



October 19, 2009



Thinking About a Declaratory Relief Action? Think Twice, Says the California Court of Appeal

Authors: [Carlos E. Needham](#)

The California Court of Appeal, Second District, has clarified the standard for evaluating an insured's application for a stay of a coverage action due to possible prejudice in a pending, underlying action against the insured. *Great American Insurance Co. v. Superior Court (Angeles Chemical Co.)*, No. B203121 (Oct. 10, 2009) ("Great American").

The Court held that a stay is mandatory where there are overlapping factual issues in the two actions.

A stay is merely discretionary, however, where no such overlap exists. In the absence of overlapping factual issues, the insured's interest in not litigating two actions simultaneously must be weighed against the insurer's interest in not having to pay for underlying defense costs in an action that may not actually be covered. Factors that inform this balancing test include: (1) the anticipated duration of the underlying action; (2) whether the insured has separate counsel in the two actions; and (3) the availability of other insurance to cover the insured's defense costs in the underlying action.

In *Great American*, the insurer defended the insureds in an underlying environmental contamination litigation. After a partial settlement of the underlying action, the insurer filed a declaratory relief action seeking a

Newsletter Editors

Amy B. Briggs, Partner
abriggs@manatt.com
415.291.7451

Carlos E. Needham,
Partner
cneedham@manatt.com
310.312.4193

Jeremiah P. Sheehan,
Counsel
jsheehan@manatt.com
212.830.7205

Our Practice

Manatt's insurance practice group is multi-faceted. Our insurance regulatory lawyers represent insurers, producers and related parties in connection with examinations and investigations by state insurance departments,

determination that its duty to defend had ended because the underlying limits had been exhausted by the settlement. The insureds disputed whether the limits had, in fact, been exhausted, and successfully sought to stay the coverage action. They argued that the resolution of the issues presented in the coverage action overlapped with the issues in the underlying action. The trial court agreed.

The Court of Appeal, however, did not. The Court began its reasoning by noting that California courts have traditionally discussed three scenarios that might warrant a stay of the coverage action. These are: (1) the insured joins forces with the plaintiffs in the underlying action to defeat coverage on some issue common to both actions; (2) factual findings against the insured in the coverage action would be binding on the insured even though findings in the insured's favor would not be binding on the underlying plaintiff; and (3) the insured is forced to fight a two-front war.

The Court went on to explain that the first two scenarios are merely different facets of the overlapping factual issues problem. As for the third scenario, the Court pointed out that the insured is always embroiled in a two-front war when there is a declaratory relief action before the underlying action is resolved. So, under the Court's new, streamlined formulation, the three scenarios collapse into a single threshold query: Is there at least one overlapping factual issue? If so, then the trial court must grant a stay. If not, then it must weigh the parties' competing interests.

Here, the Court concluded that there was no overlapping factual issue. The exhaustion issues presented in the coverage action were pure legal issues of policy interpretation that had no bearing on the defense of the underlying action. Accordingly, the Court remanded so that the trial court could determine whether a discretionary stay was warranted.

Click [here](#) to read the Court's opinion.

For additional information on this issue, contact:



[Carlos E. Needham](#) Mr. Needham's practice focuses on insurance coverage, complex litigation matters involving product liability, science-related issues, mass tort claims, consumer class actions and environmental matters. He has a broad-based litigation and trial practice, primarily representing large companies in the defense of suits in the areas of

insurer mergers and acquisitions, ... [more](#)

[Practice Group Overview](#)

[Practice Group Members](#)

Info & Resources

[Subscribe](#)

[Unsubscribe](#)

[Newsletter Disclaimer](#)

[Manatt.com](#)

insurance coverage, product liability, and commercial contracts.

ATTORNEY ADVERTISING pursuant to New York DR 2-101(f)

Albany | Los Angeles | New York | Orange County | Palo Alto | Sacramento | San Francisco | Washington, D.C.

© 2009 Manatt, Phelps & Phillips, LLP. All rights reserved.