

California Court of Appeal Decision Increases Options for Many Policyholders to Maximize Coverage at Less Cost for Progressive Injury Losses

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The California Court of Appeal, Second Appellate District, recently issued a decision in *Legacy Vulcan Corp. v. Superior Court of Los Angeles*, 2010 WL 1730788 (Apr. 30, 2010), that makes it easier for policyholders to access coverage under excess liability policies for third-party progressive injury claims. The decision clarifies the law that gives many policyholders more than one option for how to use both primary and excess liability policies to cover claims.

Where progressive injury claims are involved, such as is often the case with environmental contamination property damage claims and bodily injury claims associated with exposure to asbestos or toxic chemicals, the law in many jurisdictions, including California, with respect to third-party general liability policies, is that all policies are triggered that are in effect during each year that the property damage or bodily injury takes place. This is commonly referred to as the “continuous trigger” rule. Many policyholders have excess liability policies to provide coverage for such continuous-trigger and other third-party liability claims when their primary coverage is not sufficient to cover the full extent of their liability. Excess insurance typically provides coverage only upon the exhaustion of specified primary (and sometimes underlying excess) insurance.

The issue of a policyholder’s right to access coverage under its excess policies for progressive injury claims raises the question of whether the policyholder must exhaust all of its primary policies that cover such claims before it is allowed to seek coverage under any of its excess policies (commonly referred to as “horizontal exhaustion”), or whether it may access coverage under an excess policy once the primary policy directly below it—the policy providing primary coverage during the same policy year—is exhausted (commonly referred to as “vertical exhaustion”).

The answer to this question, of course, depends on the specific language of the excess policy regarding when the insurer’s indemnity obligations attach upon exhaustion of the underlying policy or policies. Excess policies have specific provisions, often referred to as “attachment provisions,” that tell the insured what underlying policies or limits of liability must be exhausted or satisfied before the excess policy will begin to provide coverage. For several years, the leading case in California on the “horizontal vs. vertical exhaustion” question has been *Community Redevelopment Agency v. Aetna Cas. & Sur. Co.*, 50 Cal. App. 4th 329 (1996). Insurers have for years argued that *Community Redevelopment* imposes a horizontal exhaustion requirement on insureds under all excess policies, unless the excess policy specifically states that horizontal exhaustion is not required. In other words,

the insurers have argued that courts should read into the attachment provisions of excess policies a presumption that horizontal exhaustion of all primary policies is required before an insured can access coverage under any of its excess policies, unless the excess policies specifically state that horizontal exhaustion is not required, and/or that their coverage attaches upon exhaustion of only the directly underlying primary policy.

In a decision written by Justice Walter Croskey, the *same* justice that authored the decision in *Community Redevelopment*, the California Court of Appeal recently rejected this argument in the *Vulcan* case. The court in *Vulcan* clarified that the attachment provisions of excess policies are to be interpreted in accordance with the same rules of contract interpretation as all policy provisions, without imposing presumptions in favor of a horizontal exhaustion requirement. It held that the undefined, unqualified phrase “underlying insurance” in the attachment provisions of the excess policy at issue in that case was ambiguous (that is, reasonably susceptible to differing interpretations). It therefore had to be construed in accordance with the objectively reasonable expectations of the insured to mean only the directly underlying primary policy.

The effect of the *Vulcan* court’s ruling is that excess policies are not presumed to require horizontal exhaustion of all primary policies before they provide coverage. It follows from the decision in *Vulcan* that unless an excess policy specifically states that it attaches excess of “**all** underlying insurance” or “**all** available primary insurance” (or other similarly broad phrasing), courts should interpret the attachment provisions as requiring only exhaustion of the directly underlying coverage before the insured can seek coverage under the excess policy.

For many policyholders with excess liability coverage, the *Vulcan* decision will make it easier to access that coverage for progressive property damage and/or bodily injury claims once they have exhausted the primary coverage directly beneath the excess policy. Unless the attachment provisions of their excess policies state otherwise, with specific reference to “all underlying” or “all primary” policies, the *Vulcan* decision removes any doubt that these policyholders have the option of using primary policies in multiple years that are triggered by the loss to cover the claim “horizontally,” or to pick a single primary policy and the excess policies in the same year to cover the loss “vertically.”

There are a variety of reasons for an insured to choose the latter option. For instance, in situations where the insured’s primary policies contain deductibles or self-insured retentions (SIRs) that must be paid by the insured before the primary insurers are required to provide coverage, the insured can benefit by choosing the vertical exhaustion option. If the insured is required to “horizontally” exhaust all triggered primary policies before it can access any of its excess coverage, but cannot access its primary policies until it satisfies the SIRs under each primary policy, the insured could end up paying a lot of money out of pocket in the form of multiple SIRs on large progressive injury claims.

However, if the insured has the option of vertically accessing its coverage, it may end up only paying a single SIR, and then be able to call upon its excess insurer for coverage upon exhaustion of a single primary policy. After the *Vulcan* case, the law is clearer that in many cases policyholders have more options to maximize their coverage at less cost for progressive injury losses.

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