EFiled: Feb 28 2014 04:22PM EST
Transaction ID 55074028
Case No. N10C-06-141 FSS CCLD

IN THE SUPERIOR COURT OF THE STATE OF DELAWARE
IN AND FOR NEW CASTLE COUNTY

VIKING PUMP, INC. and WARREN PUMPS, LLC,	)	
Plaintiffs,	)	C.A. No.: 10C-06-141 FSS CCLD
v.	)	**FILED BY UNDER SEAL**
CENTURY INDEMNITY COMPANY, et al.	)	
Defendants.	)	

Submitted: November 15, 2013
Decided: February 28, 2014

Upon Warren's Motion for Supplementation of the October 31, 2013 Opinion* and *Certain Excess Insurers Motion to Clarify the Court's Horizontal Exhaustion Holding

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SILVERMAN, J.

Plaintiffs, Viking Pump, Inc., and Warren Pump, LLC, seek

indemnification and defense costs from Defendants, Plaintiffs' common excess insurers, for thousands of asbestos claims. Through a comprehensive general liability insurance plan originally bought by a common parent company, Houdaille Industries, there is approximately [redacted] in excess insurance at stake.

After eight years of litigation, including a three-week trial, on October 31, 2013, this court decided the parties' post-trial motions, two follow-up motions, and responses. Following the post-trial decisions, Warren filed a Rule 59(e) motion for supplementation of the opinion to address specific policies not discussed in the opinion, and International responded. Separately, Certain Excess Insurers filed a Rule 59(e) motion to clarify the court's horizontal exhaustion holding, to which Warren responded.

I.

The history leading to this complicated litigation has been written.[1] Houdaille Industries, a large industrial conglomerate, briefly owned Plaintiffs, two industrial pump manufacturers of asbestos-containing products.[2] Each year from

[1] *See Viking Pump, Inc. v. Century Indemnity Co.*, C.A. No. 10C-06-141, Silverman, J. (October 31, 2013) (Mem. Op.) ("Opinion"); *Viking Pump, Inc. v. Liberty Mutual Ins. Co.*, 2007 WL 1207107 (Del. Ch. April 2, 2007) (Strine, V.C.) ("*Viking I*"); *Viking Pump, Inc. v. Century Indemnity Co.*, 2 A.3d 76 (Del. Ch. 2009) (Strine, V.C.) ("*Viking II*").

[2] *See* Aff. of John Winsbro, Esquire, in Support of Pltfs.' Motion for Proposed Form of Final Judgment Order After Trial, Ex. 1, Established Facts for Submission to Jury ("Undisputed Facts"), at __ 4 and 16, LexisNexis File & Serve Transaction ID ("Trans. ID") 49239633.

1972 through 1985, Houdaille bought commercial comprehensive general liability insurance ("CGL") in a seamless, layered plan consisting of occurrence-based primary and umbrella insurance from Liberty Mutual and layers of excess insurance above the Liberty policies. In total, Houdaille purchased 35 excess policies through 20 different carriers. Houdaille's 14-year, insurance towers offered $17.5 million in primary coverage, $42 million in umbrella coverage, and [redacted] million in excess coverage.

In 1985, Houdaille divested itself, leaving Viking and Warren independent entities. On October 28, 1987, Warren submitted its first asbestos claim to Liberty. Thus far, approximately [redacted] asbestos claims have been filed against Warren. Viking follows closely with [redacted] claims.

Fearing that Warren was draining its shared insurance, Viking initially filed suit in the Court of Chancery against Liberty, the primary and umbrella carrier, seeking injunctive relief, and Warren intervened. Liberty, Warren, and Viking settled and Liberty was dismissed. At that point, with the primary and umbrella carrier having settled, the excess insurers joined the litigation.

On October 14, 2009, then-Chancellor Strine decided cross-summary judgment motions in Plaintiffs' favor.[3] *Viking II* first held that Viking and Warren are entitled to exercise the rights of an insured under the excess policies. Then,

[3] *Viking II*, 2 A.3d 76 (Del. Ch. 2009) (Strine, V.C.).

Viking II held "all sums" as the proper allocation method, explaining that the alternative "pro-rata" method is inconsistent with the excess policies' language: specifically, the "non-cumulation" and "prior insurance" clauses.[4] Lastly, *Viking II* held that New York's injury-in-fact trigger applies. Together, these rulings mean that for each asbestos claim, all policies within the period triggered by injury are potentially liable for damages associated with that claim.

With no equitable remedy remaining, the Court of Chancery lost jurisdiction and the case was transferred here. In the process, Chancellor Strine lamented the parties' behavior and delay tactics, and observed that the parties had "discovered th[e] case to death."[5] The Chancellor also laid-in a scheduling order meant to clear the way for this court.

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[4] *Id.* at 121 ("Under these clauses, recovery under one policy reduces an insured's recovery from policies in effect in other periods for the same occurrence (*e.g.*, continuous asbestos exposure), and an insurer must pay for injuries caused by that occurrence that continues into other periods. These Non-Cumulation and Prior Insurance Provisions cannot sensibly be applied within a pro-rata allocation scheme.").

[5] *Viking Pump, Inc. v. Century Indemnity Co.*, C.A. No.: 1465-VCS, June 9, 2010 Status Conference Transcript, Strine, V.C., Trans. ID 31611328, 10.

This court attempted to resolve the matter through summary judgment. Ultimately, the parties submitted over 50 briefs, letters, and other supplemental materials regarding the summary judgment motions. The court then declared that "it seem[ed] desirable to inquire thoroughly into [the facts] in order to clarify the application of law to the circumstances."[6] After more motions, and so forth, the case was finally presented to a jury under the untested, yet expedient, presumption that the policies are ambiguous.

The evidence can be categorized into four major topics: exhaustion, defense obligations, trigger, and non-cumulation/prior insurance clauses. Substantially, the jury returned a plaintiffs' verdict. The court acknowledged, however, that "reading each policy closely and without extrinsic evidence, the verdict must be refined to conform to the policies' unambiguous meaning."[7]

Both sides filed post-trial briefs. In deciding the post-trial motions, the court upheld the verdict as to the injury-in-fact trigger, i.e. injury occurs through significant exposure to asbestos fibers even before manifesting itself as diagnosable illness. As discussed more thoroughly below, the court clarified the verdict as to specific Defendants' defense obligations. The opinion also addressed the new legal issue concerning horizontal vs. vertical exhaustion. The court found that horizontal

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[6] Trans. ID 40886580.
[7] Opinion at 46.

exhaustion is New York's law and, therefore, must apply here.

As mentioned, the parties then filed Rule 59(e) motions and responses. Warren filed a motion for supplementation of the opinion to address specific International policies not discussed, and clarify their defense obligations. International responded. Separately, Certain Excess Insurers filed a motion to clarify the court's horizontal exhaustion holding because the opinion was unclear as to which layers of insurance the horizontal exhaustion ruling applied and Warren responded.

II.

In its opinion, the court addressed in detail the parties' arguments as to excess insurers' defense obligations and the language in each policy requiring defense. The court also discussed whether defense costs either eroded or added to policy limits. The court concluded policies were divided into two groups:

> (1) policies SRX1889565, 9601115, CY9502120, CDE0835, CDE1462, ML52652, 06XN243WCA, 06XN194WCA, K25878, UHL0395, UKL0340, UKL0341, UKL0342, and CE5504779 all follow-form, carrying full defense obligations in addition to policy limits; and (2) policies CNZ141951, CNZ141989, CIZ425741, FB000022, 929817, 62790163, OZX11405, ML651258, GC403427, CE5503312, CX5026, K24961, UGL0160, UGL0162, ZCX003889, XCP156562, XCP145194, and 5510143 carry defense obligations within the policy's applicable limits.[8]

[8] Opinion at 80.

Three International policies, however, were inadvertently omitted, prompting Warren's motion here.

Warren seeks clarification as to those policies' obligations. Warren claims that "all of the International Policies contain provisions requiring payment of defense costs in addition to limits." Warren relies on the purportedly unambiguous policy language.

International asserts no supplementation is necessary because the court purposely omitted the three policies as they have no defense obligations. International argues that the policies do not follow-form as to defense obligations, therefore any obligation must come from the policy itself. Further, International claims the policies limit any defense obligation by excepting "the amount and limits of liability."

All three International policies provide full defense obligations in addition to policy limits. Policies 5220113076 and 5220282357 both follow-form by endorsement. The endorsements read:

> Notwithstanding anything contained herein to the contrary, it is understood and agreed that this Insurance covers the same Named Assured and is subject to the same terms, definitions, exclusions and conditions (except as regards the premium and the amount and limits of liability) as are contained in or as may be added to the first layer Umbrella of the Liberty Mutual Insurance Company

Policy No. To Be Advised.

The court previously held that, contrary to International's assertion, the limits of liability exception does not eliminate defense obligations, nor does it force defense obligations within the policy limits. The four endorsements quoted in the opinion all contain nearly identical exceptions and the court held that those endorsements carry full defense obligations in addition to policy limits.

Policy 5220489339 does not include a follow-form endorsement, but the parties agree that defense reimbursement is contemplated by the Loss Expense Endorsement. The Endorsement provides "Loss expense includes ... legal expenses incurred by the Insured with the consent of the company.... Expenses thus paid by the company shall be paid in addition to the limit of liability...." The opinion acknowledged that "consent" has a plain meaning — permission, and it also held,"any insurer that paid costs, but reserved its rights to contest the obligation, has impliedly consented to Plaintiffs' incurring reasonable defense costs." Accordingly, Warren is right, this policy also carries full defense obligations in addition to policy limits.

International argues alternatively that its "Assistance and Cooperation [with] Consent" language in each policy prohibits paying expenses in addition to policy limits without insurer's consent. Because the insurer again invokes the

consent clause, the court must remind the parties of the never-give-an-inch, concede nothing, challenge everything defense played-out over the last six years, and probably from Plaintiffs' first claim. In this case's bloated record, there is no evidence to support a finding that the carriers would consent to pay anything to their insureds. To the contrary, when the insurers' history of adamantly denying coverage is rerun, the notion that the excess insurers would have consented to defense costs verges on silly. Accordingly, all three International policies listed above carry full defense obligations in addition to policy limits.

III.

Defendants' motion concerning horizontal exhaustion is significantly more important and complex. Post-trial, the court applied horizontal exhaustion, which traditionally requires that all underlying primary policies must be exhausted before an excess policy is triggered. In this case's context, exhaustion concerns apportioning damages. Where damages occur over multiple policy periods but there is no scientific way to pinpoint what damage occurred when, the court must determine allocation amongst the triggered policies. Here, as discussed before, "all sums" allocation, a joint-and-several method, applies. The "all sums" ruling answered how a policy must pay, but not when. Following established New York precedent, this court held horizontal exhaustion applies.

The decision, however, was unclear. It first agreed with Defendants that "Plaintiffs must deplete all primary policies, then all umbrella policies, then all first layer excess policies, and so on." But, later it held "the insured must exhaust its primary and umbrella insurance layers before tapping the excess. With the underlying layers gone and the excess triggered, the insured then may choose which excess tower will cover a claim's 'all sums.'" That does not say, however, whether horizontal exhaustion applies to every layer or only the primary and umbrella layers. And, Plaintiff contends there is a meaningful distinction between primary/umbrella and excess coverage, justifying different approaches to exhaustion.

Now, the court will expand its earlier horizontal exhaustion ruling. The court will recap the parties' contentions. Then, as the potential dichotomy has only been squarely addressed by one court, a California trial court, and not in New York, the court will survey exhaustion's competing legal and policy rationales. Lastly, the court will consider how other elements of insurance law affect exhaustion.

A.

As a preliminary matter, Plaintiff argues Defendants' motion should be denied because it seeks relief not previously requested. Actually, both parties argue that the other never previously asserted its position here. The court acknowledges a

Rule 59(e) motion is not for relitigating old matters or raising new arguments.

In this case, however, earlier exhaustion discussions did not focus on whether the excess layers specifically would be horizontally exhausted. Rather, it appears both parties acted under the mistaken assumption that horizontal exhaustion was unambiguous. Or, the issue may have been latent and only now, in attempting to draft the final order as called-for in the opinion, the parties realized the excess layer horizontal exhaustion issue was more significant than previously thought. Regardless, the issues raised by the motion must be addressed.

B.

Defendants argue that when the court ruled horizontal exhaustion applies, it applied to every layer of the insurance tower, not just the primary/umbrella layer(s). Put another way, all first-layer excess policies must be exhausted before any second-layer excess policy is triggered; all second-layer policies must be exhausted before any third-layer policy is triggered, and so on. Defendants quote several cases and insurance treatises. Plaintiff, however, correctly observes that none truly holds that horizontal exhaustion applies to excess layers in subsequent policy periods.

Plaintiff cites little authority, preferring to disassemble Defendants' argument. Plaintiff simply argues this court was clear that horizontal exhaustion

applies only to the primary and umbrella policies, and once those policies are exhausted any excess tower may be triggered.

More specifically, Plaintiff begins by disputing Defendants' characterization of the insurance treatises' explanations of horizontal exhaustion. Rather than "demand[ing] exhaustion of each successive layer," as Defendants' claim, Plaintiff asserts the quoted treatise section "does not cite to *a single case* that recognizes a 'horizontal exhaustion' requirement for excess policies." Conversely, the treatises generally recognize that "while horizontal exhaustion is the general rule for primary policies, excess policies are treated differently."[9] Plaintiff emphasizes that even California, which has the most well-developed horizontal exhaustion law, did not allow excess policy stacking, which Plaintiff equates to rejecting horizontal exhaustion for excess layers.[10] Plaintiff, however, does not cite any case or treatise supporting its theory.

Instead, Plaintiff distinguishes each of Defendants' cases. In most cases Defendants cited, exhaustion was not disputed. One case, *Westport Insurance Corp. v. Appleton Papers Inc.*, explicitly rejects horizontal exhaustion.[11] Even Defendants' strongest case, *Illinois Central Railroad Company v. Accident*

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[9] Jeffrey E. Thomas & Francis J. Mootz, III, New Appleman On Insurance Law § 16.09[3][a][vi] (2012).
[10] *Id.*
[11] *Westport Insurance Corp. v. Appleton Papers Inc.*, 787 N.W.2d 894 (Wis. Ct. App. 2010).

and Casualty Company of Winterthur,[12] merely affirms the trial court's holding that the plaintiff "must first horizontally exhaust its [self-insured retention] for each triggered policy period before looking to coverage from excess insurers."[13]

[12] 739 N.E.2d 1049.
[13] *Id.* at 1054.

In *Illinois Central*, a railroad sought indemnity after settling a class action alleging discriminatory hiring. The railroad had a $1.5 million self-insured retention, followed by $2.5 million in the first layer, and several higher layers. Initially, the trial court found the first layer was not obligated to indemnify because the railroad failed to provide timely notice. Then, the case proceeded against the excess insurers. The trial court ruled on several crucial summary judgment motions, finding a single occurrence triggered every policy in force during the years covered by the class action definitions and allocated damages "horizontally ... using a pro rata time-on-the-risk formula."[14] Rejecting several of the trial court's holdings, such as the number of occurrences, the appeals court nevertheless affirmed.

Defendants make too much of *Illinois Central*. First, as mentioned above, exhaustion was not at issue on appeal. Second, as discussed below, the trial court may have conflated pro rata allocation and horizontal exhaustion. Third, exhaustion was moot in *Illinois Central* once pro rata allocation was applied there. The trial court's first ruling eliminated the first excess layer's indemnity obligations. Paired with the self-insured retention, that ruling meant the railroad was responsible for $4 million for each covered year. Only above that would any higher layer

[14] *Id.* at 1061.

excess policy contribute. Under the trial court's allocation,[15] the highest level of damages allocated to any policy year was only $3.3 million. Accordingly, regardless of the exhaustion method used, no upper layer excess policy was liable.

[15] *Id.*

Defendants' other cases provide even less support. *Westport*, as mentioned, rejected horizontal exhaustion and lamented how it would likely cause additional layers of litigation within and amongst the excess insurers. *North River Insurance Co. v. ACE American Reinsurance Co.* involved a reinsurer's liability following the original insurer's settlement.[16] Plaintiff, a second-layer excess insurer, disputed only the settlement's allocation where pre-settlement analysis identified risk of loss to higher layers. Horizontal exhaustion was applied by private agreement and neither its application generally, nor the manner of application was in dispute. Lastly, *Eagle-Picher Indus., Inc. v. Liberty Mutual Ins. Co.* is a declaratory judgment opinion regarding trigger of coverage.[17] *Eagle-Picher* conclusively states, "The coverage provided by each excess layer goes into effect only if the policy limits of the layer beneath become exhausted."[18] Even so, it offers no explanation about its basis – on policy language, legal standards, or something else.

[16] 361 F.3d 134 (2d Cir. 2004).
[17] 523 F.Supp. 110 (D. Mass. 1981) modified, 682 F.2d 12 (1st Cir. 1982).
[18] *Id.* at 112.

In short, none of Defendants' authorities stands for the proposition that horizontal exhaustion applies to every layer of an insurance tower. But, this does not mean the insurers' position here is wrong. Several cases cited by Defendant suggest an understanding that horizontal exhaustion applies to excess layers. *Westport*, for example, discusses exhausting the first layer excess before the second layer becomes available.[19] Similarly, *North River*, applying it by private agreement, defined horizontal exhaustion as a"rising bathtub," meaning "losses are allocated to the lowest layer of coverage first and, like a bathtub, fill from the bottom layer up. Under that approach, a given layer of coverage is not implicated until the layer beneath it is completely exhausted."[20]

C.

As presented above, neither Plaintiff nor Defendants cite a case deciding whether horizontal exhaustion applies to excess insurance. This appears to be a question of first impression under New York law, which controls this case.[21] Therefore, this court must rule as the New York Court of Appeals would probably rule if presented with this question.[22] One case, albeit a California Superior Court case, has addressed this question squarely. Accordingly, the court will begin by

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[19] *Westport*, 787 N.W.2d at 919.
[20] *North River*, 361 F.3d at 138, n. 6.
[21] *Viking Pump, Inc. v. Century Indem. Co.*, 2 A.3d 76, 89 (Del. Ch. 2009).
[22] *Monsanto Co. v. C.E. Heath Comp. & Liab. Ins. Co.*, 652 A.2d 30, 35 (Del. 1994).

discussing that case before surveying established exhaustion holdings and their rationales to inform its decision whether to follow the California decision.

D.

As presented here, exhaustion is essentially synonymous with priority. As discussed above, it affects apportioning damages. In other words, it concerns the order in which multiple implicated policies are triggered. Horizontal exhaustion generally becomes an issue in a variety of situations. The two most frequently litigated situations involve continuous injury due to asbestos or environmental toxins, and a discrete incident involving multiple parties, such as a construction or automobile accident. The fundamental difference between the situations comes down to whether the implicated policies are concurrent, that is cover the same period, or subsequent, covering multiple policy periods.

Horizontal exhaustion reflects the idea that all triggered primary policies must be exhausted before any excess policy will be triggered. Vertical exhaustion, on the other hand, means that, based on the policy language, an excess policy is considered excess only to the primary policy directly below it. Different jurisdictions, however, apply these concepts differently.

As mentioned, the California Superior Court once grappled with the exact question here: Are excess policies required to be exhausted horizontally where

primary policies must be exhausted horizontally?[23] *Kaiser Aluminum and Chemical Corporation v. Certain Underwriters at Lloyds, London* first established that horizontal exhaustion is the law in California, as discussed in detail below. But, the court noted that the cases establishing horizontal exhaustion as California's rule precisely limit their discussion to the interplay between primary and excess policies on the basis of policy language, such as "other insurance" clauses. *Kaiser Aluminum* found these clauses cannot "reduce the insurer's obligation to the insured but rather only relate to the apportionment of liability among the various insurers" and accordingly cannot form the basis for requiring horizontal exhaustion.[24] The court held the insured "need not horizontally exhaust its [excess] coverage."[25] In the end, horizontal exhaustion was applied to the primary layer, but vertical exhaustion was applied to the excess. While this may superficially seem counterintuitive, it actually makes sense.

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[23] *Kaiser Aluminum and Chem. Corp. v. Certain Underwriters at Lloyds, London*, Cal. Super. Ct. Case No. 312415, Kramer, J. (June 13, 2003) (Mem. Op.), *construed in* Scott M. Seaman & Jason R. Schulze, *Allocation of Losses in Complex Insurance Coverage Claims* app. A (2d ed. 2013).
[24] *Id.* at 6 *citing Dart Industries, Inc. v. Commercial Union Ins. Co.*, 28 Cal. 4th 1059, 1078-80 (2002).
[25] *Id.* at 7.

Several states requiring horizontal exhaustion, besides California, have significant case law, including Illinois and New York. As mentioned, horizontal exhaustion means all triggered primary policies must be exhausted before any excess policy will be triggered. Each jurisdiction applies this concept differently. Further, the logic behind applying horizontal exhaustion has different roots. Some states base their decisions on public policy considerations. Others rely on policy language, specifically "other insurance" clauses and retained limit definitions. Some also rely on broad legal principles. Most relevant jurisdictions have employed all these reasons over the years.

California first applied horizontal exhaustion under the insurance law principle that a "secondary policy, by its own terms, does not apply to cover a loss until the underlying primary insurance has been exhausted. This principle holds true even where there is more underlying primary insurance than contemplated by the terms of the secondary policy."[26] In a continuous harm scenario, California found horizontal exhaustion more consistent with its continuous trigger approach because "if 'occurrences' are continuously occurring throughout a period of time, all of the primary policies in force during that period of time cover these occurrences, and all of them are primary to each of the excess policies."[27]

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[26] *Olympic Ins. Co. v. Employers Surplus Lines Ins. Co.*, 126 Cal. App. 3d 593, 600 (Cal. Ct. App. 1981).
[27] *Stonewall Ins. Co. v. City of Palos Verdes Estates*, 46 Cal. App. 4th 1810, 1853 (Cal. Ct. App. 1996).

California also interpreted policy language to generally support horizontal exhaustion in the absence of specific limiting language. Where a policy's retained limit "is equal to the limits of liability indicated in the schedule of underlying policies, 'plus the applicable limit(s) of *any other underlying insurance* collectible by the Insured,'" "any other underlying insurance" can only mean all available primary coverage, regardless of policy year.[28] *Kaiser Cement & Gypsum Corp. v. Insurance Co. of State of PA* concurred with earlier law that a specific insurance provision could limit the underlying insurance and preclude horizontal exhaustion.[29]

California, in *State v. Continental Insurance Co.*, also recognized that horizontal exhaustion "only governs the relationship between the primary and excess insurers."[30] That is to say it is usually an excess insurer who argues for horizontal exhaustion of the primary policies to limit its own liability. *Continental Insurance* goes on, however, to explain that an insured can also invoke horizontal exhaustion to stack policy limits. While *Continental Insurance* thus considers the insured/excess relationship, it does not discuss whether or how horizontal exhaustion applies to the relationship between excess insurers.

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[28] *Kaiser Cement & Gypsum Corp. v. Ins. Co. of State of PA*, 126 Cal. Rptr. 3d 602, 614 (Cal. Ct. App. 2011) superseded sub nom. *Kaiser Cement & Gypsum Corp. v. Ins. Co. of State*, 264 P.3d 32 (Cal. 2011).
[29] *Id.* at 616-617.
[30] 88 Cal. Rptr. 3d 288, 306 (Cal. Ct. App. 2009) aff'd 281 P.3d 1000 (2012).

Illinois has also firmly adopted horizontal exhaustion.[31] Illinois relied both on policy language and contract law principles. For example, *U.S. Gypsum Co. v. Admiral Insurance Co.* first considered the policy's "other insurance" clause.[32] The policy provided, "If other valid and collectible insurance with any other insurer is available to the insured covering a loss also covered by this Policy, other than insurance that is in excess of insurance afforded by this Policy, the insurance afforded by this Policy shall be in excess of and shall not contribute with such other insurance." *U.S. Gypsum* held that clause "unequivocally sets forth that the excess insurer will not contribute 'if other valid and collectible insurance with any other insurer is available to the insured,'" regardless of whether they extend over multiple policy periods.[33] Illinois subsequently confirmed in several decisions that "other insurance" clauses dictate horizontal exhaustion.[34]

U.S. Gypsum further went-on to reject vertical exhaustion because it would "blur the distinction between primary and excess insurance."[35] The court refused to let a party manipulate the source of its recovery, particularly to prevent bypassing self-insured periods and insolvent insurers. Preventing insureds, especially insureds with self-retentions, from manipulating their insurance programs

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[31] *Kajima Const. Servs., Inc. v. St. Paul Fire & Marine Ins. Co.*, 879 N.E.2d 305, 308 (Ill. 2007).
[32] 643 N.E.2d 1226, 1261 (Ill. Ct. App. 1994).
[33] *Id.* at 1261.
[34] *E.g. Kajima*, 879 N.E.2d at 308; *AAA Disposal Sys., Inc. v. Aetna Cas. & Sur. Co.*, 821 N.E.2d 1278, 1289 (Ill. App. Ct. 2005); *Missouri Pac. R. Co. v. Int'l Ins. Co.*, 679 N.E.2d 801, 804 (Ill. App. Ct. 1997).
[35] *U.S. Gypsum*, 643 N.E. 2d at 1262.

unfairly is a leitmotif in horizontal exhaustion jurisprudence.

In New York, horizontal exhaustion is also the settled rule. For example, *Bovis Land Lease LMB, Inc. v. Great American Insurance Co.* based its adopting horizontal exhaustion on "consideration of the purpose each policy was intended to serve as evidenced by both its stated coverage and the premium paid for it, as well as upon the wording of its provision concerning excess insurance."[36] In *Bovis*, an employee of a subcontractor was killed at the construction site and the subcontractor, general contractor, and construction manager were each insured. After exhausting the subcontractor's primary policy, the parties disagreed as to the other policies' priority. *Bovis* emphasized how the policies' language contemplated sharing or shifting risks. The general contractor's primary policy responded first, and the umbrella policies, which were considered "true excess" policies, responded last but simultaneously because they insured against the same risk. In the middle, the construction manager's CGL policy included an "other insurance" clause seeking to shift the risks, but also included a provision providing its coverage is primary where required by contract.

In addition to policy language considerations discussed above, New York looks to the premiums paid as an indication of the parties' expectations. For

[36] *Bovis Lend Lease LMB, Inc. v. Great Am. Ins. Co.*, 855 N.Y.S.2d 459, 466 (N.Y. App. Div. 2008).

example, where a $10 million excess policy's premium was less than one-third of the $1 million primary's premium, the court found the excess policy "plainly was intended to constitute the final tier of insurance for any liability it would cover, but for any insurance specifically purchased to apply in excess of its limits."[37] A low premium suggests a policy is not primary, but is not conclusive.[38]

[37] *Id.* at 467.
[38] *In re E. 51st St. Crane Collapse Litig.*, 960 N.Y.S.2d 364, 367 (N.Y. App. Div. 2013).

Within the concurrent policy context, New York's horizontal exhaustion rule is well-developed. But, while Illinois and California have expressly applied horizontal exhaustion to continuous injury cases, such as asbestos, New York has not. *In re Liquidation of Midland Ins. Co.*, the only New York case remotely dealing with exhaustion in a continuous trigger context, addressed an excess insurer's obligations during liquidation. The court concluded the "other insurance" policy language was clear and unambiguous and, citing Illinois law, "is broad enough to cover all primary policies, prior and subsequent."[39] Later, however, New York's highest court clarified that "other insurance" clauses only prevent multiple recoveries "when two or more policies provide coverage during the same period," as opposed to successive policies.[40]

2.

Like horizontal exhaustion jurisdictions, states following vertical exhaustion use several rationales. Most jurisdictions rely on contract and insurance law precepts. Thus, Wisconsin, New Jersey, and Texas have all firmly rejected horizontal exhaustion.

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[39] *In re Liquidation of Midland Ins. Co.*, 709 N.Y.S.2d 24, 35 (N.Y. App. Div. 2000) *rev'd* 947 N.E.2d 1174 (N.Y. 2011).
[40] *Consol. Edison Co. of New York, Inc. v. Allstate Ins. Co.*, 774 N.E.2d 687, 694 (N.Y. 2002).

Wisconsin first relies on policy language in rejecting horizontal exhaustion across subsequent policies. Finding horizontal exhaustion was not required by the policies, *Westport Insurance Corp. v. Appleton Papers, Inc.* explained, "The excess insurers wrote their policies based on other policies providing coverage beneath them *in that particular policy year*; the excess policy thus required exhaustion only of the policies below them *in that particular policy year*."[41] Specifically, *Westport* focused on a lack of language dictating the exhaustion of policies issued in years before or after a particular policy.

Westport also pointed out the complexity of litigating and establishing priority and inherent unfairness of horizontal exhaustion where the delineation between the layers changes over the years at issue:[42]

> For example, although the 1978, 1979 and 1980 second level of coverage each were triggered when the $5 million of coverage below was exhausted, under horizontal exhaustion, those policies could not be reached until additional millions of dollars had been paid by first-level policies issued from 1981 through 1985 [with $51 million limits].[43]

Westport found horizontal exhaustion would create windfalls for higher level policies "if more than their attachment point had to be paid before their policies could be reached."[44]

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[41] *Westport Ins. Corp. v. Appleton Papers, Inc.*, 787 N.W.2d 894, 918 (Wis. Ct. App. 2010) (emphasis in original).
[42] *Id.* at 918-919.
[43] *Id.* at 919 n.23
[44] *Id.*

New Jersey took a unique approach to exhaustion, choosing to emphasize efficiency and predictability by establishing an overarching allocation scheme.[45] *Owens-Illinois v. United Insurance Co.*, finding the policy language did not resolve the allocation issue, created its own allocation theory "related to both the time on the risk and the degree of risk assumed."[46] *Owens-Illinois* did not, however, clarify how its proration scheme affected excess insurers.

A New Jersey district court specifically addressed the question of priority between excess carriers. Expressly rejecting horizontal exhaustion, *Chemical Leaman Tank Lines v. Aetna Casualty and Surety Co.* found *Owens-Illinois* called for allocation of damages among policy years without reference to the layers.[47] Although not calling this "vertical exhaustion," *Chemical Leaman* goes on to require the exhaustion of each layer within a given year before the next layer begins to pay.[48] This proration scheme prevents an insured from circumventing periods of self-insurance while respecting the distinction between primary and excess policies.[49]

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[45] *Owens-Illinois, Inc. v. United Ins. Co.*, 650 A.2d 974, 993 (N.J. 1994).
[46] *Id.* at 995.
[47] 978 F.Supp. 589, 605 (D. N.J. 1997).
[48] *Id.*
[49] *Benjamin Moore & Co. v. Aetna Cas. & Sur. Co.*, 843 A.2d 1094, 1103 (N.J. 2004).

This *Chemical Leaman* proration and vertical exhaustion scheme was adopted by New Jersey in *Carter-Wallace, Inc. v. Admiral Insurance Co.*[50] New Jersey's Supreme Court found the scheme promotes efficiency by spreading costs, without maximizing or minimizing any layer's liability, and respecting the primary and excess insurance distinction.[51] Further, it conforms to standard policy language.[52]

Texas first approached exhaustion in *American Physicians Insurance Exchange v. Garcia.*[53] *Garcia* addressed a medical malpractice insurer's obligations where multiple policies were triggered, one per policy year, with multiple insurers. *Garcia* held where multiple policies with different limits were triggered, policy limits could not be combined, or stacked. Rather, "the insured's indemnity limit should be whatever limit applied at the single point in time during the coverage periods of the triggered policies when the insured's limit was highest."[54]

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[50] 712 A.2d 1116 (N.J. 1998).
[51] *Id.* at 1124.
[52] *Id.*
[53] 876 S.W.2d 842 (Tex. 1994).
[54] *Id.* at 855.

Although Texas has not squarely addressed horizontal or vertical exhaustion, a federal district court held Texas would follow vertical exhaustion because horizontal cannot be reconciled with *Garcia*.[55] *LSG Technologiesv. U.S. Fire Insurance Co.* first found horizontal exhaustion would raise the per-occurrence indemnity cap, as prohibited by *Garcia*'s anti-stacking holding. The court then rejected the "other insurance" argument, finding that "other insurance" refers only to policies covering the same risk, such as concurrent policies. Subsequent policies, on the other hand, insure against different risks – different time periods – and "other insurance" clauses do not support horizontal exhaustion.[56] Lastly, the court was persuaded by *Carter Wallace*'s public policy rationale, discussed above.

E.

The spectrum of exhaustion cases also deal with other insurance law issues and often seem to conflate them. Related issues include calculating occurrences and the allocation method. Even when these issues are not conflated with exhaustion, their resolution often affects it. For example, pro rata allocation may moot the exhaustion argument, as in *Illinois Central*. Understanding the interplay between these issues clarifies the case law's limits. Similarly, these collateral issues can obscure the fact and policy reasons guiding and affecting the

[55] *LSG Technologies, Inc. v. U.S. Fire Ins. Co.*, 2010 WL 5646054 (E.D. Tex. 2010).
[56] *Id.* at *12.

exhaustion question.

1.

In continuous loss cases, some courts treat all the claims arising from one cause as one occurrence.[57] Others, like here, treat each claim as a separate occurrence.[58] In the exhaustion context, the number of occurrences matters because many insurance policies have different per-occurrence and aggregate limits. Also, many policies include per-occurrence deductibles. Accordingly, the total coverage available to the insured often requires determining the number of occurrences.

[57] *E.g. Liberty Mut. Ins. Co. v. Treesdale, Inc.*, 418 F.3d 330 (3d Cir. 2005).
[58] *E.g. Metro. Life Ins. Co. v. Aetna Cas. & Sur. Co.*, 765 A.2d 891 (Conn. 2001).

Although it was never a major issue in this case, the parties seem to agree that each asbestos claim is a separate "occurrence" under the policies. Plaintiffs stated in their "Proposed Form of Final Judgment Order After Trial" that they may select any triggered policy to "respond to any asbestos claim." Similarly, Defendants' "Memorandum of Law in Opposition to Plaintiffs' Opening Brief" distinguishes this case from those Plaintiffs' cite, because "none of the cases deal[s] with multiple occurrences." Furthermore, in this case all the excess policies carry the same per-occurrence and aggregate limits, so the amount of coverage is not contingent on the number of occurrences.

2.

The most relevant and commonly muddled exhaustion issue is allocation. Insurers can either be jointly and severally liable for all damages arising from the occurrence under "all sums" allocation, or the damages can be divided pro rata. Several pro rata schemes have been applied, such as by year, by policy limits, and by time on risk. Allocation and exhaustion, however, are different. Allocation controls how a policy pays; exhaustion controls when a policy pays.

The varying treatment of these related issues requires the cases be read closely. Some courts have outright confused allocation and exhaustion.[59] Even

[59] *E.g., Boston Gas Co. v. Century Indem. Co.*, 910 N.E.2d 290, 301 (Mass. 2009) ("This allocation method is variously referred to as 'joint and several,' 'all sums,' 'vertical exhaustion,' and 'vertical spike.'");

where the issues are not muddled, as mentioned, a pro rata ruling may moot the exhaustion argument, like *Illinois Central*. Further, because the reasons supporting horizontal exhaustion and pro rata allocation – and vice versa – are closely related, distilling each case's importance to decidin each specific issue is difficult. Similarly, earlier rulings in the cases that effect the exhaustion question must be identified for complete understanding.

F.

Several earlier holdings in this case also must be recalled, as they affect the outcome now. As discussed above, *Viking II* held "all sums" allocation applies. The post-trial opinion held injury occurs upon cellular and molecular damage and the excess policies' "non-cumulation" and "prior insurance" clauses do not erode the policies' limits. Also, each claim against Plaintiffs constitutes a separate occurrence.

G.

Westport Ins. Corp. v. Appleton Papers Inc., 787 N.W.2d 894, 918 (Wis. Ct. App. 2010) ("Horizontal exhaustion, which is another name for pro rata allocation...").

Taking that landscape and the state of the law into account, the New York high court would hold horizontal exhaustion governs only the primary and umbrella policies here, not the excess coverage. As discussed above, New York emphasizes the policies' purposes as evidenced by their language, premium amounts, and other indicators. New York has also unequivocally held that only policies insuring the same risk should respond simultaneously and that "other insurance" clauses are not relevant in allocating damages to policies over different periods. Accordingly, neither New York law nor the policy language urges, let alone requires, horizontal exhaustion of the excess layers.

Similarly, the premiums are consistent with that result. For example, in the 1984 policy year, the primary policy cost [redacted] per dollar of coverage and the umbrella cost [redacted] per dollar of coverage, while all the excess coverage cost, at most, [redacted] of the umbrella.[60] The premiums seemingly reflect a substantially different risk between the primary, umbrella, and excess policies.

[60] Stipulation Respecting Policies, Ex. 81, 82, 84, & 86-94.

Further, *Kaiser Aluminum* is persuasive. It dealt with a very similar situation: a continuous injury asbestos case with multiple occurrences in a traditionally horizontal exhaustion jurisdiction applying "all sums." *Kaiser Aluminum* found the horizontal exhaustion cases specifically applied to only primary versus excess insurance disputes based on the policies' plain language. Further, like *Consolidated Edison* in New York, *Kaiser Aluminum* found "other insurance" clauses relate only to the apportionment of liability amongst insurers, not to limit an insured's coverage. As in *Kaiser Aluminum*, Defendants here do not demonstrate a legal or policy-based requirement for horizontally exhausting the excess policies.

It is unassailable that horizontal exhaustion is a limitation tending to deny coverage. While that makes sense at a primary/umbrella level where the policies specifically contemplate responding first, this limitation ought not apply to excess. After the insured proves coverage, the insurer has the burden of proof for an exclusion or limitation.[61] As discussed above, *Kaiser Aluminum* properly required the insurer to prove horizontal exhaustion should apply to the excess layers. And, when it failed to do so, the court refused to reduce insurers' "obliga[tion] to indemnify the insured for the entirety of the ensuing damage or injury" by

[61] *Con. Edison*, 774 N.E.2d at 627.

implication.[62] Similarly, here, Defendants have not shown why, having bought insurance, Plaintiff should find itself with less coverage. It is a general tenet of New York law that policies are "construed in favor of finding coverage."[63]

[62] *Kaiser Aluminum*, Cal. Super. Ct. Case No. 312415 at 6 *citing Dart Industries*, 28 Cal. 4th at 1080.
[63] *Olin Corp. v. Certain Underwriters at Lloyd's London*, 468 F.3d 120, 129 (2d Clr. 2006).

If New York's basic approach to exhaustion were similar to New Jersey's, where a definitive legal plan controls exhaustion, or if the premium structure to the policies here were less like those in *Bovis*, the outcome here might be different. But New York's approach to horizontal exhaustion is generally similar to California's. And, *Kaiser Aluminum* squarely and nicely addresses the relationship between excess insurers, like the one here. Accordingly, New York would follow *Kaiser Aluminum*'s reasoning and not require horizontal exhaustion of all policies in each excess layer before triggering on risk, higher layer policies.

Counsel **SHALL** submit a final order after approval as to form.