*

786. See *id.*

787. *Id.*

788. *Id.*

789. See *id.*

Consider the negative probit values.⁷⁹⁰ The first one suggests: When examining the *simultaneous influences all predictor variables*, state and federal courts of appeals *are significantly less likely to order property insurers* to indemnify co-insureds or separately insureds who ask appellate courts to interpret *homeowners' insurance contracts*.⁷⁹¹ The corresponding probit value is *-1.0218*.⁷⁹² The second significant and negative probit value (*-1.1551*) strongly suggests that state and federal courts of appeals *are significantly less likely to order* insurers to indemnify co-insured fiduciaries and separately insured persons who reside or commence actions in New Mexico.⁷⁹³

The third negative probit value (*-.9182*) suggests that co-insured fiduciaries and separately insured persons *are less likely to receive favorable declarations* in courts of *appeals* when those tribunals use the *doctrine of plain meaning* to interpret various insurance contracts.⁷⁹⁴ Although the *-.2186* probit value near the bottom of Table 5 is not statistically significant, it lends support to what appears in case law and the finding in Table 4: Co-insured fiduciaries and separately insured persons are also *less likely to receive favorable declarations* when state and federal appellate courts use *general rules of contract* to interpret various insurance agreements.⁷⁹⁵ Furthermore, the positive and statistically significant *.8414* probit coefficient also supports a finding that appears in Table 4: Co-insured fiduciaries and separately insured persons *are more likely to receive favorable declarations* when appellate courts apply the *reasonable expectation doctrine*.⁷⁹⁶

Of course, the present analysis would be incomplete if some of the *statistically insignificant* probit coefficients in Table 5 were not discussed.⁷⁹⁷ Consider, therefore, the general variable *Types of Insured Persons* and the corresponding two probit values: *-.0634* and *.1650*.⁷⁹⁸ The negative value indicates that *innocent co-insured fiduciaries* are likely to lose their duty-to-indemnify actions, but the positive coefficient suggests that *innocent spouses* are more likely to win their actions.⁷⁹⁹

In addition, “community property” and “jointly owned property” appear under the heading, *Types of Insurable Interests*.⁸⁰⁰ The two corresponding probit values, *-.3889* and *-.1813*, are not statistically

790. *See id.*

791. *See id.*

792. *Id.*

793. *Id.*

794. *Id.*

795. *See* Table 5, *supra* note 776; Table 4, *supra* note 750.

796. *See* Table 5, *supra* note 776; Table 4, *supra* note 750.

797. *See* Table 5, *supra* note 776.

798. *Id.*

799. *Id.*

800. *Id.*

significant, suggesting that types of insurable interests are not even marginally relevant as predictors among multiple predictors.⁸⁰¹ However, the bivariate statistics in Table 4 revealed that co-insured persons were statistically and significantly less likely to win duty-to-indemnify cases if they (1) resided in community property states, and (2) insured their community property.⁸⁰²

Finally, there is a general impression that the Fifth Circuit Court of Appeals is a fairly "conservative court."⁸⁰³ Many have concluded that the Ninth Circuit Court of Appeals is a "liberal court."⁸⁰⁴ Therefore, one might conclude that co-insured fiduciaries and other insured persons are more likely to receive favorable outcomes when those insureds sue insurers in the Ninth Circuit.⁸⁰⁵ The converse would be true when co-insured fiduciaries and other insureds sue property and liability insurers in the Fifth Circuit.⁸⁰⁶ A review of Table 5, however, supports neither assumption.⁸⁰⁷

Under the heading *Federal Courts of Appeals*, the two probit values appear.⁸⁰⁸ The first one (-.0468) indicates the effect of litigating a duty-to-indemnify action in the Fifth Circuit, and the second one (-.0285) shows the consequence of litigating in the Ninth Circuit.⁸⁰⁹ However, coefficients are statistically insignificant, revealing that the federal courts of appeals' locations have no effect on whether insureds or insurers win or lose duty-to-indemnify disputes.⁸¹⁰ On the other hand, since those coefficients are negative, one could argue that both the Fifth and Ninth Circuit Courts of

801. *See id.*

802. *See* Table 4, *supra* note 750.

803. *See, e.g.,* Garrick B. Pursley, *Thinking Diversity, Rethinking Race: Toward A Transformative Concept of Diversity in Higher Education*, 82 TEX. L. REV. 153, 172-73 (2003) ("Other factors, such as socioeconomic history, academic background, and extracurricular activities remained legitimate bases for admissions decisions after *Hopwood*. Colleges and universities in the Fifth Circuit simply had to exclude race as one of the factors in their admissions programs. It seems, then, that even the conservative Fifth Circuit recognized the value of fostering an educational atmosphere composed of a variety of experiential backgrounds"); Ruth Colker, *Affirmative Protections for People with Disabilities, Illness and Parenting Responsibilities Under United States Law*, 9 YALE J.L. & FEMINISM 213, 249 (1997) ("Where [a] leave is foreseeable, the FMLA requires that the employee shall provide the employer with not less than thirty days' notice, before the date the leave is to begin. . . . Some courts have applied this rule stringently, requiring an employee to invoke the words 'FMLA' when requesting leave in order to evoke statutory coverage. Even the conservative Fifth Circuit Court of Appeals, however, has recognized that such a rule departs from Congress' intent.").

804. *See, e.g.,* Jonathan C. Lipson, *When Churches Fail: The Diocesan Debtor Dilemmas*, 79 S. CAL. L. REV. 363, 414 (2006) ("*Miller v. Reed* is a good example of the Ninth Circuit's comparatively liberal approach to hybrid rights claims."). *But see* Erwin Chemerinsky, *The Myth of the Liberal Ninth Circuit*, 37 LOY. L.A. L. REV. 1, 2-3 (2003) ("On the other hand, people often forget that, for every liberal on the Ninth Circuit, there is a judge who occupies the exact opposite place on the ideological continuum.").

805. *See supra* notes 803-04.

806. *See* Table 5, *supra* note 776.

807. *See id.*

808. *Id.*

809. *Id.*

810. *See id.*

Appeals would rule against innocent co-insured spouses as well as against other co-insured fiduciaries and separately insured persons.⁸¹¹

VIII. SUMMARY AND CONCLUSION

As discussed earlier, there are several types of fiduciary relationships, comprising various pairs of co-fiduciaries—estates and trustees, executors and administrators, professionals and associates, partners and partnerships, corporations and their officers and directors, employers and employees, business entities, and independent contractors, joint ventures, mortgagors and mortgagees, sellers and buyers, parents and adult children, and husbands and wives.⁸¹² Again, as a matter of law, each commercial or familial fiduciary must act in good faith and protect jointly owned and/or community property interests for the benefit of other fiduciaries.⁸¹³

Of course, many fiduciaries breach their fiduciary obligations.⁸¹⁴ In fact, they become deviant fiduciaries, intentionally or negligently violating public policy as well as criminal and civil laws. As reported above, those violations often jeopardize, undermine, or destroy innocent fiduciaries' property interests.⁸¹⁵ On other occasions, deviant fiduciaries' outrageous actions or inactions partially or totally destroy third-parties' property interests or persons, thereby exposing innocent fiduciaries to vicarious liability.⁸¹⁶

Recognizing that co-fiduciaries may engage in deviant and/or negligent activities, prudent fiduciaries purchase property and/or liability insurance to cover potentially first and third-party property damages and personal injuries.⁸¹⁷ However, based on the research for this article, the findings are conclusive: Fiduciaries generally purchase *standardized* rather than *carefully negotiated* property and liability insurance contracts.⁸¹⁸ Without a doubt, standardized or "boilerplate" insurance contracts are generally replete with archaic, poorly defined, and ambiguous words and phrases.⁸¹⁹ In addition, coverage and duty-to-indemnify provisions in

811. *See id.*

812. *See supra* Part II.

813. *See supra* Part II.

814. *See supra* Part III.

815. *See supra* Part III.

816. *See supra* Part III.

817. *See supra* Part III.

818. *See supra* Part II.

819. *See, e.g., A.M. Vann, Annotation, Loss by Heat, Smoke, or Soot Without External Ignition as Within a Standard Fire Insurance Policy*, 17 A.L.R.3d 1155 (1968) (discussing the archaic and still widely recognized legal distinction between a "friendly" fire and a "hostile" fire); *Insurance—Clause Excepting Loss or Frustration of Venture by Government Restraint Held Inapplicable to Constructive Loss of Goods*, 55 HARV. L. REV. 686, 686 (1942) ("This construction of a standard clause subjects underwriters to shipping losses accompanying the outbreak of war which they may not have anticipated in computing premiums. The frustration clause, couched in the archaic phraseology of marine

standardized property and liability insurance contracts typically contain long and poorly structured sentences.⁸²⁰

Even the most sophisticated fiduciaries fail to appreciate that liability and property insurers intentionally insert archaic words, complicated phrases, and poorly constructed long sentences in contracts for the benefit of insurers.⁸²¹ Furthermore, as discussed earlier, the definition of coverage under property insurance contracts does not comport with a commonsensical layperson's definition, and even legally trained fiduciaries who purchase property insurance contracts fail to understand or appreciate the distinction.⁸²² Perhaps, what is even more egregious is that otherwise prudent, intelligent, competent, and seasoned commercial fiduciaries do not carefully read or understand the major terms and conditions in standardized property and liability insurance contracts before signing those agreements and sending periodic premiums to the insurers.

To be sure, such poorly written, confusing, and complicated boilerplate insurance contracts beg for federal or state courts interpretations.⁸²³ As discussed in this article, state and federal courts have delivered conflicting declarations after reading and construing identical or fairly similar words and phrases in standardized insurance contracts.⁸²⁴ To repeat, for more than 150 years, some federal and state courts have ordered property and liability insurers to indemnify innocent co-insured fiduciaries.⁸²⁵ Other courts, however, have declared that first and third-party insurers have no contractual duty to indemnify innocent fiduciaries in the wake of deviant fiduciaries' destructive acts.⁸²⁶

Again, many ordinary and commonsensical laypersons think it is grossly unfair for insurance companies to benefit from fiduciaries' deviancies.⁸²⁷ After all, insurers and their agents know early on that innocent fiduciaries want and expect to be compensated when co-fiduciaries destroy property and injure persons.⁸²⁸ Therefore, some jurists and commentators have tried to explain state and federal courts' numerous and various conflicting duty-to-indemnify declarations by focusing on the following: (1) whether the deviant co-insured fiduciaries destroyed

insurance, was adopted following a decision in the last war. . . ."). *See also* *Kulukundis v. Norwich Union Fire Ins. Soc'y*, 1 K.B. 2, 34-35 (Eng. C.A. 1937) ("The archaic words of our ancient form of marine policy . . . afford little guidance in the way of description or explanation as to the circumstances which the insurer agrees shall constitute a loss for which he has to pay.") (Comment of Mr. Justice Scott).

820. *See id.*

821. *See id.*

822. *See supra* Part III. A.

823. *See supra* Part IV. B.

824. *See supra* Part IV.B.

825. *See supra* part V.B.

826. *See supra* Part V.A.

827. *See supra* Part V.A.

828. *See supra* Part V.B.

community property, a tenancy by the entirety, a tenancy in common or some other jointly owned property; (2) whether the insurance contract contained a severability clause; (3) whether liability insurance contracts covered innocent co-insured fiduciaries' vicarious liability; (4) whether the property insurance contracts required innocent fiduciaries to protect jointly owned or community property; or (5) whether the liability insurance contracts required innocent fiduciaries to protect third-parties from deviant fiduciaries' destructive intentional and/or negligent acts.⁸²⁹

Yet, after conducting an empirical investigation, the statistical results revealed that those proffered theories, i.e. property interests, severability-of-interests, vicarious-liability and duty-to-protect analyses, do not and cannot explain the conflicts even marginally.⁸³⁰ On the other hand, several statistically significant findings clearly revealed that some extralegal factors, types of property insurance contracts and the locations of state court proceedings, influence courts' decisions.⁸³¹ Arguably, those extralegal variables' effects generate some of the splits.⁸³²

After conducting a conservative and thorough analysis of the empirical study's sample data and statistical findings, the author is reasonably confident that federal and state courts' application of settled insurance-related doctrines explains the duty-to-indemnify splits.⁸³³ Again, stated briefly, insurers are more likely to prevail when courts use traditional rules of contract and the doctrine of plain meaning to interpret duty-to-indemnify, and innocent co-insured fiduciaries are more likely to win duty-to-indemnify controversies when state and federal courts apply the doctrines of ambiguity and reasonable expectations.⁸³⁴

Finally, spouses, executors, trustees, partners, subcontractors, and employers are fiduciaries, and fairly often they are legally required to purchase property insurance to cover jointly owned or community property.⁸³⁵ Under other circumstances, those same fiduciaries must purchase liability insurance that covers third-party claims.⁸³⁶ Understandably, when first- or third-party losses arise, those legally bound fiduciaries expect insurance companies to indemnify them rather than finding and using archaic language in the insurance contract to defeat the fiduciaries' claims.⁸³⁷

829. *See supra* Part V.B.

830. *See supra* Part VII.

831. *See supra* Part VII.A.1.

832. *See supra* Part VII.

833. *See supra* Part VII.

834. *See supra* Part VII.

835. *See supra* Part VII.

836. *See supra* Part VII.

837. *See supra* Part IV.

The essential point, however, is this one: At the very beginning of the bargained-for-exchange process, fiduciaries help insurers to defeat their duty-to-indemnify claims during the contract period.⁸³⁸ How? Arguably, gullible fiduciaries do not invest enough effort or time to understand the “hidden dangers and pitfalls” in standardized insurance contracts. Fiduciaries also do not invest time or effort to negotiate ironclad, clearly written and unambiguous insurance contracts, which will cover fiduciaries’ specific interests and expectations. Until otherwise innocent, highly ethical, prudent, and business savvy fiduciaries become more proactive during the formation of insurance agreements, they will continue to be twice victimized. Deviant co-insured co-fiduciaries will continue to act irresponsibly and destroy or undermine innocent fiduciaries’ various interests, and property and liability insurers will continue to pitch and sell adhesionary and inferior insurance contracts to fiduciaries.

838. *See supra* Part IV.