

# The “Innocent” Spouse

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Barry Zalma

When property is owned by more than one person, usually a husband and wife or a partnership, the intentional act of one was usually considered sufficient to declare the entire policy void. In the last ten years the courts have followed a trend to require insurers to ignore what they thought was clear and unambiguous statutory language in fire insurance policies and pay the innocent spouse or partner for the loss caused by the intentional act of the other spouse or partner. The trend needs to be changed. A recent decision of the California Supreme Court gives hope to insurers who believe that the clear and unambiguous words in a policy must be applied.

So-called innocent spouses are being paid, as a matter of public policy, in face of policy language like the following:

## **Concealment, Fraud**

This entire policy *shall be void* if, whether before or after a loss, the insured has willfully concealed or misrepresented any material fact or circumstance concerning this insurance or the subject thereof, or the interest of the insured therein, or in case of any fraud or false swearing by the insured relating thereto. [California Standard Fire Insurance Policy, California Insurance Code Section 2071]

California was one of the last to join the trend in *Watts v. Farmers Insurance Exchange*, 98 Cal.App.4th 1246, 120 Cal.Rptr.2d 694 (Cal.App. Dist.2 06/05/2002) where the court decided that Mr. Watts, a reportedly innocent spouse, was not precluded from obtaining any recovery because of his wife’s misdeeds. Farmers initially convinced the trial court to refuse indemnity to Mr. Watts because of the ruling in *Erlin-Lawler Enterprises, Inc. v. Fire Ins. Exchange* (1968) 267 Cal.App.2d 381. *Erlin-Lawler* did not involve jointly held marital property. In *Erlin-Lawler*, property belonging to a closely held corporation was destroyed in a fire and an officer and shareholder, along with an ex-officer and ex-shareholder, were convicted of arson. The corporation sued the insurer. The trial court entered judgment in favor of the insurer based on the corporation being the alter ego of the two arsonists. On appeal, the corporation pointed out that the shareholder arsonist owned only 50 percent of the shares. His ex-wife and the other arsonist’s ex-wife as their separate property owned the other 50 percent. The two women were officers and at least one of them took an active, full-time role in the operation of the corporation’s business. Neither had any role in the arson.

The *Watts* Court, comparing *Erlin-Lawler* to its facts, reported:

Finding no dispositive California law on the issue of whether a corporation could recover from its insurer under these circumstances, the appellate court conducted a lengthy review of the law in other jurisdictions and concluded there could be no bright line rule: ‘From the cases decided in the other jurisdictions, the following basic rule may be deduced: *The arsonist’s status as an officer, stockholder, employee or agent of an insured corporation does not necessarily preclude the corporation from recovering upon the policy of insurance. The basic function of the court is to see that no one takes advantage of his own wrong. . . . An analysis must be made in each case to see if the arsonist will benefit by the recovery on the policy, either directly or indirectly.*’ (Erlin-Lawler Enterprises, Inc. v. Fire Ins. Exch., supra, 267 Cal.App.2d at p. 385.) The court reversed the defense judgment and remanded the matter for findings on various factual matters such as whether the arsonist shareholder was in dominant control of the corporation, whether the cash used to set up the corporation came from separate property of the wives, whether the couples separated before or after the fire, etc. (Id. at pp. 387-388.) [Italics added]

The construction of insurance contracts has always been governed by the same rules of construction applicable to all contracts. See *Rosen v. State Farm General Insurance Company* (California Supreme Court, June 12, 2003), *Balandran v. Safeco Ins. Co. of Am.*, 972 S.W. 2d 738, 740-41 (Tex. 1998); *National Union Fire Ins. Co. v. CBI Indus.*, 907 S.W. 2d 517, 520 (Tex. 1995). In construing an insurance contract, its terms are given their “ordinary and generally accepted meaning.” *Security Mut. Cas. Co. v. Johnson*, 584 S.W. 2d 703, 704 (Tex. 1979). The primary goal of the court “is to give effect to the written expression of the parties’ intent.” *Balandran*, 972 S.W. 2d at 741 (emphasis added) [quoting *State Farm Life Ins. Co. v. Beaton*, 907 S.W. 2d 430, 433 (Tex. 1995) and *Forbau v. Aetna Life Ins. Co.*, 876 S.W. 2d 132, 133 (Tex. 1994)].

Although they claim to follow the general rules of construction *Watts* and *Rosen* seem to apply a different rule: all contracts are interpreted equally except insurance contracts, which are interpreted to favor the insured. An insurer may not rely on an ambiguous interpretation of a policy provision that, if construed as the insurer contends, would deprive the insured of coverage. *E. A. Robey and Company, Inc. v. City Title Insurance Co.*, 261 Cal. App. 2d 517, 68 Cal. Rptr. 38 (1968) nor may it rely on unambiguous, clear and explicit interpretation if a court determines a “public policy” reason exists to change the contract terms. When the language of an insurance contract is reasonably susceptible to two constructions, it should be construed in favor of the insured [*Hernandez v. First Financial*, 106 P. 2d 1278, 106 Nev. 900 (1900); *Linnastruth v. Mutual Benefit Health & Accident Association*, 22 Cal. 2d. 216, 137 P. 2d 833 (1943); *Wilkins v. American*

*Motorists*, 97 N.C. App. 266, 388 S.E.2d 191 (1990).] except when a “public policy” interferes.

These rules should be subject to the limitation that:

[a] court cannot and should not do violence to the plain terms of a contract by artificially creating ambiguity where none exists. In situations in which reasonable interpretation favors the insurer, and any other would be strained and tenuous, no compulsion exists to torture or twist the language of the contract. *An insurance company has the right to limit the coverage of a policy issued by it and when it has done so, the plain language of the limitation must be respected.* (Emphasis added). *Matsuo Yoshida v. Liberty Mutual Insurance Co.*, 240 F. 2d 824 (9th Cir 1957); *Continental Casualty Co. v. Phoenix Construction Co.*, 46 Cal. 2d. 423, 296 P. 2d. 801 (1956); *Adjuster’s Market Co. v. American Home Assurance Co.*, 4 Cal. 3d. 309, 93 Cal. Rptr. 449 (1971).

Basically, “the courts will not indulge in a forced construction of an insurance policy so as to fasten a liability on the insurance company which it has not assumed.” *St. Paul Fire & Marine Insurance Company v. Coss*, 80 Cal. App. 3d. 888, 145 Cal. Rptr. 836 (1978).

In its discussion of the relevant authority, the *Erlin-Lawler* court summarized its understanding of the rules governing recoverability by an innocent co-insured in other types of situations and relationships, important to *Watts* and any innocent spouse situation, as follows:

*Mere family relationship of the arsonist which does not bestow a property right or other direct financial benefit in the proceeds of insurance does not bar a recovery.* [Citations.] But if the property insured is community property, an innocent wife cannot recover if her husband willfully burned the property. (*California Ins. Co. v. Allen* (5th Cir. 1956) 235 F.2d 178, 179.) Even a divorce prior to the fire without a division of the community property does not alter this rule as to property presumptively community. (*Bridges v. Commercial Standard Ins. Co.* (Tex.Civ.App. 1952) 252 S.W.2d 511, 512.) Even an innocent joint tenant has been denied recovery where the fire is set by the other joint tenant. (*Klemens v. Badger Mut. Ins. Co.* (1959) 8 Wis.2d 565 [99 N.W.2d 865, 866].) (*Erlin-Lawler Enterprises, Inc. v. Fire Ins. Exch.*, *supra*, 267 Cal.App.2d at p. 386.) [Italics added]

The court in *Erlin-Lawler* cited no California authority for the propositions set forth concerning community property and was stated to be dicta and not controlling. *Erlin-Lawler* involved misfeasance by a corporate officer and shareholder and recovery for damage to corporate property. The statements concerning community property and joint tenancy merely represented a recitation of then recent authority in those areas from other jurisdictions. It also included an understanding of California Community Property Law. In California any money earned during the pendency of a marriage and any property acquired during the pendency of a marriage are owned by the marital community. Therefore, if the innocent spouse is paid for the loss caused by the crime of the criminal spouse, the criminal spouse automatically owns half of the payment and profits from his or her wrong.

The *Watts* Court, ignoring California Community Property Law, concluded that the trend noted in *Erlin-Lawler*:

has been reversed and currently favors permitting recovery by the innocent insured party up to his or her percentage share of the value of the property unless the policy contains language which clearly excludes this possibility. Of the three cases cited by the court in *Erlin-Lawler*, all have been overruled explicitly or implicitly by the highest courts in the relevant jurisdictions. *Klemens v. Badger Mutual Ins. Co.*, supra, 99 N.W.2d 865, was explicitly overruled by the Wisconsin Supreme Court in *Hedtcke v. Sentry Ins. Co.* (Wis. 1982) 326 N.W.2d 727. The issue in *Hedtcke* was whether an innocent wife could recover under a fire insurance policy if her husband, a named insured, intentionally caused the fire. Citing *Klemens* and other similar cases, the insurance company argued she could not recover because the property was jointly owned and jointly insured, although the couple was separated and in the process of divorce at the time of the fire. Comparing earlier Wisconsin decisions with more modern decisions from other jurisdictions such as Michigan, Illinois and New York, the court concluded that ‘*imputing the incendiary actions of an insured to the innocent insured and creating an absolute bar to recovery by the innocent insured, produces inequitable results.*’ (*Hedtcke, supra*, 326 N.W.2d at p. 740), whereas ‘*the modern rule adopted by courts in other jurisdictions permitting recovery by innocent insureds preserves the essence of the legal principles recognized in the [contrary Wisconsin] cases and produces an equitable result....*’ [Italics added]

In *State Farm v. Walker* (1990) 459 N.W. 2d 605, 157 Wis 2d 459 the Wisconsin Court of Appeal refused to follow *Hedtcke* and upheld denial of the claim of an innocent spouse

when the joint obligation stated in the false swearing, misrepresentation and concealment condition of the policy was breached by one insured. This appears to be the more “modern rule” in Wisconsin but was ignored by the *Watts* court. That this “modern rule” totally ignores the clear, explicit and unambiguous language of the policy is overcome by the need to be “fair” and reach an equitable result. Equity, according to the *Watts* court seems to require that the policy language be ignored.

The court in *Hedtcke* noted that *Klemens* and other similar cases were based on the “principle of fortuitousness,” that is, “that insurance covers fortuitous losses and that losses are not fortuitous if the damage is intentionally caused by the insured.” (*Hedtcke v. Sentry Ins. Co.*, *supra*, 326 N.W.2d at p. 738.) Courts adopting the modern rule, on the other hand, “focus on the contract of insurance rather than the interests and obligations arising from the nature of the property ownership. In *Klemens* this court concluded without analysis that if there are several insureds, the joint nature of the insurance contract gives rise to joint interests and obligations on the part of each policyholder.

The courts following what the *Watts* Court calls “the modern rule” discard this conclusory maxim and turn instead to the language of the policy to determine whether the rights of the insureds are joint or several.” (*Hedtcke*, at pp. 738-739, fn. omitted.) The Wisconsin Supreme Court cited an Indiana case, which noted that, the “legal fiction of the entirety’s estate in real estate is designed for the protection of the spouses and the marriage” and found it “a perversion of this legal fiction . . . to use it to destroy the property rights of an innocent spouse.” (Id. at p. 739, fn. 9, quoting *American Economy Ins. Co. v. Liggett* (Ind.App. 1981) 426 N.E.2d 136, 140.) It also relied on a New Hampshire case which justified its conclusion “by noting that one who owns an undivided interest in property may insure his or her interest under a separate insurance policy or under a joint policy with the other co-owners” and that “arson perpetrated by one owner would not influence the right of the innocent owner to recover under his or her own separate policy . . . .” (*Hedtcke*, at p. 739, citing *Hoyt v. New Hampshire Fire Ins. Co.* (1942) 92 N.H. 242 [29 A.2d 121, 123].) The courts applying this “modern rule” had no problem depriving the insurer of the property rights acquired by the wording of the policy of insurance. Instead, violating the often stated rules of insurance policy construction, the wording is changed to make the contract several rather than joint and simply ignores or re-writes the language that states the “entire” policy is void if “any insured” intentionally causes a loss, swears falsely or commits fraud.

The court in *Hedtcke* was persuaded that nothing in the language of the policy before it precluded treating the two insureds as if they had separately insured their respective interests in the property even though the property was jointly held as a single unit. The policy contained a standard provision absolving the insurer of liability for damage if it was “caused, directly or indirectly, by . . . neglect of the insured to use all reasonable means to save and preserve the property at and after a loss” or if “the hazard is increased by any means within the control or knowledge of the insured[.]” (*Hedtcke v. Sentry Ins. Co.*, *supra*, 326 N.W.2d at p. 736, fns. omitted.) This language did not make clear “whether the obligations of the insured are joint or several.” (Id. at p.740.) Accordingly, the court concluded the language was ambiguous and interpreted the policy

“as not barring an innocent insured from recovering under the policy merely by virtue of the fact that another insured intentionally caused the damage to the insured property.”

The courts of the U.S., like the *Watts* Court use the specter of public policy to dictate a rule that does damage to the clear and unambiguous language of the policy. Stating that although a wrongdoer should not benefit from his wrongdoing.” (*Kulubis v. Texas Farm Bureau Underwriters, supra*, 706 S.W.2d at p. 955.) the public policy behind the modern trend “requires that an innocent co-insured be permitted to recover based upon the insured’s reasonable expectations.” The modern rule benefits the public good by “not punishing the innocent victim for the wrongs of another” and “prevent[ing] unjust enrichment by the insurance company . . . .” After consideration of the competing policies, the court held that “the more enlightened reasoning dictates that the illegal destruction of jointly owned property by one co-insured shall not bar recovery under an insurance policy by an innocent co-insured.” The “enlightened reasoning” required the court to ignore the words of the contract and replace it with other words that allowed an insured to recover indemnity even if the insurer proves that an insured committed fraud.

Because the Kulubis’s property was not community property, the court left for another day “the problem of how to compensate the innocent spouse and yet not permit benefit to the wrongdoing spouse” where the damage occurred to community property. (*Kulubis v. Texas Farm Bureau Underwriters, supra*, 706 S.W.2d at p. 955.) That day, according to the *Watts* court came in 1999, in *Texas Farmers Ins. Co. v. Murphy* (Tex. 1999) 996 S.W.2d 873. The factual situation in *Murphy* was similar to the situation in *Kulubis*: Mr. *Murphy* set fire to the house owned by him and his wife, burning it and all its contents. Mrs. *Murphy* was found to be innocent of prior knowledge or complicity. The significant differences were that the destroyed property was held as community property, and no petition for divorce had been filed until after the lawsuit against the insurer was instituted. The court recognized that a rule permitting the innocent spouse to recover as long as there was a divorce proceeding going forward or a partition agreement in effect would make sense, but was troubled by the prospect that this could encourage married couples to divorce. (*Murphy*, at p. 877.) Equally troubling was the prospect that such actions would be undertaken in bad faith where the couple planned to get back together after recouping their losses

In the end, the court concluded that “a rule conditioning an innocent spouse’s recovery on partition or divorce is neither practical nor satisfactory. . . . [¶] It is not the courts’ business to superintend what innocent co-insureds may do with any insurance proceeds they are contractually entitled to recover. Nor, under these circumstances, is it the courts’ province to regulate an innocent spouse’s marital relationship with the culpable spouse. The preferable rule is to allow innocent spouses to recover according to their contracts, regardless of partition or divorce. [¶] We reaffirm our longstanding public policy preventing an arsonist from benefiting from fraud by denying recovery of his or her own one-half interest in the claim against the insurer. We conclude, however, that such public policy does not overcome an innocent spouse’s contractual right to recover her or his one-half interest in the policy benefits.” (*Texas Farmers Ins. Co. v. Murphy, supra*, 996 S.W.2d at p. 881.) . However, in *King v. Dallas Fire* (2000) 275 S.W. 3d 117, 2000 TX

0049304 the intentional act condition was found by the Texas Court of Appeal to deprive an innocent employer of coverage for the intentional battery by one of his employees.

The *Watts* Court reported that its research (which seems limited to those cases that agreed with its decision) indicated that nearly every court that looked at this issue in recent years has agreed with the Texas and Wisconsin Supreme Courts that the manner in which the property is held should have no significance and that, instead, the language of the policy is determinative of whether the innocent spouse will be allowed recovery. (See, e.g., *Atlas Assur. Co. of America v. Mystic* (Alaska 1991) 822 P.2d 897, 900 [following rule that “allows an innocent or divorced spouse to recover even though the co-insured spouse is at fault” under the reasoning that “policy language excluding coverage must be explicit”; that “what is in question is the spouse’s interest in the insurance policy, not the interest in the real property”; and that “the fault of the wrongdoing spouse cannot be imputed to the innocent spouse”]; *Overton v. Progressive Ins. Co.* (Fla. 1991) 585 So.2d 445, 447, fn. 1 [“Recovery under the new dominant rule . . . is grounded on the fact that the contract rights and the fraud liability are deemed to be divisible regardless of the nature of the property interests”]; *Richards v. Hanover Ins. Co.* (Ga. 1983) 299 S.E.2d 561, 563 [“Recently . . . an increasing number of courts have focused their analysis not on the joint or individual nature of the underlying property right, but on the rights and duties embodied in the language of the contract of insurance. . . . [¶] We, too, look to the rules of contract to resolve the present dispute. In Georgia, insurance is a matter of contract, and the parties to an insurance policy are bound by its plain and unambiguous terms”]; *Ryan v. MFA Mut. Ins. Co.* (Tenn.App. 1980) 610 S.W.2d 428, 437 [holding that the “new majority” rule was “better reasoned” and “produce[d] a more equitable result” and that if the insurer “wanted to assure its position, i.e. that misconduct of any insured would bar recovery by other insured,” it should have “made it clear and unambiguous in the policy” and “informed the prospective applicants for insurance of this position from the start”]; *Morgan v. Cincinnati Ins. Co., supra*, 307 N.W.2d 53, 55 [“Henceforth whenever the statutory clause limiting the insurer’s liability in case of fraud by the insured is used it will be read to bar only the claim of an insured who has committed the fraud and will not be read to bar the claim of any insured under the policy who is innocent of fraud”]; *Steigler v. Insurance Co. of North America* (Del. 1978) 384 A.2d 398, 402 [“Our construction and application of the contract rights of the parties thus leads us to agree with [the case] which seems to us to represent both a more modern analysis of the problem and to produce a fairer result”]; *Hildebrand v. Holyoke Mut. Fire Ins. Co.* (Me. 1978) 386 A.2d 329, 331, quoting *Howell v. Ohio Casualty Ins. Co.* (N.J.Super. 1974) 327 A.2d 240, 242 [holding that irrespective of whether the interests of the plaintiff and her husband in the destroyed property are deemed to be joint or several, “[t]he significant factor is that the responsibility or liability for the fraud here, the arson is several and separate rather than joint, and the husband’s fraud cannot be attributed or imputed to the wife who is not implicated therein”].)

The reasoning of these courts, although granting lip-service to applying the language of the contract of insurance, actually rewrites the contract and ignores the modern language of insurance contracts that void insurance if any insured commits fraud. In doing so these courts seem to ignore long-held rulings of the California Supreme Court. In *Williamson*

& *Vollmer Engineering, Inc. v. Sequoia Ins. Co.* (1976) 64 Cal. App. 3d 261 [134 Cal. Rptr. 427], rescission of an engineering firm's malpractice policy by the insurer was affirmed where the insured, in the application, had denied knowledge of any circumstances which might result in a claim. The court concluded that the materiality of the insured's negative representation was established by the terms of the policy and (citing *Thompson v. Occidental Life Ins. Co.*, 9 Cal. 3d 904) the fact that the question was asked on the application. In addition, as here, there was evidence that had the insurer known the truth it would not have provided insurance without an exclusion for the prior claim. Quoting from a case which dealt with an analogous problem, the court concluded that "*An insurance company is entitled to determine for itself what risks it will accept, and therefore to know all the facts relative to the applicant's physical condition. It has the unquestioned right to select those whom it will insure and to rely upon him who would be insured for such information as it desires as a basis for its determination to the end that a wise discrimination may be exercised in selecting its risks.* [Citation.]" (*Robinson v. Occidental Life Ins. Co.* (1955) 131 Cal. App. 2d 581, 586 [281 P.2d 39]. [Citation.])" (64 Cal. App. 3d at p. 273.) The decision in *Watts* and *Rosen* seems to deprive the insurer of what was called an "unquestioned right" to select those whom it will insure or indemnify.

The *Watts* court, justifying its reaching the "fair" result rather than that imposed by the contract, stated:

Focusing on how differences in the language of the policy's provisions can impact an innocent spouse's right to recover, one commentator has summarized the new majority rule as follows: "Generally, where a policy precludes recovery as a result of fraud on the part of 'the' insured, the recovery is precluded only as to the insured who committed the fraud and the innocent co-insured is allowed to recover. On the other hand, where a policy precludes recovery as a result of fraud on the part of 'any' insured, the effect of the fraudulent acts of one insured preclude recovery as to all insureds and an innocent co-insured is thereby precluded from recovery." (13 *Couch on Insurance* (3d ed. 1999) § 197:34, p. 197-65, italics added, fn. omitted.)

Regardless, the *Watts* court found it prudent to ignore the "any insured" language of the Farmers policy. Rather it followed, in *Hildebrand v. Holyoke Mut. Fire Ins. Co.*, *supra*, 386 A.2d 329, where the fraud provision stated: "This entire policy shall be void if, whether before or after a loss, the insured has willfully concealed or misrepresented any material fact or circumstance concerning this insurance or the subject thereof, or the interest of the insured therein, or in case of any fraud or false swearing by the insured relating thereto," the court explained that the language did not preclude the innocent wife from recovering despite the wrongdoing of her husband: "We construe the term 'insured' in the . . . above quoted clause of the policy to mean a specific insured, namely, the insured who (1) is responsible for causing the loss and (2) is seeking to recover under

the policy. [Citation.] We therefore conclude that the instant policy allows recovery by the 'Named Insured' [the wife] for the loss despite the fact that it resulted from the intentional act of another 'insured.' [Citation.]" (Id. at p. 331, italics omitted; accord, *Richards v. Hanover Ins. Co.*, supra, 299 S.E.2d at pp. 563-564 [where policy designated husband and wife as the "named insured," and further provides for an exclusion from liability in the event of "neglect of the insured to use all reasonable means to save and preserve property . . .," the court concluded that it was "reasonable that a person in [the wife's] position reading this homeowners policy would assume that the obligation to preserve the insured property devolved upon her individually as an 'insured' under the policy, and that the term 'insured' as used in the neglect provision referred to the individual co-insured who fails to preserve the insured property"]; In *Ryan v. MFA Mut. Ins. Co.*, supra, 610 S.W.2d at pp. 427, 440 [where policy contained standard provision stating "[t]his entire policy shall be void if, whether before or after a loss, the insured has willfully concealed or misrepresented any material fact or circumstance concerning this insurance or the subject thereof, or the interest of the insured therein, or in case of any fraud or false swearing by the insured relating thereto," court held that "a reasonable person, reading the provision in the policy . . . which referred to fraud of 'the insured,' and neglect of 'the insured,' etc. would conclude that if an insured was guilty of fraud or neglect or increasing of hazard to property, then he or she may not recover under the policy. On the contrary, in *Webb v. American Family Mut. Ins. Co.*, 493 N.W.2d at p. 812 [holding that policy reference to "an insured" in fraud provision unambiguously excluded coverage to both spouses if either insured committed fraud].)

None of the courts cited by *Watts* that recognized or applied a rule allowing an "innocent spouse" to recover (as if two separate and distinct policies had been issued) a divisible share of the damaged property applied the clear and unambiguous language of the policy. Rather, *Watts* and the cases it relied upon, decided it was equitable to deprive an insurer of property rights to give to a person it determined was an "innocent spouse" rights to recover from a policy that specifically, explicitly and clearly made the policy void.

Although it appears to be ancient and not favored, the change of the rule that now allows the "innocent" spouse to recover is an incentive to commit fraud. The finding in *Watts* and the decisions on which it relies, allowing an "innocent spouse" to recover defeats for a claimed "public policy" reason, the language of the policy that makes the entire policy void if an insured commits fraud his or her spouse can still recover. There is no downside to fraud if you are married or own property in a partnership since your spouse or your partner will still be able to recover the benefits of the insurance policy. In doing so the *Watts* court ignored the oft-stated public policy that declares it wrongful to allow recovery for insurance fraud. For example, California Insurance Code Section 1871 states the public policy as:

(a) The business of insurance involves many transactions that have the potential for abuse and illegal activities. There are numerous law enforcement agencies on the state and local levels charged with the responsibility for investigating and prosecuting fraudulent activity. This

chapter is intended to permit the full utilization of the expertise of the commissioner and the department so that *they may more effectively investigate and discover insurance frauds, halt fraudulent activities*, and assist and receive assistance from federal, state, local, and administrative law enforcement agencies in the prosecution of persons who are parties in insurance frauds.

(b) Insurance fraud is a particular problem for automobile policyholders; fraudulent activities account for 15 to 20 percent of all auto insurance payments. Automobile insurance fraud is the biggest and fastest growing segment of insurance fraud and contributes substantially to the high cost of automobile insurance with particular significance in urban areas. [Italics added]

Allowing a so-called “innocent spouse” to recover when an insurer can prove that an insured attempted or committed fraud makes the public policy to protect an “innocent spouse’s” property rights more important than the public policy to defeat fraud stated by § 1871 or to apply the clear and explicit language of a policy. The *Watts* decision appears to contradict the finding of the California Supreme Court in *Rosen* that held, with regard to a clear and unambiguous “collapse” limitation:

Our reason [for applying the contract terms] is that we do not rewrite any provision of any contract, including the standard policy underlying any individual policy, for any purpose. (citation omitted) To do so with regard to the standard policy, with which we are here concerned, might have untoward effects generally on individual insurers and individual insureds and also on society itself. ... To rewrite the provision imposing the duty to indemnify in order to remove its limitation to money ordered by a court might compel insurers to give more than they promised and might allow insureds to get more than they paid for...

The “innocent spouse” doctrine is just the type of rewriting of a policy that the California Supreme Court found unacceptable. It is time the Supreme Court took a look at the “innocent spouse” cases and determine that it is necessary that the wording of the policy, when it is clear and unambiguous, be enforced. Although paying an innocent spouse insured for a benefit for which he or she did not pay may provide society with benefits that might outweigh any costs that it might impose on individual insurers and individual insureds, as the California Supreme Court said: “It is conceivable. But unknown. Knowledge ‘depend(s) in large part on’ what we are ill suited for, that is, the ‘amassing and analyzing of complex and extensive empirical data.’ (citation omitted) Without such knowledge we could not proceed.”

Insurers must conduct a thorough investigation and if it finds that one, but not all of the insureds' have committed fraud, it must evaluate the economic benefit it will receive if it denies the claim of one spouse only to be forced to pay the "innocent spouse." The cost of defeating such a fraud will probably be more than any possible saving, and the court will have forced insurers to pay fraudulent claims in a misguided service to equity. They will also defeat the intent of the "Insurance Frauds Prevention Act" that compels insurers to create an anti-fraud program since the actions of the courts applying the "modern rule" require payment even when fraud is proved.

-- End --

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[Barry Zalma, Esq., CFE, is an insurance claims consultant and insurance coverage attorney. He is the founder of Barry Zalma, Inc., a California law firm whose practice emphasizes the representation of insurers and those in the business of insurance and ClaimSchool, a provider of consulting and training services to the insurance industry and its counsel.

Mr. Zalma is an internationally recognized expert on insurance claims and has testified as an expert witness in the California Superior Court, the United States District Court and the Superior Court of Nebraska. He is recognized as an expert on insurance claims handling, the commercial general liability policy, the comprehensive general liability policy, bad faith, insurance fraud, Jewelers' Block Insurance and other inland marine coverages. Mr. Zalma is the author of, or has rewritten, CGL, fire, auto, earthquake, Jewelers' Block and other insurance policies for insurer clients.

Mr. Zalma is the author of *Insurance Claims: A Comprehensive Guide* and the soon to be published *Mold Claims Guide* available from Specialty Technical Publishing at <http://www.stpub.com>; *The Truth, The Whole Truth & Nothing But The Truth*, *Property Claims 2nd Edition*, *Liability Claims* and all course books used by ClaimSchool, Inc. in its training programs. He is also the author of three books published by Thomas Investigative Publishing, and numerous articles for insurance trade publications and law journals. Mr. Zalma writes the monthly "*Zalma's Insurance Fraud Letter*" which is available, FREE, from ClaimSchool, Inc. and over the

internet at <http://www.zalma.com>. He writes a regular column on insurance fraud for the "John Cooke Insurance Fraud Report" and "Georgia News and Views".]