CALIFORNIA SUPREME COURT ADOPTS "ALL-SUMS-WITH-STACKING" ALLOCATION RULE IN PRO-POLICYHOLDER ENVIRONMENTAL INSURANCE COVERAGE DECISION

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On August 9, the California Supreme Court issued an important decision that will enhance the ability of policyholders to receive the full benefit of their insurance policies for long-tail environmental claims. Specifically, the Court adopted an "all-sums-with-stacking" rule that will allow policyholders to recover from insurers over multiple policy periods, effectively "stacking" their policy limits to maximize potential recovery.

The opinion issued in *The State of California v. Continental Insurance Company* (Case No. S170560, August 9, 2012) ("Continental Ins.") involved California's efforts to seek reimbursement from its insurers for environmental claims at the State's Stringfellow Acid Pits waste site. The site, near the Riverside County community of Jurupa Valley, was historically operated as a waste disposal facility, storing liquid industrial waste in evaporation ponds, primarily from metal finishing, electroplating, and pesticide production. Over time, due to the site's proximity to the groundwater table, fractures in the rock underlying the site, and ineffective design of the containment system, the groundwater became contaminated with various volatile organic compounds, perchlorate, and heavy metals such as cadmium, nickel, chromium, and manganese. Soil in the original disposal area became contaminated with pesticides, polychlorinated biphenyls, sulfates, and heavy metals. The original disposal area is now covered by a clay cap, fenced, and guarded by security services.

Facing huge remediation costs, potentially as high as $700 million, the State filed two lawsuits against its insurance carriers, the second of which included the insurers involved in the recent Supreme Court decision. The trial court held that each insurer was liable for damages under the various policies' "all sums" language, subject to the policies' particular limits, for the total amount of the loss. The trial court did not, however, allow the State to combine, or "stack," successive policy periods to recover more than one policy period's coverage limits. That "anti-stacking" decision left the State with the option of choosing just one policy period to provide coverage, a result

consistent with an earlier decision, *FMC Corp. v. Plaisted & Companies*, 61 Cal.App.4th 1132 (1998) ("FMC"). FMC prevented an insured from stacking multiple consecutive policies in a case in which the insured had caused toxic contamination "over a period of many years." *Id.* at 1142.

The net effect of the trial court's anti-stacking holding was to deny any financial recovery by the State because it had already recovered more in settlements with other insurers than was available to it under any single policy period. On appeal, the Court of Appeal for the Fourth Appellate District, Division Two, agreed that each carrier was liable for the long-tail environmental loss, but disagreed with the trial court's anti-stacking decision, thereby exposing multiple successive policy periods to liability for California's Stringfellow losses. The insurers then appealed to the Supreme Court.

The Supreme Court's analysis began by confirming that the "'continuous injury' trigger of coverage," as that principle was explained in *Montrose Chemical Corp. v. Admiral Ins. Co.*, 10 Cal.4th 645, 655 (1995) ("Montrose") and the "all sums" rule adopted in *Aerojet-General Corp. v. Transport Indemnity Co.*, 17 Cal.4th 38, 55-57 (1997) ("Aerojet") would apply, providing that the insurers had insured the site at some point during the period of loss. The Court explained the nature of long-tail environmental claims, where environmental harm continues over many years and policy periods, make it virtually impossible to identify precisely when harm occurred. If limited to its ability to prove exactly when environmental harm occurred, the Court explained, "an insured who had procured insurance coverage for each year during which a long-tail injury occurred likely would be unable to recover." Continental Ins., at 8. The Court continued, citing a law review article:

> "While CGL policies [such as the ones at issue here] limit coverage to their policy period, the policies . . . require only that some damage occur during the policy period. . . . Unfortunately, CGL policies leave unanswered the crucial question for long-tail injuries: when does a continuous condition become an 'occurrence' for the purposes of [triggering] insurance coverage?" (Bratspies, Splitting the Baby: Apportioning Environmental Liability Among Triggered Insurance Policies (1999) 1999 B.Y.U. L.Rev. 1215, 1228-1229, fn. omitted (Bratspies).)

Id. In light of Montrose's continuous trigger rule, the Court had little difficulty concluding that each policy's coverage obligations had been triggered by the progressive property damage at the Stringfellow site. "The fact that all policies were covering the risk at some point during the property loss is enough to trigger the insurers' indemnity obligation." *Id.* at 11. The Court found each insurer severally, not jointly, liable on its own policy up to its policy limits.

The Court also rejected the insurers' proposed *pro rata* allocation of liability among policy periods. Describing such an allocation methodology as a limitation on the "all sums" rule, the Court explained:

> "This approach emphasizes that part of a long-tail injury will occur outside any particular policy period. Rather than requiring any one policy to cover the entire long-tail loss, [pro rata] allocation instead attempts to produce equity across time." (Bratspies, supra, 1999 B.Y.U.L.Rev. at p 1232.)

Id. at 12. Noting that a *pro rata* form of allocation would assign liability to the insured during periods when it lacked coverage, the Court explained that such a result would be inconsistent with the express language of the carriers' policies, which obligated them to pay "all sums" that the insured became liable to pay for damages due to property damage. Thus, the Court concluded that all the policies were required to pay the State's losses, up to their policy limits, as long as some of the continuous property damage occurred during a given policy period. Such a ruling "best reflects the insurers' indemnity obligation under the respective policies, the insured's expectations, and the true character of the damages that flow from a long-tail injury." *Id.* at 14.

The Court then turned to the important "stacking" question. The State's ability to combine, or "stack," its policy periods to provide coverage for the continuous property damage was vital to its ability to compel the carriers to reimburse its losses. The State had already recovered more than $120 from other insurers for its Stringfellow liabilities. The most it could recover under one policy period was $48 million. Thus, the trial court's anti-stacking decision had left the State with a nominal victory but zero recovery.

As explained by the Court, "'[s]tacking policy limits means that when more than one policy is triggered by an occurrence, each policy can be called upon to respond to the claim up to the full limits of the policy.' (Colon, Pay It Forward: Allocating Defense and Indemnity Costs in Environmental Liability Cases in Cal. (Feb. 2002) 24 Ins. Litig. Rptr. 43, 53.)" *Id.* at 15. The Court then expanded on the practical effect of applying a stacking rule in the context of a long-tail environmental claim:

> The all-sums-with-stacking indemnity principle properly incorporates the Montrose continuous injury trigger of coverage rule and the Aerojet all sums rule, and "effectively stacks the insurance coverage from different policy periods to form one giant 'uber-policy' with a coverage limit equal to the sum of all purchased insurance policies. Instead of treating a long-tail injury as though it occurred in one policy period, this approach treats all the triggered insurance as though it were purchased in one policy period. The [insured] has access to far more insurance than it would ever be entitled to within any one period." (Bratspies, supra, 1999 B.Y.U. L.Rev. at p. 1245.)

Id. The Court wrote approvingly of the Court of Appeal's rejection of FMC, noting that the FMC court's anti-stacking decision "disregarded the policy language entirely." *Id.* at 16. As with the policies in the FMC case, none of the pertinent insurance policies contained anti-stacking provisions and, "absent antistacking provisions, statutes that forbid stacking, or judicial intervention, 'standard policy language permits stacking.'" *Id.* The Court agreed with the Court of Appeal and expressly disapproved FMC's anti-stacking rule.

The Court found that an all-sums-with-stacking rule resolves the question of coverage for long-tail injuries equitably and comports with the parties' reasonable expectations in entering into the insurance contract. The insurers committed to pay all sums for which the insured became liable to pay, up to the policy limits, and the insured receives the full benefit of the bargained-for insurance. The Court also described the rule as "a comparatively uncomplicated calculation" that does not require that the parties or the Court artificially divide the continuous property damage into "distinct periods of injury." *Id.* at 16-17. In future policies, the Court noted, insurers can insert anti-

stacking language, although that certainly provides no relief for policies issued in the 1970s and 1980s, when the State's policies were issued.

The Supreme Court's decision will likely provide far-reaching benefits for policyholders. Armed with the Court's all-sums-with-stacking rule, policyholders will be in a far stronger negotiating position with their carriers as they seek coverage for long-tail claims. The Court's rejection of the carriers' proposed *pro rata* allocation methodology and of FMC's anti-stacking rule eliminates two of the carriers' favored defenses to claims for long-tail environmental claims.

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