UNITED STATES DISTRICT COURT

SOUTHERN DISTRICT OF CALIFORNIA

ZOE BERNSTEIN, a minor, by her Guardian ad Litem Kelsie Valdez, Plaintiff, v. NAUTILUS INSURANCE COMPANY, Defendant.	Case No.: 16-cv-02883-L-RBB **ORDER GRANTING DEFENDANT'S MOTION TO DISMISS**

In this insurance breach of contract and bad faith action, Defendant Nautilus Insurance Company ("NIC") filed a motion to dismiss for failure to state a claim. Plaintiff Zoe Bernstein opposed and NIC replied. The Court decides this matter on the briefs without oral argument. *See* Civ. L. R. 7.1.d.1. For the reasons stated below, Defendant's motion is granted.

I. BACKGROUND

Plaintiff was injured in a single car accident. She filed a personal injury complaint in San Diego County Superior Court against the driver and owner of the vehicle, David Bernstein (the "Underlying Action"). (*See* doc. no. 1-2 ("Compl.") at 3.) Mr. Bernstein was employed by Pierview Investments II, Corp. ("Pierview"). The operative complaint

in the Underlying Action alleged that the accident was caused by his negligence in the course and scope of his employment with Pierview.

At the relevant time, Pierview was covered by a commercial general liability policy issued by NIC (the "Policy").[1] Pierview tendered the defense of the Underlying Action to NIC, which NIC refused. The Underlying Action settled with Plaintiff taking judgment against Pierview for $6,240,893.37, and Pierview assigning its rights and interests in the Policy to Plaintiff.

Subsequently, Plaintiff filed this action against NIC pursuant to California Insurance Code § 11580(b)(2) for breach of contract and breach of the implied covenant of good faith and fair dealing. Plaintiff alleged that NIC breached its duty to defend and indemnify Pierview in the Underlying Action. NIC removed the action to this Court based on diversity jurisdiction under 28 U.S.C. § 1332, and filed a motion to dismiss for failure to state a claim under Federal Rule of Civil Procedure 12(b)(6).

II. DISCUSSION

A Rule 12(b)(6) motion tests the sufficiency of the complaint. *Navarro v. Block*, 250 F.3d 729, 732 (9th Cir. 2001). In reviewing a Rule 12(b)(6) motion, the Court must assume the truth of all factual allegations and construe them most favorably to the nonmoving party. *Huynh v. Chase Manhattan Bank*, 465 F.3d 992, 997, 999 n.3 (9th Cir. 2006). "To survive a motion to dismiss, a complaint must contain sufficient factual matter, accepted as true, to 'state a claim to relief that is plausible on its face.'" *Ashcroft v. Iqbal*, 556 U.S. 662, 678 (2009) (quoting *Bell Atl. Corp. v. Twombly*, 550 U.S. 544, 570 (2007)). Dismissal is warranted where the complaint lacks a cognizable legal theory. *Shroyer v. New Cingular Wireless Serv., Inc.*, 622 F.3d 1035, 1041 (9th Cir. 2010) (internal quotation marks and citation omitted). Alternatively, a complaint may be dismissed where it presents a cognizable legal theory, yet fails to plead essential facts

[1] The Policy is attached as Exhibit 1 to the Complaint. (*See* doc. no. 1-2 at 14-127.) The page number references are to the page numbers assigned by the ECF system, rather than the Policy's own page numbers.

under that theory. *Robertson v. Dean Witter Reynolds, Inc.*, 749 F.2d 530, 534 (9th Cir. 1984).

A. Breach of Insurance Contract

Plaintiff claims that NIC breached its insurance contract by failing to defend and indemnify Pierview. NIC counters the case should be dismissed because it had no duty to do either. To prevail on a claim for breach of duty to defend,

> the insured must prove the existence of a *potential for coverage*, while the insurer must establish *the absence of any such potential*. In other words, the insured need only show that the underlying claim may fall within policy coverage; the insurer must prove it cannot. The duty to defend exists if the insurer becomes aware of, or if the third party lawsuit pleads, facts giving rise to the potential for coverage under the insuring agreement.

Delgado v. Interins. Exch. of Auto. Club of S. Cal., 47 Cal.4th 302, 308 (2009) (emphasis in original, internal quotation marks and citations omitted). "The nature and kinds of risks covered by the insurance policy establish the scope of duty to defend." *Essex Ins. Co. v. City of Bakersfield*, 154 Cal. App. 4th 696, 704 (2007) (citing *Waller v. Truck Ins. Exchange, Inc.*, 11 Cal.4th 1, 19 (1995). "'If, as a matter of law, neither the complaint nor the known extrinsic evidence indicate any basis for potential coverage, the duty to defend does not arise in the first instance.'" *Essex*, 154 Cal. App. 4th at 704 (quoting *Scottsdale Ins. Co. v. MV Transportation*, 36 Cal.4th 643, 655 (2005). Duty to defend, "which applies even to claims that are groundless, false, or fraudulent, is separate from and broader than the insurer's duty to indemnify." *Waller*, 11 Cal.4th at 19 (internal quotation marks and citation omitted).

NIC contends that the Policy's auto exclusion precludes coverage, and the Underlying Action therefore did not trigger a duty to defend. "An insurer is ... obligated to provide a defense even when an exclusion applies but may be reasonably interpreted to be inapplicable to the alleged facts." *Essex*, 154 Cal. App. 4th at 704 (citation omitted). Accordingly, an insurer cannot escape its duty by means of an exclusionary clause that is unclear. *Id.* at 705 (citation omitted). Plaintiff maintains that the Policy's auto exclusion

is at best ambiguous and does not clearly exclude coverage for bodily injuries arising from Plaintiff's auto accident.

The parties' arguments are focused on policy interpretation. "Interpretation of an insurance policy is a question of law. While insurance contracts have special features, they are still contracts to which the ordinary rules of contractual interpretation apply." *Palmer v. Truck Ins. Exch.*, 21 Cal.4th 1109, 1115 (1999) (internal brackets, quotation marks and citations omitted). [2]

The starting point of policy interpretation is its express language. If the language is unambiguous, the court need not look further.

> Under statutory rules of contract interpretation, the mutual intention of the parties at the time the contract is formed governs interpretation. Such intent is to be inferred, if possible, solely from the written provisions of the contract.

AIU Ins. Co. v. Super. Ct. (MFC Corp.), 51 Cal.3d 807, 822-23 (1990) (internal citations omitted).

> [I]n interpreting an insurance policy, we seek to discern the mutual intention of the parties and, where possible, to infer this intent from the terms of the policy. When interpreting a policy provision, we must give its terms their ordinary and popular sense, unless used by the parties in a technical sense or a special meaning is given to them by usage. We must also interpret these terms in context, and give effect to every part of the policy with each clause helping to interpret the other.

Essex, 154 Cal. App. 4th at 704-05 (internal quotation marks omitted, citing *Haynes v. Farmers Ins. Exch.*, 32 Cal.4th 1198, 1204 (2004) and *Palmer*, 21 Cal.4th at 1115).

While Defendant argues the Policy unambiguously precludes coverage for auto accidents, Plaintiff contends the auto exclusion is ambiguous, and should be construed in favor of greater coverage. Exceptions to coverage are interpreted against the insurer:

> Any exception to the performance of the basic underlying obligation must be so stated as clearly to apprise the insured of its effect. Coverage may be

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[2] California substantive law applies in this diversity action. *See Erie R.R. Co. v. Tompkins*, 304 U.S. 64 (1938).

> limited by a valid endorsement and, if a conflict exists between the main body of the policy and an endorsement, the endorsement prevails. But to be enforceable, any provision that takes away or limits coverage reasonably expected by an insured must be conspicuous, plain and clear. Thus, any such limitation must be placed and printed so that it will attract the reader's attention. Such a provision also must be stated precisely and understandably, in words that are part of the working vocabulary of the average layperson. The burden of making coverage exceptions and limitations conspicuous, plain and clear rests with the insurer.

Essex, 154 Cal. App. 4th at 705 (quoting *Haynes*, 32 Cal.4th at 1204, internal quotation marks and brackets omitted).

NIC's Commercial General Liability Coverage Form of the Policy begins with the admonition: "Various provisions in this policy restrict coverage. Read the entire policy carefully to determine rights, duties and what is and is not covered." (Policy at 75.) The Policy further states:

> We will pay those sums that the insured becomes legally obligated to pay as damages because of "bodily injury" … to which the insurance applies. We will have the right and duty to defend the insured against any "suit" seeking those damages. However, we will have no duty to defend the insured against any "suit" seeking damages for "bodily injury" … to which this insurance does not apply.

(*Id.*) Accordingly, to determine whether the auto accident is covered, exclusions and limitations must be considered. The exclusions state in pertinent part:

> **SECTION 1 – COVERAGES**
>
> [¶]
>
> **2. Exclusions**
>
> This insurance does not apply to:
>
> [¶]
>
> **g. Aircraft, Auto or Watercraft**
>
> "Bodily injury" … arising out of the … use … of any … "auto" … owned or operated by or rented or loaned to any insured.

(*Id.* at 75, 76, 78. (emphasis in original) ("Exclusion g".) This exclusion is supplemented by the endorsement, which states in pertinent part:

> Exclusion g. **Aircraft, Auto or Watercraft** under paragraph 2., **Exclusions of Section I – Coverage A – Bodily Injury and Property Damage Liability** is replaced by the following:
>
> **2. Exclusions**
>
> This insurance does not apply to:
>
> **g. Aircraft, Auto or Watercraft**
>
> "Bodily injury … arising out of the … use … of any … "auto"… ."

(*Id.* at 109 ("Endorsement").)

Plaintiff contends that Exclusion g, when read with the Endorsement, is vague and ambiguous. The Court disagrees. The Endorsement eliminates the language that requires the auto to be "owned or operated by or rented or loaned to any insured" for the exclusion to take effect, and clearly states that the Policy does not cover bodily injury arising from the use of "any 'auto'." Plaintiff claims injury from a negligently caused car accident, hence, the use of an "auto." The remainder of Exclusion g, as modified by the Endorsement, does not change the fact that bodily injury arising from automobile use is excluded from coverage. It continues in pertinent part:

> This exclusion applies even if the claims allege negligence or other wrongdoing in the supervision, hiring, employment, training, or monitoring of others, if the "occurrence" which caused the "bodily injury" or "property damage" involved the ownership, maintenance, use, or entrustment to others of any aircraft, "auto" or watercraft.

(Id.) It concludes with two provisions which limit Exclusion g, *i.e.*, broaden coverage, in ways that are not relevant to Plaintiff's case -- with respect to (1) watercraft; and (2) bodily injury and property damage arising out of the operation of certain "mobile

equipment" attached to a land vehicle. (*Id.*) Accordingly, bodily injury from an auto accident is clearly excluded from coverage. NIC therefore was not obligated to defend or indemnify.

Plaintiff's reliance on *Essex Insurance Company v. City of Bakersfield* is unpersuasive. In *Essex*, the insurance company brought an action seeking declaratory judgment that it was not obligated to defend or indemnify the city in a lawsuit stemming from an auto accident. The city was being sued by one of the drivers for creating a dangerous condition. Although the policy in *Essex* contained nearly identical auto exclusion language, the complaint survived the city's motion to dismiss because the personal injury claim was not based on the use of the automobile but the city's negligence in organizing a public event, which allegedly created a dangerous condition. *Essex*, 154 Cal. App. 4th at 708. The court acknowledged that the city was not liable for the negligent operation of the cars involved in the accident. *Id.* at 709. It concluded, however, that the dangerous condition was distinct from the ultimate auto accident, thus forming a separate basis for coverage to which the auto exclusion did not apply. *Id.* at 708. The court reasoned that the policy was issued for the public event and the city reasonably expected to be covered against a lawsuit arising out of a claim that its negligence in organizing the event created a dangerous condition. *Id.* at 707. The court found that the auto exclusion was not clear enough to defeat the city's reasonable expectation of coverage for claims arising out of a dangerous condition. *Id.* at 711.

The Underlying Action is based solely on the negligent use of an automobile. Unlike *Essex*, there is no alternative basis upon which the Policy could provide coverage. *Essex* is therefore inapposite.

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B. Direct Action to Recover Policy Benefits

Plaintiff also alleges that California Insurance Code § 11580(b)(2) entitles her to recover the amount NIC owes to Pierview. Section 11580(b)(2) provides in pertinent part:

> A policy insuring against losses … shall not be … issued … unless it contains … a provision that whenever judgment is secured against the insured … in an action based upon bodily injury …, then an action may be brought against the insurer on the policy and subject to its terms and limitations, by such judgment creditor to recover on the judgment.

The statute does not expand a carrier's liability, but provides a legal basis for a judgment creditor to bring a claim against the judgment debtor's insurer. As an assignee and judgment creditor of Pierview, Plaintiff has the right to recover no more than the amount NIC owes Pierview. Since the Policy excluded auto accident coverage, NIC had no duty to defend or indemnify Pierview. In her capacity as Pierview's assignee, Plaintiff therefore cannot state a claim against NIC.

C. Breach of the Implied Covenant of Good Faith and Fair Dealing

Finally, Plaintiff alleges breach of the implied covenant of good faith and fair dealing. "A 'bad faith' claim cannot be maintained unless policy benefits are due … ." *McMillin Scripps N. P'ship v. Royal Ins. Co.*, 19 Cal. App. 4th 1215, 1222 (1993); *see also Brehm v. 21st Century Ins. Co.*, 166 Cal. App. 4th 1225, 1235 (2008) ("As a general rule . . . there can be no breach of the implied covenant of good faith and fair dealing if no benefits are due under the policy."). Since NIC had no duty to defend or indemnify Pierview, Plaintiff cannot state a claim for breach of the implied covenant of good faith and fair dealing.

III. CONCLUSION AND ORDER

For the foregoing reasons, Defendant's motion is granted. The Court next considers whether Plaintiff should be granted leave to amend. Rule 15 advises leave to amend shall be freely given when justice so requires. Fed. R. Civ. P. 15(a)(2). "This

policy is to be applied with extreme liberality." *Eminence Capital, LLC v. Aspeon, Inc.*, 316 F.3d 1048, 1051 (9th Cir. 2003) (internal quotation marks and citation omitted).

> In the absence of any apparent or declared reason – such as undue delay, bad faith or dilatory motive on the part of the movant, repeated failure to cure deficiencies by amendments previously allowed, undue prejudice to the opposing party by virtue of allowance of the amendment, futility of amendment, etc. – the leave sought should, as the rules require, be "freely given."

Foman v. Davis, 371 U.S. 178, 182 (1962). Dismissal without leave to amend is not appropriate unless it is clear the complaint cannot be saved by amendment. *Id*.

Plaintiff has not requested leave to amend. Because it does not appear that Plaintiff can allege facts to state a claim, the complaint is dismissed without leave to amend.

IT IS SO ORDERED.

Dated: July 24, 2017

Hon. M. James Lorenz
United States District Judge