



California Insurance Law Alert

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California Court of Appeal Applies Horizontal Exhaustion Rule In Continuing Damage Case But Also Enforces Anti-Stacking Provision of Carrier's Policies

Summary: The California Supreme Court's seminal Montrose [1] decision held that bodily injury and property damage which is continuous or progressively deteriorating over several policy periods is potentially covered by all policies in effect during those periods.

The Montrose decision raised several corollary questions, two of which were whether all triggered primary policies must exhaust before any excess policy attaches (horizontal exhaustion) and whether the limits of the triggered primary policies stack.

In Kaiser Cement and Gypsum Corp. v. Insurance Company of the State of Pennsylvania, [2] the Second Appellate District of the California Court of Appeal answered both questions. The court held that language in the excess policy providing that the insured's retained limit was equal to the underlying limits "plus the applicable limits of any other collectible underlying insurance," meant that the excess policy required the horizontal exhaustion [3] of all collectible underlying policies.

On the other hand, the Court of Appeal ruled that under the language of the underlying primary carrier's policies, the "each occurrence" limits of the policies did not "stack." In other words, the underlying primary carrier did not have to pay one occurrence limit per year or per policy before its limits exhausted. Accordingly, while all underlying policy limits must exhaust before excess insurance attaches, at the same time, with appropriate language, only one "per occurrence" limit applies *per carrier* despite the number of years that the carrier has coverage.

The Horizontal Exhaustion Issue: Kaiser purchased primary insurance policies (from four different insurers) spanning the period of 1947 through 1987. It also purchased excess policies during many of the same years. Kaiser was sued for asbestos bodily injury claims, and selected its 1974 primary policy, issued by Truck Insurance Exchange ("Truck") to initially respond to all claims that alleged asbestos exposure in that year. The Truck policy limits were \$500,000 per "occurrence", with no annual liability limit. Kaiser and Truck contended that Kaiser's first level excess insurer for the 1974 policy period, Insurance Company of the State of Pennsylvania ("ICSOP"), was responsible to pay claims over \$500,000. ICSOP disagreed, arguing that all of the primary policies issued from 1947 through 1987, including those issued by insurers other than Truck, had to be "stacked" together and exhausted before ICSOP's policy applied.

The Court of Appeal held that under ICSOP's policy language, ICSOP's liability was excess to all other collectible primary insurance – whether in 1974 or in any other year. It agreed with an earlier decision, that horizontal exhaustion is most consistent with the principles of insurance coverage for continuing loss established in Montrose. Accordingly, the ICSOP policy only attaches after all available primary insurance has been exhausted.

[1] Montrose Chemical Corp. v. Admiral Insurance Co., 10 Cal. 4th 645 (1995).

[2] Kaiser Cement and Gypsum Corp. v. Insurance Company of the State of Pennsylvania, 196 Cal. App. 4th 140 (2011).

[3] The question was whether only the collectible primary policies directly underlying an excess policy had to exhaust before the excess coverage applied ("vertical exhaustion"), or whether all of the insured's collectible primary policies, which spanned many years, had to exhaust before the excess coverage applied ("horizontal exhaustion").

The Court of Appeal explained that its conclusion was consistent with, and distinguishable from, Employers Ins. of Wausau v. Granite State Ins. Co., [4] a continuing damage case in which Wausau issued five primary policies and Granite issued five excess policies to the same insured for the same policy periods. There, however, each Wausau policy contained a \$2 million dollar “per year” limit of liability for each “occurrence.” The Wausau court held that “stacking” of primary limits was proper because the policy limits were “per occurrence per year.”

Conclusion: The decision of the Court of Appeal in Kaiser was grounded on policy language, and thus, the language of all triggered primary policies, and the language of the overlaying excess policies, must be examined carefully in order to reach the correct result in a given case.

[4] Employers Ins. Of Wausau v. Granite State Ins. Co., 330 F. 3d 1214 (9th Cir. 2003) (“Wausau”).

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