

Failure to Mention Exclusion in Denial Letter Does Not Result in Estoppel; Might Result in Waiver

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Applying California law, the United States District Court for the Eastern District of California has held that an insurer was not estopped from denying coverage under a particular exclusion based solely upon allegations that the insurer had failed to rely on the exclusion in a letter denying coverage. However, the court held that the insured sufficiently pled that the insurer waived its right to rely upon the exclusion because the insurer trained its claims handlers that the failure to mention a particular exclusion in a denial of coverage letter could result in waiver. The court also found that, absent waiver or estoppel, the underlying claims were excluded from coverage because they did not constitute Employment Practices Wrongful Acts as defined in the policy. *California Dairies, Inc. v. RSUI Indem. Co.*, 2009 WL 2475004 (E.D. Cal. Aug. 11, 2009).

In the underlying suit, the insured's current and former employees filed a class action lawsuit alleging that the insured violated various provisions of the California Labor Code concerning wages, hours and related matters. The insurer denied coverage based on Exclusion 4, which barred coverage for "violation of any of the responsibilities, obligations or duties imposed by . . . the Fair Labor Standards Act . . . or any similar provision of federal, state or local statutory law or common law" The denial letter did not mention Exclusion 7, which excluded coverage for any claim "[b]rought by or on behalf of any Insured, except: . . . (b) an Employment Practices Claim brought by an Insured Person." The policy defined "Insured Person" to include current or former employees.

The insured filed suit, and the insurer moved to dismiss on the grounds that coverage was precluded by Exclusion 4 and Exclusion 7. The insured argued that the insurer was estopped from relying upon Exclusion 7 by its failure to raise the exclusion in its denial letter. The court rejected the insured's equitable estoppel argument, reasoning that, even if the insurer violated California insurance regulations by failing to articulate all bases for denial of coverage in its final denial letter, the insured had not alleged reasonable detrimental reliance.

The court held that the insured sufficiently alleged that the insurer impliedly waived its right to rely on Exclusion 7. The court stated that in order to demonstrate waiver under California law, the insured must prove

that the carrier intentionally relinquished a right or that the carrier's acts are so inconsistent with an intent to enforce the right as to induce a reasonable belief that such right has been relinquished. The court rejected an argument that the insurer's failure to comply with California insurance regulations constituted a *per se* waiver of its right to rely upon Exclusion 7.

However, the insured had also alleged that the insurer trained its representatives that "failure to include all potentially applicable coverage provisions in a denial could constitute a waiver of [the insurer's] right to subsequently assert any omitted bases for denying coverage" The court held that if the insurer trained its representatives in that regard, then its failure to include Exclusion 7 in the final denial letter arguably constituted conduct sufficiently inconsistent with an intent to enforce Exclusion 7 so as to result in waiver.

The court then held that, absent waiver or estoppel, Exclusion 7 barred coverage for all claims in the underlying action. The insured argued that the carveback from Exclusion 7 for Employment Practices Claims brought by an Insured Person created a "blanket exception" to Exclusion 7 for claims brought by employees. The court opined that the insured misread the policy language, which plainly excluded coverage for claims brought by or on behalf of any Insured unless the claim is an Employment Practices Claim, which the policy further defined as a claim alleging an Employment Practices Wrongful Act. The court held that Exclusion 7 therefore barred coverage for all claims in the underlying action because none of the claims alleged an Employment Practices Wrongful Act as defined in the policy.