"Other Insurance" Clauses in Property and Liability Insurance Policies: Frequently Misunderstood Provisions

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Most property and liability insurance policies contain "other insurance" clauses that insurers insert to restrict or limit their liability if another insurance policy affords coverage for the "same loss."[1] These clauses intend to preclude insureds from over or double insuring their properties, to conform to the principle of indemnity, and to reduce moral hazards by preventing profiting from losses.

Unfortunately, insurers sometimes misunderstand their own "other insurance" clauses, and occasionally assert their applicability to a given factual situation when inappropriate, mainly because the competing policies don't insure the "same loss." This flawed interpretation has resulted in substantial penalty-interest awards against insurers for unreasonable delay or denial of claim payments.

Analyzing a potential "other insurance" issue is often a three-step process:

1. Do the competing policies insure the "same loss";
2. What type of "other insurance" clause do the competing policies contain; and
3. What contract-construction principals do courts utilize to resolve conflicting clauses.

Definition of "Same Loss"

The first step in analyzing whether there is a potential "other insurance" issue is determining if the competing policies insure the "same loss." Michigan courts have interpreted the "same loss" requirement consistently;[2] they will enforce an "other insurance" clause when and if the competing policies satisfy a four-trigger requirement:

1. They insure the same property;[3]
2. They insure the same insurable interest;[4]
3. They insure against the same risks or perils;[5] and
4. The insurance proceeds are payable to the same parties.[6]

If any one of these four requirements is missing, then the competing policies don't insure the "same loss," and there is no "other insurance" problem. Consequently, the primary insurance policy must fully pay the insured's loss.

Interestingly, this "same loss" requirement is litigated more often in "other insurance" clauses involving property-insurance disputes. In the last 100 years,[7] Michigan courts have rarely applied "other insurance" clauses in property-insurance disputes because the policies didn't insure the "same loss." Typically, the Michigan cases have involved situations where the competing policies insured separate and distinct insurable interests but one of the insurers asserted proration was required. For example, the following disputes didn't satisfy the "same loss" requirement:

1. Policies separately insuring a land-contract vendor and a land-contract vendee;[8]
2. A policy issued jointly to two brothers versus a separate policy insuring an individual brother;[9]
3. An owner's builders-risk policy versus a general contractor's builders-risk policy;[10]
4. Policies separately insuring a landlord and a tenant;
5. Policies separately insuring a condominium association versus a unit owner.[11]

Types of "Other Insurance" Clauses

If the competing policies insure the "same loss," then the second step in analyzing an "other insurance" problem is to determine what type of clause the competing policies contain. Generally, insurers may either insert their own "other insurance" clauses, usually those the Insurance Services Office approves and adopts on the forms that it writes, or they may draft their own manuscript clauses to address certain risks or unacceptable insurance classifications. The types of "other insurance" clauses inserted could vary depending on whether the insurance policy is a liability or a property policy.

Liability Insurance Policies

In liability policies, like commercial general liability, professional liability, pollution liability, or automobile liability policies, there are often four types of "other insurance" clauses that may limit an insurer's liability if two or more policies insure the "same loss."

1. A pro-rata clause: an insurer usually pays its loss's share in the proportion its policy limits relates to the aggregate coverage available under all applicable insurance policies;[12]

2. An excess clause: an insurer pays a loss only after other primary insurance is exhausted;
3. An escape clause: an insurer doesn't pay for any loss if other insurance coverage is available.[13]
4. An excess-escape clause: an insurer pays for the loss's amount exceeding the limits of other insurance available, but it doesn't pay where the amount of other insurance coverage available equals or exceeds its own.

Property Insurance Policies

In property insurance policies, especially those insuring fire as a basic peril, like most homeowners or dwelling policies, Michigan law requires admitted[14] insurers to only insert pro-rata "other insurance" clauses. [15]

Although some admitted insurers ignore Michigan law, and instead, insert only excess or escape clauses in their fire insurance policies, Michigan courts will void any policy provisions that contradict Michigan law, and would add any missing statutory provisions, like a pro-rata clause, into any non-conforming fire insurance policy.[16]

When the dispute involves non-admitted insurers,[17] and the policies include excess clauses, for example, instead of pro-rata clauses, courts still apply a pro-rata formula, relying on contract-interpretation principals, because a literal application of the excess clauses would leave the insured without any available insurance.[18]

Construction of "Other Insurance" Clauses

Where the competing policies aren't true "other insurance" (not concurrent) because they don't insure the "same loss" (same property, same insurable interest, same risks or perils, and insurance proceeds are payable to the same parties), there is no "other insurance" issue, and the primary insurer must fully pay the insured's loss.[19]

But when "other insurance" clauses conflict because the policies do insure the "same loss" but have differing provisions, courts nationally follow one of two methods to resolve the conflict:

1. The majority view, including Michigan, reconciles the conflicting clauses by discerning the parties' intent, usually requiring the insurer with the pro-rata clause to cover all losses up to its policy limits;[20]
2. The minority view finds the conflicting clauses to be "mutually repugnant," rejecting them completely, and then prorating the loss among all insurers.[21]

Thus, where two policies have pro-rata clauses insuring the "same loss," insurers must contribute equally to the insured's loss.[22] For example, a building is insured for $1,000,000, with insurer A providing $700,000 in coverage, and insurer B providing $300,000 in coverage. If the building suffers a loss of $200,000, and the two policies include pro-rata clauses, then insurer A pays $140,000 (70 percent of $200,000) and insurer B pays $60,000 (30 percent of $200,000).

Where two policies insure the "same loss," and one policy has an excess clause and the other policy has a pro-rata clause, the policy with the pro-rata clause is primary and the other policy is excess.[23] If one policy has an escape clause and the other has a pro-rata clause, then the escape clause will not apply and the policy with the pro-rata clause pays the entire claim. Finally, if one policy has an escape clause and the other has an excess clause, then an analysis of the parties' intent will resolve the conflict.[24]

The Primary Insurer's Payment Obligation

"Other insurance" clauses only affect insurers' rights among themselves, and should not adversely affect the insured's right to recovery under each clause or concurrent policy. Therefore, insurers may never allocate a loss to the insured, and paying the insured's claim must take priority over any loss-allocation disputes among concurrent insurers.[25] The primary insurer must fully indemnify the insured for the loss, then seek contribution from the other insurer or insurers.[26] Alternatively, the primary insurer may also institute a declaratory judgment action.[27]

Conclusion

"Other insurance**"** clauses apply when the two or more policies insure the "same loss." The "same loss" is satisfied when the two or more policies insure 1) the same property; 2) the same insurable interest; 3) the same risks or perils; and 4) the insurance proceeds are payable to the same parties. If the policies insure the "same loss," then analyzing the type of the "other insurance" clause inserted would permit the court to properly declare the insured's rights under the competing policies. But when a literal application is impossible because it would leave the insured without any available insurance, Michigan courts reconcile the conflict by pro-rating the loss between the insurers. Finally, when there is an "other insurance" dispute, a primary insurer can't simply ignore the claim; it has only two options: 1) fully pay the insured's claim, and then seek contribution from the other insurer or insurers, or 2) file a declaratory-judgement action. ■

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Endnotes

1 *Lubetsky v Standard Fire Ins Co*, 217 Mich 654; 187 NW2d 260 (1992); *Root v Hamilton Mut Ins Co*, 116 Mich App 596; 323 NW2d 298 (1981); *McCoy v Continental Ins Co*, 326 Mich 261; 40 NW2d 146 (1949).

2 *Id*.

3 *Lubetsky*, 217 Mich at 656.

4 *American & Foreign Ins Co v Allied Plumbing & Heating Co*, 36 Mich App 561; 194 NW2d 158 (1971); *Dietzel v Patrons' Mut Fire Ins Co of Michigan*, 232 Mich 415; 205 NW 149 (1925).

5 *Lubetsky*, 217 Mich at 655-56.

6 *Id.*; *Root v Hamilton Mut Ins Co*, 116 Mich App 596; 323 NW2d 298 (1981).

7 Only some of the published cases are included in this article.

8 *McCoy v Continental Ins Co*, 326 Mich 261; 40 NW2d 146 (1949); S*mith v American Ins Co*; 177 Mich 123; 143 NW 54 (1913); *State Farm Fire & Cas Co v Farmers Ins Exchange*, 80 Mich App 567; 264 NW2d 62 (1978); *Tyler v Pacific Indem Co*, 2012 WL 300883 (ED Mich, Feb 1, 2012).

9 *Dietzel v Patrons' Mut Fire Ins Co of Michigan*, 232 Mich 415; 205 NW 149 (1925).

10 *American & Foreign Ins Co v Allied Plumbing & Heating Co*, 36 Mich App 561; 194 NW2d 158 (1971).

11 Concurrent coverage maybe created by extrinsic documents, not part of the insurance policies themselves, like condominium association by-laws, or the master deed.

12 Some older policies include pro-rata clauses that allocate the loss between insurers by equal shares, and not policy limits.

13 *St Paul Fire & Marine Ins Co v American Home Assur Co*, 444 Mich 560; 514 NW2d 113 (1994).

14 Admitted insurers are those that are licensed and authorized to do business in Michigan.

15 MCL 500.2833(k).

16 *Randolph v State Farm Fire & Cas Co*, 229 Mich App 102; 580 NW2d 903 (1998).

17 Non-admitted insurers are not licensed in Michigan and do not contribute to the state's guaranty fund, which protects policyholders in case a non-admitted insurer declares bankruptcy.

18 *Travelers Property Casualty Company of America v XL Insurance America, Inc*, unpublished opinion of the Court of Appeals, issued [Mar 16, 2017] (Docket No. 329277 and 329293).

19 *American & Foreign Ins Co v Allied Plumbing & Heating Co*, 36 Mich App 561; 194 NW2d 158 (1971).

20 *St Paul Fire & Marine Ins Co*, 444 Mich at 560.

21 *Lamb-Watson Inc v Oregon Auto Ins Co,* 219 Or 110; 314 P2d 110 (1959).

22 *Interstate Fire & Cas Co v Hartford Fire Ins Co*, 548 F Supp 1185 (ED Mich, 1982).

23 *St Paul Fire & Marine Ins Co v American Home Assur Co*, 444 Mich 560; 514 NW2d 113 (1994).

24 *Pacific Ins Co v Cordova Chemical Co of Michigan*, unpublished opinion per curiam of the Court of Appeals, issued [June, 14, 2005] (Docket No. 248778). *State Farm Fire & Cas Co v Liberty Ins Underwriters, Inc*, 613 F Supp 2d 945 (W D Mich, 2009), aff'd, 398 F Appx 128 (CA 6, 2010).

25 *Auto-Owners Ins Co v Southern Michigan Mut Ins Co*, 123 Mich App 39; 333 NW2d 168 (1983).

26 *Reliance Ins Co v Liberty Mutual Fire Ins Co*, 13 F3d 982 (CA 6, 1994).

27 *Auto-Owners Ins Co v S Michigan Mut Ins Co*, 123 Mich App 39; 333 NW2d 168 (1983); *State Farm Fire & Cas Co v Farmers Ins Exchange*, 80 Mich App 567; 264 NW2d 62 (1978).