INSOLVENT INSURERS: WHO WILL BEAR THE BURDEN—THE EXCESS CARRIERS, THE GUARANTY ASSOCIATIONS, OR THE INSURED?

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I. Introduction

As the number of insolvent insurance companies increases, the question continues to arise: who will carry the burden of those companies' obligations? Most states have created guaranty associations or funds to deal with the problem of insolvent insurers.[1] The funds provide coverage up to a specified amount when the primary insurer is insolvent and there is no other insurance coverage.[2] However, the creation of these associations has not solved the problem, since many of the funds limit coverage to a certain dollar amount.[3] Therefore, the question arises: who will assume responsibility for any gaps in coverage between the guaranty association's limits and the excess carrier's lower limit? One solution requires the excess insurer to "drop down" to the guaranty association's limit to eliminate any gap in the insurance coverage. For example, assume there is primary coverage to $500,000, excess coverage from $500,000 to $1.5 million, a guaranty association limit of $300,000, and a judgment for $600,000. If the primary insurer is insolvent, the guaranty association will pay its limit of $300,000, and the excess carrier would pay the remaining $300,000. Another solution requires the excess carrier to drop down in the place of the insolvent primary insurer. In the example above the excess carrier would provide the entire coverage of

1. *See infra* notes 82-83 & 124. The definition of "covered claim" varies from state to state. This note deals with Iowa's Guaranty Association Statute, Iowa Code ch. 515B (1987). In Iowa "covered claim" is defined as "an unpaid claim, including one for unearned premiums, which arises out of and is within the coverage and is subject to the applicable limits of an insurance policy to which this chapter applies issued by an insurer, if such insurer becomes an insolvent insurer . . . ." Iowa Code § 515B.2(3) (1987).

2. *E.g.*, Iowa Code § 515B.2 (1987).

3. *E.g.*, Iowa Code § 515B.5 (1987).

$600,000. The solution most often applied requires the guaranty association to pay its limit of $300,000 and the excess carrier to pay $100,000 to cover that part of the judgment which exceeds $500,000. The insured would be responsible for the $200,000 which is within the primary limits but not covered by either the guaranty fund or the excess carrier.

This note will examine the various rulings on this problem. Some jurisdictions base their rulings on public policy while others base their rulings on policy interpretation.

This author will support the premise that the Iowa Guaranty Association should raise its coverage limit to $500,000. The number of recoveries in excess of $300,000 is on the increase and primary insurance policies very often provide coverage to the $500,000 mark. The excess insurer would still be required to pay its limits at the amount provided for by contract. For example, if excess coverage starts at $400,000 and the judgment is for $500,000, the excess insurer will provide $100,000 of the judgment. To require excess insurers to drop down would be contrary to contract law, as the courts would be reading provisions into insurance policies. Further, the courts should not require the excess carrier to perform the guarantee association's function: to provide coverage where the primary insurer is insolvent.

II. Excess Insurers

A. *Drop-Down Required*

The question of whether an excess insurer should be required to drop down in the place of an insolvent primary insurer has been addressed by a few jurisdictions.[4] The results are anything but consistent. The majority of courts resolve the conflict in favor of the excess carrier, leaving the insured to carry the burden of the insolvent primary insurer.[5] The courts which rule

4. *See, e.g.*, Zurich Ins. Co. v. The Heil Co., 815 F.2d 1122 (7th Cir. 1987); Continental Marble & Granite Co. v. Canal Ins. Co., 785 F.2d 1258 (5th Cir. 1986); Garmany v. Mission Ins. Co., 785 F.2d 941 (11th Cir. 1986); Wright v. Newman, 767 F.2d 460 (8th Cir. 1985); Fried v. The North River Ins. Co., 710 F.2d 1022 (4th Cir. 1983); St. Paul Fire & Marine Ins. Co. v. The Medical Protective Co., 691 F.2d 468 (10th Cir. 1982).

5. *See, e.g.*, Zurich Ins. Co. v. The Heil Co., 815 F.2d 1122 (7th Cir. 1987); Duke Transp., Inc. v. Mission Nat'l Ins. Co., 792 F.2d 550 (5th Cir. 1986); Continental Marble & Granite Co. v. Canal Ins. Co., 785 F.2d 1258 (5th Cir. 1986); Garmany v. Mission Ins. Co., 785 F.2d 941 (11th Cir. 1986); Wright v. Newman, 767 F.2d 460 (8th Cir. 1985); Fried v. The North River Ins. Co., 710 F.2d 1022 (4th Cir. 1983); St. Paul Fire & Marine Ins. Co. v. The Medical Protective Co., 691 F.2d 468 (10th Cir. 1982); Molina v. United States Fire Ins. Co., 574 F.2d 1176 (4th Cir. 1978); Holland v. Stanley Scrubbing Well Serv., 666 F. Supp. 898 (W.D. La. 1987); Radiator Specialty Co. v. First State Ins. Co., 651 F. Supp. 439 (W.D.N.C.), *aff'd*, 836 F.2d 193 (4th Cir. 1987); Guaranty Nat'l Ins. Co. v. Bayside Resort, Inc., 635 F. Supp. 1456 (D.V.I. 1986); Golden Isles Hosp., Inc. v. Continental Casualty Co., 327 So. 2d 789 (Fla. Dist. Ct. App. 1976); United States Fire Ins. Co. v. Capital Ford Truck Sales, Inc., 257 Ga. 77, 355 S.E.2d 428 (1987); Thompson Nat'l Press Co. v. National Union Fire Ins. Co., 16 Mass. App. 242, 451 N.E.2d 432

in favor of drop-down do so on the theory that there is an ambiguity in the excess carrier's policy.[6] The words most often found ambiguous are "amount recoverable" and "collectible."[7] However, while a minority of courts finds those words ambiguous, the majority do not.[8]

The California Supreme Court in *Reserve Insurance Co. v. Pisciotta*[9] found that the words "amounts recoverable" were ambiguous.[10] The court determined that "amounts recoverable" could mean that the excess carrier was to be liable either for "amounts over the dollar limits of the underlying insurance or [for] amounts which the insured is not able to actually recover from the underlying insurer because of its insolvency."[11]

The court in *Pisciotta* declined to hold that drop-down was necessary solely because of the primary carrier's insolvency.[12] In a footnote the court noted a prior California case, *McConnell v. Underwriters at Lloyds*,[13] which required mandatory drop-down. That early decision was distinguished because it pre-dated the creation of the California Insurance Guaranty Association.[14] The court stated that "absent a violation of public policy, a statute, or a constitutional provision, the parties to a private agreement may allocate risks in any manner they choose."[15] Therefore, the court in *Pisciotta* did not base its decision on *McConnell*.[16]

The court in *Pisciotta* stated that the reasonable expectations of the insured are of primary importance in determining the effect of a standardized insurance contract.[17] In most cases the insured will believe that coverage exists if its policy premiums have been paid.[18] These expectations will be limited by a policy exclusion which "clearly and unmistakably communi-

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(1983); Pergament Distribs., Inc. v. Old Republic Ins. Co., 128 A.D.2d 760, 513 N.Y.S.2d 467 (1987); Prince Carpentry, Inc. v. Cosmopolitan Mut. Ins. Co., 124 Misc. 2d 919, 479 N.Y.S.2d 284 (1984); St. Vincent's Hosp. & Medical Center v. Insurance Co. of North America, 117 Misc. 2d 665, 457 N.Y.S.2d 670 (1982).

6. *See, e.g.*, Reserve Ins. Co. v. Pisciotta, 30 Cal. 3d 800, 640 P.2d 764, 180 Cal. Rptr. 628 (1982); MacNeal v. Interstate Fire & Casualty Co., 132 Ill. App. 3d 564, 477 N.E.2d 1322 (1985); Gros v. Houston Fire & Casualty Ins. Co., 195 So. 2d 674 (La. Ct. App. 1967); Gulezian v. Lincoln Ins. Co., 399 Mass. 606, 506 N.E.2d 123 (1987); Massachusetts Insurers Insolvency Fund v. Continental Casualty Co., 399 Mass. 598, 506 N.E.2d 118 (1987).

7. *See* cases cited *supra* note 6.

8. *See supra* notes 4-5.

9. Reserve Ins. Co. v. Pisciotta, 30 Cal. 3d 800, 640 P.2d 764, 180 Cal. Rptr. 628 (1982).

10. *Id.* at 815, 640 P.2d at 772, 180 Cal. Rptr. at 636.

11. *Id.*

12. *Id.* at 815, 640 P.2d at 772, 180 Cal. Rptr. at 637.

13. *Id.* at 814, 640 P.2d at 772, 180 Cal. Rptr. at 636 (citing McConnell v. Underwriters at Lloyds, 56 Cal. 2d 637, 365 P.2d 418, 16 Cal. Rptr. 362 (1961)).

14. *Id.* at 814 n.7, 640 P.2d at 772 n.7, 180 Cal. Rptr. at 636 n.7.

15. *Id.* at 814, 640 P.2d at 772, 180 Cal. Rptr. at 636.

16. *Id.*

17. *Id.* at 809, 640 P.2d at 769, 180 Cal. Rptr. at 633.

18. *Id.*

cates" the exclusion.[19] Here, however, because the insurance contract could be read in two different ways, the exclusion was not clearly communicated and ambiguity was resolved so as to give effect to the insured's expectations.[20]

In *Gulezian v. Lincoln Insurance Co.*, the word "collectible" was held to be ambiguous, and therefore drop-down was required.[21] The primary carrier, Ambassador, provided coverage to $500,000, and the excess carrier, Lincoln Insurance Company, provided an additional $1 million.[22] After Ambassador was declared insolvent, the insured looked to Lincoln for coverage.[23] The language to be interpreted was "over and above sums collectible by the plaintiff pursuant to underlying coverage."[24] Before interpreting this contract clause, however, the court focused on a contract clause which referred to "the total of the applicable limits of liability."[25] The court questioned whether "applicability" could include post-occurrence events, including the insolvency of Ambassador.[26] Further, the excess policy stated that, if the primary insurance was not collectible due to the fault of the insured, there would be no drop-down.[27] However, the policy did not state whether drop-down would occur if the insured was not at fault.[28] Because the policy did not provide for the possibility that the primary insurer would become insolvent, it was ambiguous.[29] Furthermore, "[t]he phenomenon of the insolvency of an insurer is not, however, so rare as to excuse that omission of attention to detail."[30] Therefore, the excess insurer was required to drop-down.[31]

The definition of "collectible" was challenged again in a Louisiana Court of Appeals case, *Poirrier v. Cajun Insulation, Inc.*[32] In *Poirrier* the insolvent primary insurer, Northwest, was liable for $500,000, and the excess insurer, Pacific, for $5 million.[33] The insured argued for coverage because the underlying insurance was not collectible due to Northwest's insolvency.[34] Pacific argued that the term "collectible" used in the policy applied to in-

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19. *Id.*

20. *Id.* The excess insurer was only required to cover the insolvent primary insurer's limits of $100,000 and not the $200,000 from the lapsed policy. *Id.* at 813, 640 P.2d at 771, 180 Cal. Rptr. at 635.

21. Gulezian v. Lincoln Ins. Co., 399 Mass. 606, 506 N.E.2d 123 (1987).

22. *Id.*

23. *Id.* at ___, 506 N.E.2d at 124.

24. *Id.*

25. *Id.*

26. *Id.* at ___, 506 N.E.2d at 126.

27. *Id.*

28. *Id.*

29. *Id.*

30. *Id.*

31. *Id.*

32. Poirrier v. Cajun Insulation, Inc., 501 So. 2d 800 (La. Ct. App. 1986).

33. *Id.* at 806.

34. *Id.* at 807.

surance other than that provided by the primary insurer.[35] The language in question read, "an amount equal to the limits of liability indicated besides the underlying insurance listed in Schedule A hereof [designating Northwest's $500,000 comprehensive liability coverage] plus the applicable limits of *any other* underlying insurance collectible by the Insured."[36] The court interpreted this clause as applicable to the primary insurance because the phrase "any other" referred to the insurance provided by Northwest, which the insured had proven uncollectible.[37] Having proven the primary insurance uncollectible, the insured was able to collect from the excess carrier.[38]

B. *No Drop-Down Required*

The majority of courts which have considered the obligation of an excess insurer when the primary insurer is insolvent have held that there is no requirement that the excess carrier drop-down and provide coverage.[39] Their reasoning is based on explicit policy language, interpretation of policy language, and public policy. As in cases requiring drop-down, the issue presented to the court is whether the terms "collectible" and "amount recoverable" create an ambiguity in the contract.

A recent Michigan case, *Morbark Industries, Inc. v. Western Employers Insurance Co.*, also examined the obligation of the excess insurer where the primary insurer was insolvent.[40] The insured argued that there was an ambiguity because the declarations page definition of underlying limits—"[t]he amount recoverable"—did not state a specific dollar amount.[41] However, the insurance agreement provided: "The provisions of the policy thus state the threshold of liability level thereof as an amount which is the policy limit of the underlying general liability insurance, $1,000,000."[42] The insured's argument was based upon the use of the phrase "amounts recoverable"; the insured maintained that this term spoke to the amount the primary insurer was actually able to pay.[43] The insured, therefore, sought to have the excess carrier drop-down.[44]

The Michigan court rejected the insured's contention.[45] Finding that "amounts recoverable" was not ambiguous, the court adopted the majority

35. *Id.*
36. *Id.* at 806 (emphasis added).
37. *Id.* at 806-08.
38. *Id.*
39. *See supra* note 5.
40. Morbark Indus., Inc. v. Western Employers Ins. Co., 170 Mich. App. 603, 429 N.W.2d 213 (1988).
41. *Id.* at ___, 429 N.W.2d at 215.
42. *Id.*
43. *Id.*
44. *Id.* at ___, 429 N.W.2d at 216.
45. *Id.*

viewpoint and refused to require the excess carrier to drop-down.[46] The court justified its position by stating that it "accords with the recognized intent of the parties, the purpose of the umbrella coverage being to provide, at a relatively low premium, extended coverage up to high limits, over and above primary insurance coverage."[47] Further, the purpose of excess insurance is not to compensate for the insolvency of primary insurers.[48] The court in *Morbark* noted the Fifth Circuit opinion in *Continental Marble & Granite Co. v. Canal Insurance Co.*,[49] in which the court held that requiring the excess insurer to drop-down would require the excess insurer to guaranty the solvency of the primary insurer.[50] Placing this burden on the excess carrier would increase the excess carrier's risk and thus increase the cost of excess coverage.[51] Further, such a burden would require excess carriers to make in-depth investigations of primary insurers before issuing secondary coverage.[52]

In addition to rejecting the argument that the contract was rendered ambiguous by the words "amount recoverable" and that it should therefore be construed against the insurer, the court in *Morbark* noted that it is also hornbook law that the court should read the policy as a whole when determining the intent of the parties.[53] The court stated, "if a contract, however inartfully worded or clumsily arranged, fairly admits of but one interpretation it may not be said to be ambiguous or, indeed, fatally unclear."[54]

The plaintiff argued that the Michigan court should follow *Pisciotta*, in which the California court found two possible meanings for "amount recoverable."[55] The Michigan court, however, declined to follow the California court's decision because the court in *Pisciotta* did not look at the contract in its entirety,[56] and also because the *Pisciotta* decision did not constitute binding precedent in Michigan and the Michigan court was not obligated to follow its reasoning.[57]

The "drop-down" theory was also rejected by a Georgia court in *United States Fire Insurance Co. v. Capital Ford Truck Sales*.[58] In *U.S. Fire* the

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46. *Id.*
47. *Id.*
48. *Id.*
49. Continental Marble & Granite Co. v. Canal Ins. Co., 785 F.2d 1258 (5th Cir. 1986).
50. *Id.* at 1259.
51. *Id.*
52. *Id.*
53. Morbark Indus., Inc. v. Western Employers Ins. Co., 170 Mich. App. at ___, 429 N.W.2d at 217.
54. *Id.* (citing Raska v. Farm Bureau Mut. Ins. Co., 412 Mich. 355, 362, 314 N.W.2d 440, 441 (1982)).
55. *Id.* at ___, 429 N.W.2d at 218.
56. *Id.* at ___, 429 N.W.2d at 219.
57. *Id.*
58. United States Fire Ins. Co. v. Capital Ford Truck Sales, Inc., 257 Ga. 77, 355 S.E.2d 428 (1987).

insolvent primary insurer, Aspen, had limits of $1 million, while U.S. Fire provided excess coverage up to $5 million.[59] The insured argued that "collectible" referred to the primary policy.[60] The policy referred to "the underlying policies [the Aspen policy] listed in Schedule 4 hereof, and the applicable limits of any other insurance collectible by the insured . . . ."[61] The court held that the policy clearly stated that "collectible" referred only to other insurance.[62] Its analysis also included a thorough review of the decisions of other jurisdictions which had held that the excess carrier was not required to drop-down.[63] Further, looking at the contract as a whole, the court found no ambiguity in it.[64]

In *Continental Marble & Granite Co. v. Canal Insurance Co.*,[65] a decision often cited in "drop-down" cases, the court considered the definition of "inapplicable." The policy language provided: "The company shall be liable only for ultimate net loss resulting from any one occurrence in excess of . . . if the insurance afforded by such underlying insurance is inapplicable to the occurrence, the amount stated in the declarations as the retained limit."[66] Continental Marble argued that the primary insurer's insolvency meant that the insurance was "inapplicable" and, therefore, that drop-down was required.[67] The court rejected this contention because Continental Marble was relying on a case, *Gros v. Houston Fire & Casualty Insurance Co.*,[68] in which there was a policy provision referring to "other valid and collectible insurance."[69] This provision was absent from Continental Marble's policy.

The court in *Continental* next considered whether there was a general public policy requiring the excess insurer to guaranty the solvency of the primary insurer.[70] The court refused to recognize such a public policy because it would place too great a burden on the excess carrier.[71] The court reasoned, "[e]xcess or secondary coverage [applies] only after a predetermined amount of primary coverage has been exhausted. A second insurer thus greatly reduces his risk of loss. This reduced risk is reflected in the cost of the policy."[72] The court in *Continental* saw no advantage in requiring a secondary insurer to scrutinize the solvency of a primary insurer, consider-

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59. *Id.* at ____, 355 S.E.2d at 429.
60. *Id.*
61. *Id.*
62. *Id.* at ____, 355 S.E.2d at 432.
63. *Id.* at ____, 355 S.E.2d at 430-32.
64. *Id.* at ____, 355 S.E.2d at 432.
65. Continental Marble & Granite Co. v. Canal Ins. Co., 785 F.2d 1258 (5th Cir. 1986).
66. *Id.* at 1259.
67. *Id.*
68. Gros v. Houston Fire & Casualty Ins. Co., 195 So. 2d 674 (La. Ct. App. 1967).
69. *Id.* at 676.
70. *Id.*
71. *Id.*
72. *Id.* (citing Whitehead v. Fleet Towing Co., 110 Ill. App. 3d 759, ____, 442 N.E.2d 1362, 1366 (1982)).

ing that insurance is already a highly regulated area.[73] The court found that "this additional burden on companies such as Canal would only further our legal system's lamentable trend of complicating commercial relationships and transactions."[74]

III. Guaranty Associations

Virtually every state has created a guaranty association or insolvency fund[75] to provide security when an insurer becomes insolvent.[76] If the unavailability of primary coverage constitutes a "covered claim," the guaranty association may provide coverage. In Iowa a "covered claim" is: "[a]n unpaid claim, including one for unearned premiums, which arises out of and is within the coverage and is subject to the applicable limits of an insurance policy to which this chapter applies issued by an insurer, if such insurer becomes an insolvent insurer after July 1, 1970 . . . ."[77] When a covered claim cannot be paid due to insolvency, the association will pay the claim, subject to a deductible of $100 and an upper limit of $300,000, and subject also to the upper limit provided by the policy itself.[78] Thus, if the primary policy limit is $100,000, the insured can recover up to $100,000.[79] If the primary insurer was to provide $500,000 worth of coverage, a maximum of $300,000 would be recoverable.[80]

The guaranty association statute also provides that no duplication of recovery can occur.[81] Therefore, if another insurance policy or guaranty association will cover the claim, the Iowa Guaranty Association will not.

The $300,000 maximum is not uncommon among state guaranty statutes.[82] Many states, however, have a policy limit of $100,000 or $150,000.[83]

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73. *Id.*
74. *Id.*
75. *See infra* notes 82-83 & 124.
76. Iowa Code § 515B.5 (1987).
77. *Id.* at § 515B.2(3) (1987).
78. *Id.* at § 515B.5(1)(a) (1987).
79. *Id.*
80. *Id.*
81. *Id.* at § 515B.9.
82. Jurisdictions having limits of $300,000 include:

Jurisdiction	*Statute*
Alaska	Alaska Stat. § 21.80.100 (1987)
Connecticut	Conn. Gen. Stat. § 38-278 (1988)
Delaware	Del. Code Ann. tit. 18, § 4208 (1986)
District of Columbia	D.C. Code Ann. § 35-1906 (1981)
Florida	Fla. Stat. § 631.57 (1988)
Hawaii	Haw. Rev. Stat. § 431D-8 (1987)
Idaho	Idaho Code § 41-3608 (1988)
Indiana	Ind. Code § 27-6-8-7 (1987)
Iowa	Iowa Code § 515.8 (1987)
Maine	Me. Rev. Stat. Ann. tit. 24-A, § 4438 (1987)

Such limits present a problem: who is to provide coverage above the statutory amount? If an insured who carries $500,000 primary coverage has a $250,000 judgment against him, and his primary insurer proves to be insolvent, and his state guaranty association has a limit of $150,000, then $100,000 of the judgment will not be covered by insurance. But the insured should be entitled to the coverage for which he bargained and paid.

Taking the same scenario a step further, suppose the insured has an excess policy providing coverage from $500,000 to $1.5 million. If a judgment of $750,000 is awarded against him, the guaranty association pays $150,000, the excess insurer pays $250,000, and the insured is responsible for $350,000.

There are three possible approaches to coverage when a primary insurer is insolvent. Under the first, the guaranty association pays in the statutory amount, the insured pays the portion of the primary coverage which is not covered by the guaranty association, and the excess carrier pays the amount which falls within its coverage. Under the second, the excess carrier is required to drop-down in the place of the insolvent insurer. The amounts which exceed the excess carrier's liability are covered by the guaranty association to its limits, and the rest falls on the insured. Under the third, the guaranty association pays its limits, the excess carrier drops-down to the guarantee association's limits, and the insured is responsible for anything beyond excess coverage.

The state of Washington adopted the first approach in *Washington In-*

Massachusetts MASS. GEN. L. ch. 175D, § 5 (1988)
Minnesota MINN. STAT. § 60C.09(2) (1986)
Mississippi MISS. CODE ANN. § 83-23-115 (1988)
Missouri MO. REV. STAT. § 375.785(4)(1) (1988)
Montana MONT. CODE ANN. § 33-10-105 (1987)
Nebraska NEB. REV. STAT. § 44-2401 (1987)
New Jersey N.J. STAT. ANN. § 17:30A-8 (West 1988)
North Dakota N.D. CENT. CODE § 26.1-42-05 (1987)
Ohio OHIO REV. CODE ANN. § 3955.01 (Anderson 1987)
Pennsylvania 40 PA. CONS. STAT. ANN. § 1701.201 (Purdon 1988)
Rhode Island R.I. GEN. LAWS § 27-34.9 (1987)
South Carolina S.C. CODE ANN. § 38-31-60(a) (1987)
Utah UTAH CODE ANN. § 31A-28-207 (1988)
Vermont VT. STAT. ANN. tit. 8, § 3615 (1988)
Virginia VA. CODE ANN. § 38.2-1606 (1988)
Washington WASH. REV. CODE § 48.32.060 (1988)
West Virginia W. VA. CODE § 33-25-8 (1988).

83. Jurisdictions providing coverage of either $100,000 or $150,000 include:
Jurisdiction Statute
Alabama ALA. CODE § 27-42-8 (1975)
Arizona ARIZ. REV. STAT. ANN. § 20-667 (1987)
Kentucky KY. REV. STAT. ANN. § 304.36-080 (Baldwin 1985)
Louisiana LA. REV. STAT. ANN. § 22:1382 (West 1970)
New Mexico N.M. STAT. ANN. § 59A-43-4 (1978)
Tennessee TENN. CODE ANN. § 56-12-107 (1987).

surance Guaranty Ass'n v. Guaranty National Insurance Co.[84] The Washington Insurance Guaranty Association (WIGA) brought suit to determine "who is responsible for the costs of defending an insured whose primary insurer has gone bankrupt."[85] (Pursuant to a court order the insolvent primary insurer had withdrawn from the defense of the case, and WIGA had stepped in to defend.[86])

The arguments presented by WIGA included: (1) Guaranty National Insurance Company (GNIC) should drop-down because the policy language "collectible by the insured" referred to the primary policy; the proceeds of the primary policy were not collectible so the excess should become primary; (2) GNIC, not WIGA, was required to defend the insured; (3) if GNIC had no clear duty to defend, the contract was ambiguous; and (4) the statutory prohibition against duplication of recovery meant that WIGA was excess to all other coverage, and the GNIC policy constituted other coverage.[87]

In addition to denying the arguments of WIGA, GNIC added: (1) the coverage provided by WIGA was an amount collectible because it qualified as "other underlying insurance" as provided in the contract; and (2) GNIC had provided a true umbrella policy which was intended only for excess coverage.[88]

In making its determination the court considered the purpose of WIGA.[89] It determined that the purpose of the fund was to protect innocent insureds from the insolvency of insurers.[90]

Then the court considered the GNIC policy.[91] It determined that the policy clearly and unambiguously stated that GNIC was liable only in excess of "applicable limits of underlying insurance as stated in item 5 of the Declarations, and any other underlying insurance collectible by the insured."[92] The court refused to find that the placement of the comma created two tiers of primary coverage.[93] Relying on the Ohio Court of Appeals decision in *Wurth v. Ideal Mutual Co.*,[94] the court held that "collectible" did not refer to money actually paid to the insured, but rather to "the existence of other applicable insurance coverage based on the particular occurrence in question."[95] Basing its decision on this interpretation of the contract, the court

84. Washington Ins. Guaranty Ass'n v. Guaranty Nat'l Ins. Co., 685 F. Supp. 1160 (W.D. Wash. 1988).

85. *Id.*

86. *Id.* at 1161.

87. *Id.*

88. *Id.* at 1161-63.

89. *Id.* at 1163.

90. *Id.*

91. *Id.*

92. *Id.* at 1163-64.

93. *Id.* at 1164.

94. Wurth v. Ideal Mut. Ins. Co., 34 Ohio App. 3d 325, 518 N.E.2d 607 (1987).

95. Washington Ins. Guaranty Ass'n v. Guaranty Nat'l Ins. Co., 685 F. Supp. 1160, 1165

assigned the first level of coverage to WIGA, and did not require GNIC to drop-down.[96] The court held that WIGA was to pay its limits of $300,000 and GNIC would become liable to the extent the judgment exceeded $500,000.[97] The court did not say how the insured was to bear the $200,000 which was left uninsured because of the insolvency. This demonstrates the problem created by the first approach: though the insured has obtained coverage, he may nevertheless be compelled to satisfy a judgment from his own assets.

An example of the second approach is found in *Massachusetts Insurers Insolvency Fund v. Continental Casualty Co.*[98] In this case the insolvency fund sought a determination that the excess insurer, Continental, should be required to drop-down in the place of the insolvent primary insurer.[99] A decision in favor of the insolvency fund was entered based upon the excess carrier's policy language.[100] The Continental policy provided that, "if the underlying limit of liability has been 'reduced,' the policy becomes excess of that reduced limit."[101] The court interpreted this to mean: "if the underlying coverage is reduced to nothing, the excess policy in effect provides first dollar coverage."[102] Further, the court determined that an ambiguity existed with respect to what would happen if the primary insurer was insolvent, but the court resolved the ambiguity against the excess insurer.[103]

Although the court noted that the excess insurer might assume that its coverage would not take the place of coverage provided by an insolvent insurer, a reasonable policyholder would expect the excess carrier to step into the shoes of an insolvent primary carrier.[104] Therefore, if the excess policy language provides for any drop-down, the excess carrier will become the primary insurer.[105]

The second approach creates two problems. First, unless the excess insurer's policy provides, explicitly or by ambiguity, for a drop-down in the event of a reduction or exhaustion of the primary limits, there is no reason to require drop-down. Second, if excess carriers are required to drop-down, the guaranty fund will not be required to step in unless there is no excess coverage, since the statute provides that the guaranty fund will only provide

(W.D. Wash. 1988).

96. *Id.*

97. *Id.*

98. Massachusetts Insurers Insolvency Fund v. Continental Casualty Co., 399 Mass. 598, 506 N.E.2d 118 (1987).

99. *Id.* at 599, 506 N.E.2d at 119.

100. *Id.*

101. *Id.* at 600, 506 N.E.2d at 120.

102. *Id.*

103. *Id.*

104. *Id.* at 600-01, 506 N.E.2d at 120.

105. *Id.* at 601, 506 N.E.2d at 121.

coverage if there is no other coverage.[106] For example, assume primary limits of $500,000, excess coverage from $500,000 to $1.5 million, and a judgment of $1.2 million. If the primary insurer is insolvent and the excess carrier is required to drop down, coverage will be provided for the first $1 million, leaving $200,000 uncovered. (The excess policy provides $1 million of coverage, so if the excess carrier is required to drop-down, it will provide coverage from $1 to $1 million.) Even though the guaranty fund covers losses up to $300,000, in this situation it would not provide coverage for the remaining $200,000, due to statutory limits on coverage.[107]

The third approach is exemplified by a Louisiana Court of Appeals decision, *McGuire v. Davis Truck Services, Inc.*[108] In *McGuire* the Louisiana Insurance Guaranty Association (LIGA) argued that its coverage should come second in the excess carrier's policy because Louisiana's statute reads: "Any person having a claim against an insurer under any provision in an insurance policy other than a policy of an insolvent insurer which is also a covered claim, shall be required to exhaust first his right under such a policy."[109] This argument was rejected because excess insurers were not included in the statute.[110] As LIGA had policy limits of $150,000 and the excess carrier provided coverage starting at $500,000, the court had to determine whether the excess carrier should be required to drop-down to LIGA's limits.[111] Angelina, the excess carrier, argued that its coverage was intended to compensate only for catastrophic losses and that its modest premiums supported this conclusion.[112] Angelina's policy stated that it would only be liable in excess of amounts recoverable.[113] The Louisiana court interpreted "amounts recoverable" to mean the same as "collectible," thereby determining that Angelina was required to drop-down.[114]

The court rejected Angelina's contention that the policy section covering "maintenance of underlying insurance" related to the insolvency of an underlying insurer.[115] The section related only to the insured's duty to maintain underlying insurance.[116] The court also rejected the argument that the phrase "in excess of underlying policy" referred to the primary policy regardless of its solvency.[117] The court found that the section was not deter-

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106. Iowa Code § 515B.2(3) (1987).

107. *Id.* at § 515B.5(1) (1987).

108. McGuire v. Davis Truck Servs., Inc., 518 So. 2d 1171 (La. Ct. App. 1988).

109. La. Rev. Stat. Ann. § 22-1386 (West 1970), *cited in* McGuire v. Davis Truck Servs., Inc., 518 So. 2d at 1173.

110. McGuire v. Davis Truck Servs., Inc., 518 So. 2d at 1173.

111. *Id.*

112. *Id.*

113. *Id.* at 1172.

114. *Id.* at 1174.

115. *Id.*

116. *Id.*

117. *Id.*

minative because the terms "amount recoverable" and "valid and collectible" created an ambiguity.[118] Finally, the court rejected Angelina's argument that requiring it to drop-down meant that it was a guarantor of the primary insurer's solvency.[119] The court responded that excess insurers could rewrite their policies.[120]

The Louisiana court came to a decision which requires not only that the guaranty association must perform its duties as provided by statute, but also that where the guaranty fund exhausts its limits, the excess carrier must provide coverage instead of the insured.[121] This approach also presents two problems. First, unless there is some ambiguity in the excess carrier's policy, no drop-down will be required. Second, if the excess carrier is required to drop-down, then the coverage provided by the excess carrier constitutes another insurance policy, which relieves the guaranty association of any liability.

IV. Conclusion

It is not easy to determine what should be done when insurers become insolvent. Excess insurers argue that their policies are intended to provide coverage only in the event of unusual, catastrophic losses. They threaten increased rates if they are required to drop-down in the place of an insolvent insurer. They also state that higher rates will result if they are required to investigate the financial soundness of the primary insurer. Such an investigation would become a necessary prerequisite to the issuance of any coverage, if the excess carrier were faced with the risk of being required to drop-down if the primary insurer became insolvent.

On the other hand, guaranty associations would prefer to see the excess carriers bear more of the burden. The associations claim that their only purpose is to fill in when there is no insurance available, and that available insurance should include insurance issued by an excess carrier. Since the excess carrier has received the benefit of premiums, it should be required to drop-down.

The objection to all of these arguments is that the guaranty associations and excess carriers have access to the money necessary to pay judgments, while the insureds do not. The insured, who has paid all of the premiums, may be left to pay a large judgment which should have been covered under his insurance policy. It can be argued that the insured should investigate the financial soundness of the insurer; but this hardly seems fair, since insureds (unlike excess carriers) rarely have either the knowledge or the means to perform such an investigation.

118. *Id.*
119. *Id.*
120. *Id.*
121. *Id.*

Contract law and interpretation would suggest that excess carriers cannot be required to bear the burden of primary insurers' liabilities when their policies specifically exclude such coverage. However, if there is an ambiguity in the contract, the excess carriers should be required to drop-down and provide coverage. If an excess carrier is required to drop-down, the guaranty association will be relieved of liability for coverage. The Iowa statute specifically provides that the guaranty association is liable only if there is no other coverage.[122]

The most troublesome problem arises where the excess carrier is not required to drop-down and the guaranty association covers only a portion of the claim. In many instances the insured is not in a position to bear the financial burden which will result. The excess carrier is in a much better position to step in and take responsibility. The question is whether the state should impose such responsibility on the excess carrier, as a matter of public policy. This approach seems very difficult to justify under ordinary principles of contract law. Therefore, if such a policy is to be adopted, it should be adopted by the legislature.

One approach is to rewrite guaranty association statutes to cover claims up to $500,000, since many primary policies provide coverage to this amount.[123] Some legislatures have already provided for guaranty association coverage to the full extent of the primary coverage.[124] A specific limit may be desirable, however, to protect the guaranty association.

A second approach is to adopt a public policy that all excess insurers will be required to drop-down to the limits of the guaranty association in the event of a primary carrier's insolvency. This approach creates a problem of inconsistency; states have different guaranty limits, so the excess carrier would be exposed to different levels of liability in different states. Also, the increased risk of liability would presumably cause excess carriers to raise their rates.

This writer advocates an amendment to the Iowa guaranty statute to provide for coverage up to $500,000. Such an amendment is of paramount importance, since the number of insolvent insurance companies is on the

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122. Iowa Code § 515B.9 (1987).

123. *See* L. Lasley, P. Winters & D. Puebla, Insurance Guaranty Funds: The New "Money Pit"? (1987) (available on Westlaw in the PLI database). This commentary suggests that, given the increasing number of insolvent insurance companies and the growing demand on guaranty associations, the associations will run into financial difficulty. The article suggests that federal intervention will be necessary.

124. These jurisdictions have already provided for full coverage of the primary insurer's obligations through the guaranty association:

Jurisdiction	*Statute*
California	Cal. Ins. Code § 1063.1(5) (West 1988)
Colorado	Colo. Rev. Stat. § 10-4-503(4) (1987)
Maryland	Md. Ann. Code art. 48A, § 508 (1985)
Oregon	Or. Rev. Stat. § 734.510-4(b)(A) (1987).

rise and is not likely to decrease in the near future.[125] The amendment is necessary to protect insureds, who take the initiative and purchase insurance coverage, from having to bear the burden of a company's mistakes.

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125. United States Fire Ins. Co. v. Capital Ford Truck Sales, Inc., 257 Ga. 77, 355 S.E.2d 428 (1987).