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UNITED STATES DISTRICT COURT

CENTRAL DISTRICT OF CALIFORNIA

NORTHROP GRUMMAN CORPORATION, Plaintiff, v. FACTORY MUTUAL INSURANCE COMPANY, Defendant.	Case No. CV 05-08444 DDP (PLAx) **ORDER GRANTING NORTHROP'S MOTION FOR PARTIAL SUMMARY JUDGMENT AND DENYING FACTORY MUTUAL'S MOTION FOR PARTIAL SUMMARY JUDGMENT** [Motions filed on March 19, 2007]

Plaintiff Northrop Grumman Corporation ("Northrop") and Defendant Factory Mutual Insurance Company ("Factory Mutual") each seek partial summary judgment on the issue of whether the 2005-2006 excess insurance policy that Factory Mutual sold to Northrop covers Northrop's storm surge loss caused by Hurricane Katrina. After reviewing the papers submitted by the parties, the Court grants Northrop's motion, denies Factory Mutual's motion and adopts the following order.

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I. STATEMENT OF FACTS[1]

Northrop is a global defense and technology company that provides a broad array of innovative systems, products, and solutions in information and services, electronics, aerospace, and shipbuilding to government and commercial customers worldwide. Northrop is a Delaware corporation with its principal place of business in Los Angeles, California. Northrop's Mississippi subsidiary, Northrop Grumman Ship Systems ("NGSS"), is a shipbuilder headquartered in Pascagoula, Mississippi.

Factory Mutual is a Rhode Island corporation with its principal place of business in Rhode Island. Factory Mutual is authorized to transact business in the County of Los Angeles and the State of California.

This litigation centers upon Northrop's 2005-2006 property insurance. Northrop employs AON Risk Services of Southern California ("AON") to represent its needs in the insurance market. To obtain property insurance for Northrop for the 2005-2006 policy year, AON submitted a proposal to the insurance market. The proposal specified details of the coverages and sub-limits that Northrop wanted to purchase. It requested a sub-limit of "$400 million per occurrence and in the Annual Aggregate as respects Flood." The proposal also contained a "suggested layering," describing the primary layer(s) as "All risk including earthquake, flood & boiler & machinery," and the excess layer as "All Risk Including Boiler & Machinery (Excluding Earthquake and Flood)." AON's suggested premium for the primary $500 million totaled

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[1] The Court understands these facts to be undisputed.

$12,730,000. The suggested premium for the excess layer was $950,000.[2]

In response to AON's submission, Factory Mutual provided a quote for the 2005-2006 property renewal for its 15% participation in the first $100 million of coverage, and "Blanket limit" participation excess of $500 million, "subject to applicable policy sub-limits." Factory Mutual's quote reflected the sub-limits that AON requested, including the $400 million sub-limit for Flood.

Northrop, through AON, accepted Factory Mutual's quote and, on March 31, 2005, Factory Mutual transmitted its primary and excess policies to AON. The Primary Policy no. UB270 participated 15% in the first $100 million of coverage and expressly provided coverage for Flood, subject to all other Policy terms, conditions, and exclusions.[3] The Excess Policy no. UB276 provided the remaining $19.8 billion in blanket coverage limits.

The Primary Policy defines and covers the separate perils of "Flood," "Wind," and "Named Windstorm." Flood is defined in the Primary Policy as:

> [F]lood waters, rising waters, waves, tide or tidal water, surface waters, or the rising, overflowing, or breaking of boundaries of lakes, reservoirs, rivers, streams or other bodies of water, whether driven by wind or not, including spray and sewer back-up resulting from any of the

[2] Neither party submitted any evidence indicating whether these suggested premiums were typical for this insurance market.

[3] Factory Mutual has paid its $15 million limit under the primary policy and Northrop has not sued under that policy.

foregoing, all regardless of any other cause or event contributing concurrently or in any other sequence of loss

(emphasis added). Wind is defined in the Primary Policy as the "[d]irect action of wind including substance driven by wind." "Named Windstorm" is defined as:

> The direct action of wind including any substance driven by wind, and/or flood when such wind or flood is associated with or occurs in conjunction with a storm or weather disturbance which is identified by name prior to loss by any meteorological authority such as the U.S. National Weather Service or National Hurricane Center.

The Primary Policy contains a $10 million per occurrence deductible for loss or damage caused by "Named Windstorm" at the Mississippi and Avondale, Louisiana locations.

The Excess Policy does not repeat the Primary Policy's definitions of Named Windstorm or Wind, nor does it exclude coverage for losses caused by either peril. The Excess Policy does, however, contain the following Flood Exclusion:

> Flood; surface waters; rising waters; waves; tide or tidal water; the release of water, the rising, overflowing or breaking of boundaries of natural or man-made bodies of water; or the spray therefrom; or sewer back-up resulting from any of the foregoing; regardless of any other cause or event contributing concurrently or in any other sequence of loss.

On August 29, 2005, Hurricane Katrina struck the U.S. Gulf Coast, making landfall near the Louisiana/Mississippi border. NGSS/Northrop sustained property damage from Hurricane Katrina at

three separate facilities. The storm surge from Hurricane Katrina was a significant cause of the damage.

Northrop claimed coverage for its losses under the Primary Policy and the Excess Policy. Factory Mutual rejected coverage for a substantial part of Northrop's loss, asserting that the Flood Exclusion in the Excess Policy bars coverage for losses caused by Hurricane Katrina's wind-driven storm surge. Both parties now move for summary judgment on this issue - the sole issue presented in Phase I[4] of this litigation.

II. LEGAL STANDARD

Under the Federal Rules of Civil Procedure 56(c), summary judgment is proper only where "the pleadings, depositions, answers to interrogatories, and admissions on file, together with the affidavits, if any, show that there is no genuine issue as to any material fact and that the moving party is entitled to a judgment as a matter of law." Fed. R. Civ. P. 56. The moving party has the burden of demonstrating the absence of a genuine issue of fact for trial. See Anderson v. Liberty Lobby, Inc., 477 U.S. 242, 256 (1986). If the moving party satisfies the burden, the party opposing the motion must set forth specific facts showing that there remains a genuine issue for trial. See id.; Fed. R. Civ. P. 56(e).

A non-moving party who bears the burden of proof at trial to an element essential to its case must make a showing sufficient to

[4] Phase I is limited to "issues regarding contract interpretation, including any purported admissions of the parties." (Stip. & Order Regarding Scheduling for Phase I, May 26, 2006.)

establish a genuine dispute of fact with respect to the existence of that element of the case or be subject to summary judgment. See Celotex Corp. v. Catrett, 477 U.S. 317, 322 (1986). Such an issue of fact is a genuine issue if it reasonably can be resolved in favor of either party. See Anderson, 477 U.S. at 250-51. The non-movant's burden to demonstrate a genuine issue of material fact increases when the factual context renders her claim implausible. See Matsushita Electrical Industrial Co. v. Zenith Radio Corp., 475 U.S. 574, 587, 106 S. Ct. 1348, 1356 (1986). Thus, mere disagreement of the bald assertion that a genuine issue of material fact exists, no longer precludes the use of summary judgment. See Harper v. Wallingform, 877 F.2d 728 (9th Cir. 1989); California Architectural Building Products, Inc. v. Franciscan Ceramics, Inc., 818 F.2d 1466, 1468 (9th Cir. 1987), cert. denied, 484 U.S. 1006 (1988).

III. CHOICE OF LAW

As an initial matter, the Court must determine whether California law should apply to this insurance contract dispute. Choice-of-law rules are "substantive" for purposes of diversity jurisdiction. Federal courts sitting in diversity must apply the same choice-of-law rules that local courts would apply. Klaxon Co. V. Stentor Elec. Mfg. Co., 313 U.S. 487, 496 (1941).

California resolves choice-of-law questions using a "governmental interest analysis" to find the proper law to apply based upon the interests of the litigants and the involved states. Offshore Rental Co. v. Continental Oil Co., 22 Cal.3d 157, 161 (1978) (quotation omitted). California applies its own rule of

decision unless a party litigant properly invokes the law of a foreign state. A party advocating application of foreign law must demonstrate that the [foreign] rule of decision will further the interest of that foreign state and, therefore, that it is an appropriate one for the forum to apply to the case before it." Hurtado v. Super. Ct., 11 Cal. 3d 574, 581 (1974); see Liew v. Official Receiver and Liquidator, 685 F.2d 1192, 1197 (9th Cir. 1982).

Factory Mutual does not perceive that a conflict of laws exists between the states of California and Mississippi on the issues presented. However, Factory Mutual has indicated that if the Court determines that an actual conflict of law exists, it will offer additional briefing on this issue at the Court's request.

As indicated above, the burden of finding a conflict between Mississippi and California law does not rest with the Court. The Court is not aware of any conflict between the two states' contract interpretation laws that would affect its analysis of these motions. Accordingly, the Court will apply the California rules of contract interpretation to these motions.

IV. CONTRACT INTERPRETATION

Under statutory rules of contract interpretation, the mutual intention of the parties at the time the contract is formed governs interpretation. Cal. Civ. Code. § 1636; AIU Ins. Co. v. Super. Ct., 51 Cal. 3d 807, 821 (1990). Such intent is to be inferred, if possible, solely from the written provisions of the contract. Id. § 1639. The clear and explicit meaning of these provisions, interpreted in their ordinary and popular sense, unless used by the

parties in a technical sense or a special meaning is given to them by usage, controls judicial interpretation. Id. § 1644.

If the Court finds that a policy provision is capable of two or more constructions - i.e., if the provision lacks a "clear and explicit meaning" - it must interpret the contract "as a whole" to determine which construction reflects the mutual intention of the parties at the time of formation. Bank of the West v. Super. Ct., 2 Cal. 4th 1254, 1265 (1992). The burden is on the insured to establish that its claim is within the basic scope of coverage and on the insurer to establish that the claim is specifically excluded. MacKinnon v. Truck Ins. Exchange, 31 Cal. 4th 635, 648 (2003). Stated differently, a court that is faced with an argument for coverage based on assertedly ambiguous policy language must first attempt to determine whether coverage is consistent with the insured's objectively reasonable expectations. Bank of the West, 2 Cal. 4th at 1265. In so doing, the Court must interpret the language in context, with regard to its intended function in the policy.[5] Id.

Furthermore, the Ninth Circuit has observed that while the rule of contract interpretation applying to coverage provisions

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[5] Northrop argues that once the Court determines that the language is capable of two or more constructions, it must rule in Northrop's favor. However, this argument omits an important step in contract interpretation: the Court must still determine whether Northrop's construction is consistent with Northrop's objectively reasonable expectation of coverage at the time of contract formation. Only after finding that Northrop's construction is reasonable under the circumstances of the case may the Court resolve any ambiguity in Northrop's favor. Bank of the West, 2 Cal. 4th 1254, 1265 ("[L]anguage in a contract must be construed in the context of that instrument as a whole, and in the circumstances of that case, and cannot be found ambiguous in the abstract.").

"favors the insured over the insurer," the contract interpretation rule applicable to exclusions is "substantially" even more stringent. PMI Mortgage Ins. Co. v. Am. Int'l Specialty Lines Ins. Co., 394 F.3d 761, 765 n.5 (9th Cir. 2005); see also Zurich Ins. Co. v. Smart & Final Inc., 996 F. Supp. 979, 987 (C.D. Cal. 1998) (special rules apply to policy exclusions).

> "[Whereas], insurance coverage is interpreted broadly so as to afford the greatest possible protection to the insured, . . . exclusionary clauses are interpreted narrowly against the insurer. An insurer cannot escape its basic duty to insure by means of an exclusionary clause that is unclear. As we have declared time and again any exception to the performance of the basic underlying obligation must be so stated as clearly to apprise the insured of its effect. Thus, the burden rests upon the insurer to phrase exceptions and exclusions in clear and unmistakable language. The exclusionary clause must be conspicuous, plain and clear."

MacKinnon, 31 Cal. 4th at 648 (citations omitted).

If, after considering the overall circumstances of the case, the Court determines that the insured's construction is reasonable, the Court will construe the ambiguous language against the party who caused the uncertainty to exist. AIU, 51 Cal. 3d at 822; see also MacKinnon, 31 Cal. 4th at 655 (reasoning that even if an insurer's interpretation of a policy exclusion is reasonable, if the insured's interpretation is at least as reasonable, that interpretation will govern). This party is typically the insurer; because the insurer writes the policy, it is held responsible for

ambiguous policy language, which is therefore construed in favor of coverage. Id. However, where the policy holder does not suffer from lack of legal sophistication or a relative lack of bargaining power, and where it is clear that an insurance policy was actually negotiated and jointly drafted, courts need not go so far in protecting the insured from ambiguous or highly technical drafting. Id. at 823.

IV. WHETHER THE PLAIN LANGUAGE OF THE EXCESS POLICY EXCLUDES DAMAGE FROM STORM SURGES

It is undisputed that the Excess Policy explicitly excludes coverage for Flood damage. The question presented is whether the plain language of the Excess Policy requires the Court to find that the Flood exclusion encompasses "storm surge."

The term "Flood" is defined in the Excess Policy as follows:

> Flood; surface waters; rising waters; waves; tide or tidal water; the release of water, the rising, overflowing or breaking of boundaries of natural or man-made bodies of water; or the spray therefrom; or sewer back-up resulting from any of the foregoing; regardless of any other cause or event contributing concurrently or in any other sequence of loss.

Factory Mutual argues that this Flood exclusion clearly and explicitly encompasses losses caused by "storm surges." First, Factory Mutual contends that the ordinary meanings of both "flood" and "storm surge" are "an inundation of water on normally dry

land."[6] It also contends that the terms "rising water," "tide" or "tidal water," and "the rising overflowing or breaking of boundaries of natural or man-made bodies of water" - terms all found within the Excess Policy's definition of Flood - describe a "storm surge." Factory Mutual points to the deposition excerpts of several Northrop employees as evidence that laymen, as well as

[6] Factory Mutual notes that the first term used to define Flood is "flood." The Oxford English Dictionary defines "flood" as "an overflowing or irruption of a great body of water over land not usually submerged; an inundation, a deluge." 5 Oxford English Dictionary 1076 (2nd ed. 1989). Webster's Ninth New Collegiate Dictionary defines "flood" as "a raising and overflowing of a body of water esp. onto normally dry land." Webster's Ninth New Collegiate Dictionary 474 (9th ed. 1988). Thus, Factory Mutual contends, the ordinary meaning of Flood can be discerned from reading the dictionary definition and heeding the term's common usage.

Factory Mutual also offers the testimony of Northrop and AON executives - Curtis Anderson, AON's Managing Director of Property Claims, and Steve Pierce, Northrop's Manager of Risk Management - whose personal interpretations reveal a common understanding of "flood" and "storm surge" as the inundation of normally dry areas of land by water. (*Factory Mutual Ins. Co.'s Mem. of P. & A. in* Supp. of its Mot. for Partial Summ. J. ("FM Mot.") 15:6-11; Ex. 19 Curtis Anderson Dep. 73:14-21, 23-24, 74:5; Ex. 7 Steven Pierce Dep. 68:1-16, 71:15-25.) Northrop, however, correctly objects to the admissibility of this evidence because it is not indicative of the parties' intentions at the time of contracting. Nat'l Union Fire Ins. Co. v. Lawyers' Mut. Ins. Co., 885 F. Supp. 202, 207 (S.D. Cal. 1995) (sustaining an evidentiary objection where "the documents themselves do not deal with evidence concerning the parties intention in formation of the policy, but rather post-formation dealings between the insured and the carriers," and thus have "dubious relevance"). Therefore, the definitions provided by English dictionaries and AON/Northrop executives are irrelevant.

Factory Mutual further claims that there is no evidence that at the time of contracting, the parties intended for these terms to *be interpreted in any manner other than their "ordinary and popular* sense." However, because these insurance policies are elaborate contracts negotiated and signed by sophisticated parties, it would be reasonable for a party to believe the policy terms were being used in a technical manner. Thus, Northrop could have disregarded the various ordinary and popular meanings of the terms and, instead, relied strictly upon the definitions as they were written in the contract. If so, it would have been reasonable for Northrop to have assumed that the dissimilarities in the definitions created an exclusion for flood caused by wind or hurricane.

those in the insurance industry, would interpret these terms to encompass "storm surge."[7] Thus, Factory Mutual contends that

[7] Factory Mutual notes that AON representative Robert Hayes testified that storm surge is both "rising water" and "the rising or overflowing or breaking of natural boundaries." (FM Mot. 15:16-17; Ex. 9 Robert Hayes Dep. pp. 120-122.) Mr. Hayes also testified that a named storm like Katrina can produce storm surge flooding. (FM Mot. 15:17-18, 16:1; Ex. 9 Hayes Dep. 120:11-14.) Moreover, AON's Curtis Anderson testified that the terms "rising water" and "the release of water, the rising, overflowing or breaking of boundaries of natural or man-made bodies of water" are associated with "storm surge." (FM Mot. 16:1-3; Ex. 19 Anderson Dep. pp. 75-79.)

Similarly, Northrop's Director of Risk Management Dean Reynolds testified that the terms "rising water," "tide" or "tidal water," and "the rising, overflowing or breaking of boundaries of natural or man-made bodies of water" encompass or include "storm surge." (FM Mot. 16:4-7; Ex. 16 Dean Reynolds Dep. pp. 152-154.) Northrop's Manager of Risk Management Steve Pierce also testified that "storm surge" could be considered "rising waters" and "waves." (FM Mot. 16:7-8; Ex. 7 Pierce Dep. pp. 68-69.) Finally, Northrop's Treasurer Jim Sanford, to whom Northrop's Risk Management department reports, wrote an e-mail well before Hurricane Katrina occurred stating that "from a layman's perspective" hurricane storm surge is "flood." (FM Mot. 16:9-11; Ex. 22 February 20, 2004 E-Mail String.)

However, various Northrop employees whose statements were cited by Factory Mutual also contradicted these assertions. (Northrop's Opp'n p. 23-24.) Northrop employee Dean Reynold's 30(b)(6) testimony states that in connection with the 2005 renewal process, he (1) reviewed the Underwriting Detail, and its definition of "storm surge," and believed that storm surge was part of "Windstorm," and (2) received representations from AON that the Factory Mutual Policies were all-risk policies that covered, without limitation, losses caused by Named Windstorm and Windstorm. (Northrop's Mem. of P. & A. in Opp'n to Factory Mutual's Mot. for Partial Summ. J. "Northrop Opp'n" 23:17-24:6; CSOF ¶¶ 66, 68.) Additionally, Factory Mutual omits Jim Sanford's testimony that Northrop "felt [it] had purchased windstorm coverage, including all the property damage associated with windstorm." (Northrop Opp'n 24:7-10; CSOF ¶ 70.) Factory Mutual also did not cite Northrop employee David Strode's testimony that he "presumed that any loss arising our of a hurricane or a wind storm would be covered" because the Excess Policy "was an all-risk policy and [he] didn't think there were any exclusions for hurricanes or a wind storm." (Northrop Opp'n 24:11-14; CSOF ¶ 71.) Mr. Pierce also made a statement that it "was [his] understanding, that [Northrop] had full coverage for any loss related to hurricane damage." (Northrop Opp'n 24:14-18; CSOF ¶ 69.)

AON's witnesses similarly testified that they believed the Factory Mutual Policies provided blanket limit coverage for loss (continued...)

because the definition of Flood as written in the Excess Policy clearly encompasses the storm surge damage that occurred at Pascagoula, the absence or omission of other words is entirely inconsequential.

Factory Mutual further argues that the courts of Mississippi and other jurisdictions where hurricanes occur treat wave action, tidal water, tidal surge, rising water, and storm surge as "flood," which is typically excluded or limited under property insurance policies. (See Factory Mutual Mot. 16 n.63.) Factory Mutual cites this authority as additional evidence that the Flood exclusion in the Excess policy is clear and unambiguous.

To understand whether "storm surge" is plainly encompassed by the Excess Policy's Flood exclusion, the Court must first determine the "ordinary and popular" meaning of this term. This is not an easy task; "storm surge" is not defined in the Excess or Primary Policy and it is not a term with which the "lay" person is typically familiar. The National Hurricane Center offers the following definition of storm surge:

> Storm surge is simply water that is pushed toward the shore by the force of the winds swirling around the storm. This

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[7] (...continued)
caused by hurricanes, including loss caused by storm surge, because the Factory Mutual Policies were all-risk policies and did not exclude Named Windstorm. (Northrop Opp'n 24:18-21; CSOF ¶¶ 73-76.)

In short, for every statement Factory Mutual uses to support its conclusion that storm surge flooding was excluded in the Excess Policy, Northrop cites other testimony indicating that Northrop employees expected storm surge coverage under the all-risk policy. Thus, although the statements do not provide the Court with a clear indication of whether storm surge was actually excluded by the Flood definition in the Excess Policy, the contradictory statements demonstrate the ambiguity created by the inconsistent definitions.

advancing surge combines with the normal tides to create the hurricane storm tide, which can increase the mean water level 15 feet or more. In addition, wind driven waves are superimposed on the storm tide. This rise in water level can cause severe flooding in coastal areas, particularly when the storm tide coincides with the normal high tides.[8]

Other authorities also state that "the main driver of storm surges is the stress that the wind exerts on the water." See Kerry Emanuel, Divine Wind: The History and Science of Hurricanes 147 (2005). These definitions characterize "storm surge" as water pushed by the wind that combines with the hurricane storm tide to cause significant flooding.[9] Thus, at first blush, it appears that

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[8] The Court takes judicial notice of this definition, located at http://www.nhc.noaa.gov/HAW2/english/storm_surge.shtml.

[9] Factory Mutual emphasizes that the federal government has also defined "flood" broadly to encompass flooding from a hurricane event. The terms "flood or flooding" as used in the regulations governing the National Flood Insurance Program ("NFIP") are defined as "[a] general and temporary condition of partial or complete inundation of two or more acres of normally dry land areas from . . . the overflow of inland or tidal waters." National Flood Insurance Program, Definitions, 44 C.F.R. § 59.1 (2001). Additionally, the FEMA Flood Insurance Study ("FIS") for the City of Pascagoula, Mississippi states in Section 2.1 that its analysis "includes coastline flooding due to hurricane-induced storm surge." (FM Mot. 18:16-18; Ex. F, Federal Emergency Management Agency, Flood Insurance Study, City of Pascagoula, Mississippi, Jackson County 2 (1983) § 2.1.) Section 2.3 of the FIS states, under the subheading "Principal Flood Problems," that "[c]oastal areas along the Mississippi sound . . . are subject to coastal storm surge flooding and wave action as a result of hurricane and tropical storm activity in the Gulf." (FM Mot. 18:18-21; Ex. F § 2.3.)

Conversely, Northrop notes that the Insurance Services Office's ("ISO") standard property insurance form's "Water Exclusion" - which is comparable to a "flood exclusion - includes the phrase "whether driven by wind or not." (Notice of Northrop Grumman Corporation' Mot. for Partial Summ. J., and Mem. of P. & A. in Supp. Thereof ("Northrop Mot.") 19:5-7.) "ISO is a nonprofit trade association that provides rating, statistical, and actuarial policy forms and related drafting services to approximately 3,000 (continued...)

the Flood exclusion encompasses storm surges. It also appears that this interpretation would be consistent with a majority of the Mississippi and Louisiana court decisions.[10]

However, there are significant problems with interpreting this provision as clearly encompassing storm surge damage. Because the Excess Policy is undisputedly an "all risk" policy, "the limits of coverage are defined by the exclusions." Benavides v. State Farm Gen. Ins. Co., 136 Cal. App. 4th 1241, 1247 (2006) ("An all-risk policy covers risks of physical loss except those excluded under the terms of the insuring contract."). Accordingly, when determining whether a claim is covered under an all risk policy, "the insured does not have to prove that the peril proximately causing his loss was covered by the policy. This is because the policy covers all risks save for those risks specifically excluded by the policy." Strubble v. United Serv. Auto. Ass'n, 35 Cal. App. 3d 498, 504-05 (1973). Because "the burden rests upon the insurer to phrase exceptions and exclusions in clear and unmistakable language," the exclusionary clause in the Excess Policy "must be conspicuous, plain and clear" to preclude coverage for storm surge

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[9] (...continued)
nationwide property or casualty insurers. Policy forms developed by ISO are approved by its constituent insurance carriers and then submitted to state agencies for review." Pardee Constr. Co. v. Ins. Co. of the West, 77 Cal. App. 4th 1340, 1358 n.15 (2000) (citation and internal quotation marks omitted).

Although these definitions demonstrate that hurricane storm surge flooding may be defined with or without the words "whether driven by wind or not," the issue is not whether the Excess Policy standing on its own excludes flood. Rather, the issue is whether the inconsistent definitions of flood within the policies created an ambiguity that led the parties to have different beliefs about storm surge flood coverage. The Court finds that they did create such ambiguity.

[10] See, e.g., cases cited infra note 11.

damage. Mackinnon, 31 Cal. 4th at 648, quoting Aydin Corp. v. First State Ins. Co., 18 Cal. 4th 1183, 1188 (1998).

Here, none of the terms in the Excess Policy's Flood definition plainly and clearly reference hurricanes or damage caused by wind. Though Factory Mutual asserts that the terms "rising waters," "waves," "tide or tidal water," and "the overflowing or breaking of boundaries of natural or man-made bodies of water" - all terms included in the Excess Policy's Flood definition - should be interpreted to encompass storm surge, none of the terms expressly include wind-driven damage. In fact, each of those water events can be caused by phenomena other than wind, which is a peril covered by "all risk" property policies such as the Excess Policy. This is exacerbated by the fact that the Primary Policy's Flood definition contains the words "whether driven by wind or not," the Excess Policy omits these clarifying terms. Given that a storm surge is a particular type of "inundation of water" - an inundation caused, in part, by wind - this omission creates ambiguity in the Excess Policy's Flood exclusion.[11]

Moreover, as Northrop notes, the authority provided by Factory Mutual does not alleviate the ambiguity inherent in the contract. Specifically, Northrop argues that every case cited by Factory Mutual either involved a flood exclusion that contained the words "whether driven by wind or not" or did not address whether

[11] See MacKinnon, 31 Cal. 4th at 648 ("A policy provision will be considered ambiguous when it is capable of two or more constructions, both of which are reasonable.")

hurricane damage constitutes "flood" under an insurance policy."[12] Although none of the cases discuss or reference the words "whether driven by wind or not" as material to their conclusion that flooding arising out of a hurricane is excluded, the absence of that phrase in the Excess Policy lends support to Northrop's argument that the omission of the phrase creates ambiguity.

Additionally, Northrop maintains that the definitions of Wind and Named Windstorm in the Primary Policy control with respect to the Excess Policy. The Excess Policy does not separately define or exclude Wind or Named Windstorm, yet Factory Mutual does not dispute that Wind is a covered peril under the Excess Policy. (Northrop Mot. 12:19-20; SOF ¶¶ 44-45.) Similarly, Northrop contends, because the perils of "wind and/or flood" in association with a hurricane are redefined as the peril of Named Windstorm and

[12] While Northrop claims that "in every case [Factory Mutual] cites that quotes a flood exclusion, the quoted exclusion contains the words 'whether driven by wind or not' (or words to that effect)," only fifteen of the twenty-five cases actually refer to the phrase in question. (Northrop's Mem. of P. & A. in Opp'n to Factory Mutual's Mot. for Partial Summ. J. ("Northrop Opp'n") 5:13-14 (emphasis in original).)

The following cases reference the relevant language: Lunday v. Lititz Mut. Ins. Co., 276 So. 2d 696 (Miss. 1973); Grace v. Lititz Mut. Ins. Co., 257 So. 2d 217 (Miss. 1972); Lititz Mut. Ins. Co. v. Buckley, 261 So. 2d 492 (Miss. 1972); Lititz Mut. Ins. Co. v. Boatner, 254 So. 2d 765 (Miss. 1971); Fireman's Ins. Co. of Newark v. Schulte, 200 So. 2d 440 (Miss. 1967); West Beach Dev. Co. v. Royal Indem. Co., No. 99-0782-P-S, 2000 WL 1367994 (S.D. Ala. Sept. 19, 2000); Mayton v. Auto-Owners Ins. Co., No. 3:-5CV667, 2006 WL 1214831 (E.D. Va. May 2, 2006); Opar v. Allstate Ins. Co., 751 So. 2d 758 (Fl. Ct. App. 2000); Hardware Dealers Mut. Ins. Co. v. Berglund, 393 S.W.2d 309 (Tex. 1965); Transcon. Ins. Co. v. RBMW, Inc., 551 S.E.2d 313 (Va. 2001); Tuepker v. State Farm Fire & Cas. Co., No. 1:05CV559, 2006 WL 1442489 (S.D. Miss. May 24, 2006); Leonard v. Nationwide Mut. Ins. Co., 438 F. Supp. 2d 684 (S.D. Miss. 2006); Greer v. Owners Ins. Co., 434 F. Supp. 2d 1267 (N.D. Fla. 2006); Paulson v. Fire Ins. Exchange, 393 S.W.2d 316 (Tex. 1965); Transcon. Ins. Co. v. RBMW, Inc., 262 Va. 502, 551 S.E.2d 313 (2001).

are not explicitly excluded in the Excess Policy, the Excess Policy's flood exclusion cannot be said to "clearly" exclude hurricane storm surge damage.[13]

Factory Mutual attempts to account for this discrepancy by noting that the Primary Policy and the Excess Policy were written on two different policy forms. The Primary Policy is an AON/Factory Mutual "hybrid" form drafted by AON, and the Excess Policy is a separate Factory Mutual "Advantage" form drafted by Factory Mutual. Thus, Factory Mutual contends that the additional words may add emphasis, but their absence does not negate the plain meaning of the words used in the Flood exclusion.

Nevertheless, although Factory Mutual may have intended for the flood definition in the AON/Factory Mutual hybrid form to convey the same intent as Factory Mutual's Flood definition, the language used did not clearly and explicitly accomplish that objective. Moreover, as a matter of California law, the words "whether driven by wind or not" in the Primary Policy are not surplusage, and their absence from the Excess Policy cannot be

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[13] Factory Mutual argues that the Named Windstorm reference in the Primary Policy does not affect the exclusions in the Excess Policy because Named Windstorm appears only in the "Deductible" section of the Primary Policy. However, Named Windstorm, Flood and Wind are defined as general terms in the "definitional" section of the Primary Policy. (Volume of Exhibits in Support of Northrop Grumman Corporation's Mot. for Partial Summ. J. Ex. F Primary Policy UB270 60.L.) Because neither Wind nor Named Windstorm are redefined in the Excess Policy, it would have been reasonable for Northrop to presume that those definitions in the Primary Policy would be extended and applied to the Excess Policy. Moreover, because neither is listed as a specific exclusion, it would have been reasonable for Northrop to presume that the perils of Wind and Named Windstorm were covered by the Excess Policy. Conversely, where a term is given a new definition in the Excess Policy, without specifying whether it replaces or expands upon the previous definition given in the Primary Policy - i.e., Flood - the inconsistent definitions create ambiguity.

deemed meaningless. See Maxconn, 74 Cal. App 4th 1267, 1279 (1999); Mirpad, 132 Cal. App. 4th 1058, 1072-73 (applying "fundamental principle that policy language be so construed as to give effect to every term" to avoid rendering words in policy "superfluous and meaningless"). The absence of the terms "whether driven by wind or not" convey meaning, or at least create ambiguity, just as the inclusion of those words in the Primary Policy cannot be rendered surplusage and must convey meaning. See Maxconn, 74 Cal. App. 4th 1267, 1279 (1999).

It is conceivable that, if the Court were to construe the provisions of the Excess Policy in the absence of the Primary Policy, it might reach the same conclusion as Factory Mutual - that the policy clearly and explicitly encompasses a storm surge exclusion. However, the ambiguity present in the Flood exclusion is exacerbated by the inconsistent definitions of flood in the two policies. Specifically, it is not the mere omission of the phrase from the Excess Policy that creates ambiguity. Rather, it is the deviation from the initial definition used in the Primary Policy which creates uncertainty about whether "Flood" had different meanings in the Primary and Excess Policies.

The Court is bound by California law and common standards of contract interpretation to construe the language of the Excess Policy in the context of the document as a whole. MacKinnon, 31 Cal. 4th at 648 (stating that "language in a contract must be interpreted as a whole, and in the circumstances of the case"). In giving effect to every term in the two definitions of Flood, it is clear that the incongruent definitions create an ambiguity as to whether storm surge flooding is excluded in the Excess Policy.

Thus, although Factory Mutual argues that the Court should interpret the terms of the Excess Policy without regard to the Primary Policy, this approach seems illogical. The Excess Policy is clearly "excess" of something. It does not exist in a vacuum. Further, Factory Mutual was aware[14] of the definitions of Flood, Wind, and Named Windstorm in the Primary Policy. By using a definition of "Flood" in the Excess Policy that differed from the definition of "Flood" in the Primary Policy, Factory Mutual created an ambiguity that may have led Northrop to believe that Factory Mutual drafted an exclusion for flood" that did not clearly encompass storm surge damage. Accordingly, on its face, the Excess Policy fails to clearly exclude loss caused by "storm surge" or "wind-driven water."

V. OVERALL CONTEXT OF THE EXCESS POLICY

Because the Court finds that the plain language of the Flood Exclusion does not clearly encompass "storm surge," it must now examine the overall context of the Excess Policy to determine

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[14] The Primary Policy was structured in a shared/layered arrangement with approximately 30 participating insurers including Factory Mutual. (FM Mot. 4:7-9.) The second layer, above $500 million, was an excess layer with Factory Mutual as the only insurer. (FM Mot. 4:9-10.) To obtain property insurance for Northrop for the 2005-2006 policy year, AON submitted a proposal to the insurance market that requested a primary policy described as "All Risk including Earthquake, Flood, Boiler & Machinery" and suggested an excess layer described as "All Risk including Boiler & Machinery (Excluding Earthquake and Flood)." (FM Mot. 4:12-5:6; Ex. 24 398, emphasis in original.) In response, Factory Mutual provided a quote for the 2005-2006 property renewal insurance coverage. (FM Mot. 5:7-10.) Northrop, through AON, accepted Factory Mutual's quote and on March 31, 2005, Factory Mutual transmitted its primary and excess policies to AON. (FM Mot. 5:12-13; Ex. 3 March 31, 2005 E-Mail String p. 108.) Thus, Factory Mutual was clearly aware of the flood definition in the Primary Policy when it was issuing the Excess Policy.

whether Northrop's objectively reasonable expectations as understood by Factory Mutual at the time of contracting were that hurricane storm surge damage is Flood. Cal Civ. Code § 1649; see also Bank of the West, 2 Cal. 4th at 1264-65. Examples of what the Court may consider include: (1) negotiations or discussions about the scope of coverage; (2) any special meaning given to particular phrases by usage; or (3) other matters that might reflect the mutual understanding of the parties concerning the scope of coverage. Fireman's Fund Ins. Companies v. Atlantic Richfield Co., 94 Cal. App. 4th 842, 852 (2001).

First, Factory Mutual argues that Northrop had identified similar storm surge as Flood damage after Hurricane Isabel, which occurred in September 2003.[15] However, in response to Factory

[15] At the time of Hurricane Isabel, Northrop and its subsidiary, Newport News Shipbuilding, were insured under Factory Mutual Insurance Company Policy No. UB060, which contained Factory Mutual's Flood definition, identical to the Flood definition in the Excess Policy at issue. (FM Opp'n 14:3-7; Ex. 50 Policy No. UB060.) After Hurricane Isabel, Northrop segregated the damage between wind damage and flood damage. (FM Opp'n 14:8-9; Ex. 32 Eley Depo. 72:1-19, 78:12-79:4; Ex. 45 September 17, 2003 E-Mail String.) Northrop used its own internal guidelines for its accounting system to set up and track work orders and costs wherein flood related damage was defined as damage caused by "rising or surge flood water." (FM Opp'n 14:9-10; Ex. 43 Hurricane Isabel Project Plans & Cash Flow Data; Ex. 32 Eley Depo. 55:1-10 (emphasis omitted).) Thus, Factory Mutual argues, Northrop's internal guidelines demonstrate that Northrop believed "storm surge" was Flood under the same definition used in the Excess Policy, which does not contain the phrase "whether driven by wind or not." That coverage claim, however, evolved at a different site, involved different personnel from those involved in procuring the Excess Policy, and constituted a loss that was well within the sub-limit for Flood coverage and therefore did not raise any of the issues being disputed here. Thus, the events that occurred in connection with Hurricane Isabel are too remote to singlehandedly prove either party's point.

However, the Court does note that the parties' previous dealings are relevant in determining whether Northrop's expectation of coverage was objectively reasonable.

Mutual's arguments, Northrop emphasizes that the Northrop corporate risk management personnel responsible for the purchase of the Excess Policy were not involved in the Hurricane Isabel claim. Thus, Northrop concludes, the assessments procured in the other claim are irrelevant. Moreover, when Factory Mutual adjusted storm surge damage claims from the Pascagoula facility arising out of Hurricane Georges, which occurred in September 1998, Factory Mutual classified the "storm surge" damage under the "wind" peril, not the "flood" peril.[16] (Northrop Reply 18:15-17; RSOF-III ¶ 5.)

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[16] When Hurricane Georges hit the Pascagoula facility at issue here, then owned by Northrop's predecessor Litton, the property was covered under a policy sold by a Factory Mutual company. (Northrop Grumman's Reply Mem. of P. & A. in Further Supp. of its Mot. for Partial Summ. J. "Northrop Reply" 18:18-19:3; RSOF-III ¶¶ 4, 6-7.) The same adjustor Factory Mutual assigned to Northrop's Katrina claim, Chris Roza, was responsible for adjusting Litton's Hurricane Georges claim for Factory Mutual. (Northrop Reply 19:3-5; RSOF-III ¶¶ 8-9.) After Mr. Roza visited the Pascagoula shipyard, he sent a letter to then Litton employee, and subsequent Factory Mutual underwriter Jeff Green, confirming notification of the loss. (Northrop Reply 19:5-7; RSOF-III ¶¶ 10, 14.) In that letter, Mr. Roza stated that "as a result of Hurricane Georges, there was extensive wind and water damage at the facility." (Northrop Reply 19:7-9; RSOF-III ¶¶ 11.) In the document's heading, however, Mr. Roza clearly branded: "LOSS DESCRIPTION: Wind." (Northrop Reply 19:9-10; RSOF-III ¶¶ 12.) Mr. Roza testified that the reference in that letter to "Loss Description" was intended to reference the peril under which Factory Mutual was adjusting the claim, and that although Factory Mutual's practice was to open multiple perils for a given loss, in that instance Factory Mutual decided to adjust the entire claim under the "wind" peril. (Northrop Reply 19:11-14; RSOF-III ¶¶ 30.)

Numerous other documents pertaining to Litton's Hurricane Georges loss state that all such loss, including the "storm surge" loss, were caused by the single peril of "wind." (Northrop Reply 19:14-16; RSOF-III ¶¶ 12, 25.) For example, Mr. Roza's September 28, 1998 and November 19, 1998 internal Factory Mutual claim adjustment memoranda reporting on Northrop's Hurricane Georges claim make clear that despite characterizing the loss as "extensive wind and storm surge damage," Factory Mutual adjusted the claim under the "wind" peril and applied the "Named Storm" deductible. (Northrop Reply 19:17-21; RSOF-III ¶ 25.) Likewise, Mr. Roza sent another letter to Mr. Green dated November 23, 1998 in response to (continued...)

Additionally, Factory Mutual fails to mention that in February 2001, after Hurricane Georges, its loss control engineers conducted an Engineering Risk Assessment of Northrop's properties shortly before Northrop finalized its acquisition of Litton, in order to characterize the types of perils Northrop's facilities reasonably could face. (Northrop Reply 20:3-6; RSOF-III ¶¶ 18-22.) That report included a glossary of terms defined and explained by Factory Mutual. (Northrop Reply 20:6-7; RSOF-III ¶ 18.) Two of the terms were "Flood" and "Wind." (Northrop Reply 20:8; RSOF-III ¶ 19.) Consistent with its description of the Hurricane Georges claim, "storm surge" damage is referenced in the "wind" description. (Northrop Reply 20:8-10; RSOF-III ¶ 20.) Specifically, Factory Mutual notes that wind peril "[s]everity is based on the surrounding topography, exposure to storm surge, and other factors." (Northrop Reply 20:10-12; RSOF-III ¶ 22.) In contrast, Factory Mutual does not reference storm surge when discussing flood. (Northrop Reply 20:12-13; RSOF-III ¶ 21.)

Given the foregoing, it appears that the parties' actions in connection with hurricanes which previously affected the Pascagoula shipyards suggest that the parties have not had a consistent view of whether storm surge is a "wind" or a "flood" event. This inconsistency is further established by policies Factory Mutual previously sold to Northrop and to its predecessor, Litton, that

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[16] (...continued)
Mr. Green's request for an advance payment, in which Mr. Roza again described the loss to its insured as "Wind." (Northrop Reply 19:21-20:2; RSOF-III ¶ 12.) Though these instances did not occur in connection with the 2004-2005 Policy or Hurricane Katrina, Factory Mutual's response after Hurricane Georges may have created an expectation that storm surge was characterized as a "wind," not "flood," event.

expressly excluded coverage for loss caused by storm surge. For example, Factory Mutual Policy No. UA848, which provided all risk property coverage to Litton for the policy period August 1, 2000 to August 1, 2001, specifically excluded "*wind driven storm surge*" as part of the exclusion for "Sturmflut" applicable to certain European locations.[17] (Northrop Mot. 18:19-22; SOF ¶¶ 51, 53.) This policy also included a separate definition for the peril of "flood," further supporting Northrop's argument that it reasonably believed Factory Mutual considered Flood and "storm surge" (or "Sturmflut") as separate and distinct perils. (Northrop Mot. 18:25-19:1; SOF ¶ 54.) Factory Mutual included a similar Sturmflut Exclusion in Policy No. UA726, which covered Northrop from April 1, 1999 to April 1, 2002, and likewise included a separate definition for the peril of "flood." (Northrop Mot. 19 n.5; SOF ¶¶ 55-57.) Thus, Factory Mutual's failure to include this or comparable clarifying language in the Excess Policy, when contrasted with the definite terms used in previous policies, could have created reasonable confusion as to whether the Excess Policy excludes storm surge flooding.

Because the parties' history of dealing does not resolve the ambiguity, the Court turns to the evidence submitted regarding the

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[17] Policy No. UA848 includes a "Sturmflut Exclusion," and defines "Sturmflut" as:

> general and temporary condition of partial or complete inundation of dry land areas caused by or resulting from the overflow of river, lake, bay, estuary or tidal waters because of the rapid accumulation of runoff of surface waters from any source or from wind driven storm surge, tidal wave, high tide, flood tide, wave wash, or tsunami."

(Northrop's Reply Statement of Genuine Issues and Additional Facts in Supp. of Northrop's Mot. for Partial Summ. J. "Northrop SOF" ¶¶ 51, 53.)

process of procuring the insurance policies at issue. A detailed review reveals that neither party was clear about the breadth of the Flood exclusion. Both parties rely on the 2005 Underwriting Detail, a document that AON, Northrop's broker, prepared and submitted to the insurance market in approximately February 2005 in connection with the renewal of Northrop's property insurance. Northrop emphasizes the definition of storm surge included in its Natural Hazard Loss Analysis section:

> Storm Surge - Quickly rising ocean water levels associated with windstorms that can cause widespread flooding at or near coastal areas. Considerable storm surge damage is possible far inland. <u>Storm surge loss estimates are included in our windstorm analyses unless mentioned otherwise.</u>

(Northrop Opp'n 17:27-18:6; CSOF ¶ 56.) Northrop claims this statement memorializes its understanding that storm surge is associated with a wind or windstorm event, rather than a flood event. (Northrop Opp'n 17:23-26.) Factory Mutual, however, emphasizes that the submission specifically requested a sub-limit of "$400 million per occurrence and in the Annual Aggregate as respects Flood." (Factory Mutual Ins. Co.'s Mem. of P. & A. in Supp. of its Mot. for Partial Summ. J. "Factory Mutual Mot." 4:16-17; Ex. 24 2005 Submission.) According to Factory Mutual, this proves Northrop expected the Flood exclusion to encompass all types of flooding - including storm surge damage.

However, while these statements shed light on Northrop's storm surge interpretation and flood sub-limit expectations prior to securing the Primary and Excess Policies, neither confirms that the

Flood definition in the Excess Policy specifically includes, or excludes, storm surge damage. Moreover, there are other terms defined in the Primary Policy that are essential to coverage determinations under the Excess Policy. For example, the term "occurrence" is not defined in the Excess Policy, yet Factory Mutual cannot reasonably deny that the term "occurrence" is necessary to determining coverage under the Excess Policy or that the Primary Policy's definition of that term applies to the Excess Policy. Similarly, Factory Mutual admits that losses caused by the peril of Wind are covered without sub-limit by the Excess Policy, (RSOF-I/UF ¶¶ 44-45), yet Factory Mutual defined that term only in the Primary Policy and did not repeat that definition in the Excess Policy. (Northrop Reply 6:10-13; RSOF-I/UF ¶¶ 24, 36.) Notably, one of Factory Mutual's experts on underwriting issues stated that, at least for certain purposes, adjusting a claim under the Excess Policy would require consideration of the Primary Policy's Named Windstorm definition. (Northrop Reply 6:1-4; RSOF-III ¶ 31.) Given the overlap between the terms used in each policy, it would be inconsistent for the Court to determine that some defined terms in the Primary Policy carry over to the Excess Policy while others do not.

Additionally, Factory Mutual's failure to use available alternative language supports the reasonableness of Northrop's expectation. The Excess Policy's intent to cover loss caused by storm surge is underscored by contrasting the Excess Policy with other insurance policies that Factory Mutual has written that (1) clearly and specifically exclude coverage for loss caused by storm surge; and/or (2) define "flood" to include water events that are

"driven by wind." Factory Mutual's "failure to use available language to exclude certain types of liability gives rise to the inference that the parties intended not to so limit coverage." Fireman's Fund Ins. Companies v. Atlantic Richfield Co., 94 Cal. App. 4th 842, 852 (2001). As the Ninth Circuit has explained:

> The language of the insurance policy is broad, and the onus was on the drafter of the policy to convey any limitations. If [the insurer] desired to limit coverage . . . , it could have expressly done so. Instead, it used broader language . . . . Once again, [the insurer] failed to communicate an asserted limitation conspicuously, plainly and clearly.

Pension Trust Fund for Operating Engineers v. Fed. Ins. Co., 307 F.3d 944, 953 (9th Cir. 2002). Thus, Factory Mutual's use of broad language where more specific terms were available may have given rise to the reasonable inference that Factory Mutual did not intend to exclude wind-driven flood.

Additionally, Factory Mutual's omission of the words "whether driven by wind" in the Excess Policy's Flood Exclusion is significant when compared with its inclusion of those very words in the Primary Policy and in another exclusion in its Excess Policy.[18] Arguably, the terms are used in an exclusion pertaining to "rain,

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[18] Factory Mutual used the words "whether or not driven by wind" in a different exclusion in the Excess Policy, which applies to buildings under construction:

> C. This Policy excludes . . . :
> . . . .
> 7) loss or damage to the interior portion of buildings under construction from rain, sleet or snow, whether or not driven by wind, when the installation of the roof, walls and windows of such buildings has not been completed.

(Northrop Mot. 16:1-7; SOF ¶ 48.)

sleet and snow," in the completely different context of buildings under construction. However, it is notable that Factory Mutual used the terms in one section of the Excess Policy and omitted them in another.

Finally, Factory Mutual argues that Northrop's conduct immediately after Hurricane Katrina proves that Northrop considers storm surge damage as Flood. Factory Mutual cites the reactions of AON and Northrop executives in the direct aftermath of Hurricane Katrina to demonstrate that they in fact interpreted the terms of the policies to exclude storm surge coverage.[19] However, these

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[19] Immediately after Hurricane Katrina, AON representatives Brad Skinner and Robert Hayes reminded Northrop that its insurance program had a $400 million Flood sub-limit. (Factory Mutual Ins. Co.'s App. of Ex. ("FM App.") Ex. 8 Bradley Skinner Dep. 71:9-14; Ex. 9 Hayes Dep. 198:12-16, 199:1-9; Ex. 21 August 30, 2005 E-Mail String; Ex. 26 September 1, 2005 E-Mail String.) Mr. Hayes also sent Northrop senior executive David Strode a copy of a policy declarations page with the notation "Dave: here is the page that limits the flood to $400 million." (FM App. Ex. 9 Hayes Dep. 199:4-9; Ex. 26 September 1, 2-5 E-Mail String.)

On August 31, 2005, Northrop's Director of Risk Management, Dean Reynolds, sent an email to Mr. Strode [Northrop senior executive] stating, in part:

> The size of the loss is unknown but Brad [Skinner of AON] reminded us this afternoon that we have a 400 M sublimit for FLOOD claims and that first report of Katrina's damage indicated significant flood damage from the storm surge at Pascagoula. If this is confirmed, then we must carefully watch the damage allocation between NAMED WINDSTORM and FLOOD.

(FM App. Ex. 16 Reynolds Dep. 174:2-25; Ex. 21 August 30, 2005 E-Mail String.) Northrop's David Strode replied, "[g]iven our exposure to hurrican [sic], I assume the 400M was the max we could buy at a reasonable price or the max period?" (FM App. Ex. 21 August 30, 2005 E-Mail String.)

Factory Mutual insists that these initial reactions are crucial for identifying Northrop's expectations of coverage. (FM App. Ex. 8 Bradley Skinner Dep. 72:9-16; Ex. 25 August 31, 2005 E-Mail String.) However, most of the post-loss statements were made by individuals who were uninvolved with procuring the Excess Policy. (Northrop Opp'n 17:3-5; CSOF ¶¶ 52-54.) Moreover, post-loss admissions are irrelevant because they do not demonstrate the intent of the parties at the time of contracting. National Union, (continued...)

post-loss admissions do not confirm the parties beliefs at the time of contracting. More importantly, while these post-loss admissions demonstrate that Factory Mutual's understanding is at least reasonable, they do not demonstrate that Northrop's understanding is unreasonable. Where a policy exclusion is ambiguous, and the insured's interpretation is at least objectively reasonable, that ambiguity is strictly construed against the insurer and in favor of coverage.

> "[W]e are not required, in deciding the case at bar, to select one 'correct' interpretation from the variety of suggested readings. To affirm the trial courts' decision in favor of claimants, we need not determine that the two interpretations proposed by the insurer are not possible, or even reasonable, interpretations of the clause in question . . . . Instead, even assuming that the insurer's suggestions are reasonable interpretations which would bar recovery by the claimants, we must nonetheless affirm the trial courts' finding of coverage so long as there is any other reasonable interpretation under which recovery would be permitted in the instant cases."

Mackinnon, 31 Cal. 4th at 655 (quoting State Farm Mut. Auto Ins. Co. v. Jacober, 10 Cal. 3d at 202-203). The Court recognizes the

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[19] (...continued)
885 F. Supp. at 207 (sustaining an evidentiary objection where "the documents themselves do not deal with evidence concerning the parties intention in formation of the policy, but rather post-formation dealings between the insured and the carriers," and thus have "dubious relevance"). Therefore, although the statements support Factory Mutual's stance that its interpretation of the Flood exclusion is reasonable, they do not prove that Northrop's expectations are unreasonable.

reasonableness of Factory Mutual's interpretation. However, Factory Mutual cannot prove that its interpretation is the <u>only</u> reasonable interpretation. In order to prevail on a policy exclusion defense, the insurer must prove that "its interpretation is the <u>only</u> reasonable one." <u>MacKinnon</u>, 31 Cal. 4th at 655. Factory Mutual has shown only that there are at least two reasonable interpretations of the Excess Policy - not that Northrop's interpretation is unreasonable.

In sum, after reviewing the evidence - the parties' conduct in connection with Hurricanes Isabel and Georges, the terms of previous policies, the Underwriting Detail for the 2004-2005 Policy, the interdependency of the Primary and Excess Policy definitions, alternative available language, and the post-loss admissions - the Court finds that Northrop's expectation of coverage was reasonable. It appears that both parties had inconsistent understandings of the term "storm surge" and whether it would be characterized as "wind," "flood," or "Named windstorm." There are several ways that Factory Mutual could have unambiguously excluded storm surge damage: it could have drafted a Named Windstorm exclusion; it could have drafted a "storm surge" exclusion similar to the ones it included in other policies it previously sold to Northrop and Litton; it could have defined "Flood" to include "water resulting from a Named Windstorm"; or it could have used the wording of the Primary Policy's Flood definition. Additionally, there is no evidence indicating whether "storm surge" damage was explicitly discussed with regard to the Excess policy or whether the premiums that Northrop paid reflected the insurance market's calculation of the risk of "storm surge"

damage payment. In short, the parties' past dealings do not illuminate or resolve any ambiguity that exists with respect to coverage for storm surge under the Excess Policy. Therefore, in light of the omission of "whether driven by wind or not" in the Excess policy, the inclusion of "Flood" in the definition of "Named Windstorm" under the Primary Policy, and the inconsistent treatment of "storm surge" damage in the parties' prior dealings, the Court holds that Northrop's expectation of coverage was reasonable.

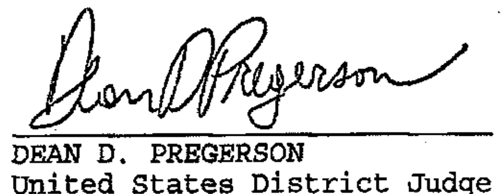
Given Northrop's reasonable expectation of coverage, the Court must construe the ambiguity against the party who caused the uncertainty to exist. As noted earlier, in the insurance context, this party is typically the insurer. Although both parties in this case are sophisticated, and it does not appear that Northrop suffered from a lack of bargaining power, the burden was still on Factory Mutual, as the drafter of the Excess Policy and a provider under the Primary Policy, to state the Flood exclusion unambiguously. The Court finds that it failed to do so, and that, pursuant to the California rules of contract interpretation, judgment must therefore be entered in Northrop's favor.

VII. CONCLUSION

For the foregoing reasons, the Court grants Northrop's motion and denies Factory Mutual's motion.

IT IS SO ORDERED.

Dated: 8-16-07



DEAN D. PREGERSON
United States District Judge