A CALIFORNIA CD PRIMER: TRIGGER AND ALLOCATION

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INTRODUCTION

Construction Defect – A Working Definition

A "construction defect" can be defined as a failure of the construction to perform in an intended or expected way. This failure to perform can, but not necessarily, cause physical injury to the work itself and/or other property or work. "Construction defects" include defects in design, faulty work, defective building products/material, and various types of soil failure, and can be characterized as a breach of a contractual obligation or a breach of a duty outside of a contract. They can be discovered as early as during construction and can go undetected for many years until certain symptoms appear.

What is a Construction Defect Claim?

A construction defect claim is a claim for *damages* arising out of a defect in construction, including design, workmanship, and materials. The defect can, but not necessarily, cause *damage* (or physical injury) to the work itself, to other work or property, or to both. The construction defect may cause no *damage* at all but still result in a claim for *damages.*

A defect, while causing no *damage*, can still result in *damages* because the work or product that is defective does not perform at all, or does not perform as it should, causing some kind of monetary loss for which a claim is made. A defect can also cause physical injury or damage to the work itself and to other work or property. (It can also cause bodily injury.)

In either case of damage or no damage, it is common in the construction defect world for the defect and/or damage to manifest (become apparent) or be discovered some time after the initial construction or installation. It remains latent, or hidden, for a time. The distinction between the defective work and its' manifestation is important for a couple of reasons. First, insurance coverage will depend on the type of "trigger of coverage" employed in a specific jurisdiction, i.e. when did the property damage occur?

Second, the distinction between the defect and its manifestation is important with respect to liability and the statutes of limitations and repose. The statute of limitations or repose, in a given state, can be 10, even 15 years, meaning that a lawsuit can be filed up to 10 or 15 years after substantial completion of a project.

A "construction defect" claim, then, typically involves initially latent, long-term problems with construction, including its design, that manifests, or becomes apparent, later and for which damages are claimed. And when the problem manifests in the form of property damage it is typically a continuous and progressive process.

Duty to Defend v. Duty to Indemnify

It is a well-established principle that the duty to defend is broader than the duty to indemnify. It is often touted as being "axiomatic". If there is a reasonable potential for coverage under the policy (with the benefit of the doubt accruing to the insured), there is a duty to defend a *suit*. The duty to indemnify, on the other hand, depends on the insured demonstrating that a loss is actually covered.

The analysis of the duty to defend begins with an examination of the facts and the policy. It is necessary to determine what information an insurer must, or can, review when determining its defense obligation in a particular jurisdiction. Is the examination of the facts limited to those stated in the lawsuit? Or can information extrinsic to the lawsuit be consulted?

While it is universally accepted that the duty to defend is broader than the duty to indemnify, jurisdictions differ as to what information can be used to determine that duty.

For instance, in a "four-corner" or "eight-corner" state, also known as the "complaint rule" or "comparison test"[1], the decision to defend must be based on a review of the policy and the lawsuit. Use of information outside of the complaint is not permitted.

In other states, extrinsic information (extrinsic to the complaint) must be considered. In some cases, this information can be used to defeat coverage as well as afford it. In other cases, the information can be used only to afford coverage.

California requires that the duty to defend must be determined by a comparison between the pleadings and the policy. The analysis does not end here, however. If facts/information extrinsic to complaint indicate a potential for coverage the insurer must defend.

CGL Coverage – Is Faulty Workmanship An Occurrence? Are Construction Defects Property Damage?

The definition of an occurrence in the CGL policy requires that the faulty work be an accident:

> "Occurrence" means an accident, including continuous or repeated exposure to substantially the same general harmful conditions.[2]

Is defective or faulty work an accident for the purpose of this definition? "Accident" is not defined in the policy. An accident can be defined as "an unforeseen and unplanned event or circumstance" or "an unfortunate event resulting especially from carelessness or ignorance" or "an unexpected happening causing loss or injury which is not due to any fault or misconduct on the part of the person injured but for which legal relief may be sought."[3]

Defective work, or faulty workmanship, can qualify as an accident, and therefore an occurrence, if there is property damage to property or work other than that of the insured's and, of course, the consequences were not expected or intended. This is not controversial.

On the other hand, defective work causing direct damage, or damage to the work itself, *may not* be an occurrence, some argue, because such a result should be objectively expected. Also, there may not be an occurrence when the damage is caused to other non-defective work *of the insured*, other than the defective work.

Subcontractor's Work

But suppose the work that is damaged was conducted on the insured's behalf by a subcontractor? If a completed operation, does the subcontractor exception to the Damage to Your Work exclusion matter in the analysis of whether there is an occurrence? Are proponents of the position that damage limited to the work itself is not an occurrence misreading the definition of occurrence and ignoring the very purpose of the Damage To Your Work exclusion and its exception? In other words, do the exclusion and its exception justify the argument that faulty workmanship can be an occurrence in the first instance?

Keep in mind that a policy must be read and interpreted in its entirety. It is persuasively argued that the very existence of the exclusion and its exception nullifies the argument that defective work causing damage to the work itself is not an occurrence. Otherwise, the exclusion would be unnecessary.[4]

The exclusion and its exception follow:

This insurance does not apply to:

l. Damage To Your Work

"Property damage" to "your work" arising out of it or any part of it and included in the "products-completed operations hazard".

This exclusion does not apply if the damaged work or the work out of which the damage arises was performed on your behalf by a subcontractor.

Property damage is defined in the policy as follows:

"Property damage" means:

a. Physical injury to tangible property, including all resulting loss of use of that property. All such loss of use shall be deemed to occur at the time of the physical injury that caused it; or

b. Loss of use of tangible property that is not physically injured. All such loss of use shall be deemed to occur at the time of the "occurrence" that caused it.

In California, defective workmanship causing property damage can be an occurrence. The next step is to determine whether property damage has occurred.

TRIGGER OF COVERAGE

"Trigger" is a term of art used by legal and insurance practitioners that you will not find in the CGL policy. It is a useful term that simply describes how and when coverage is activated. In the CGL occurrence form, property damage must occur during the policy period:

COVERAGE A BODILY INJURY AND PROPERTY DAMAGE LIABILITY

1. Insuring Agreement
…

b. This insurance applies to "bodily injury" and "property damage" only if:

…

(2) The "bodily injury" or "property damage" occurs during the policy period; and…

In the context of insurance claims, most of the time there is no controversy. The cause (occurrence) and effect (property damage) are definite in both time and place, and readily apparent. It is simple to pinpoint when the property damage occurred and it is when the property damage occurs that triggers coverage, not when the work is done, for example, in a construction defect claim.

But in the case of latent (hidden) damage, the effect may not become apparent until sometime after the work is completed so the timing of the property damage is unclear and the controversy begins.

Furthermore, latent property damage can be characterized by a continuous and progressive process (and practically indivisible if there are multiple causes). This is the rule and not the exception in the construction defect claim world. Even experts cannot agree on when property damage occurs.

A coverage analysis begins with the requirement that property damage happen during the policy period as the result of an occurrence. The insured has the burden of demonstrating at least the potential that an occurrence caused property damage during the policy period.

The trigger of coverage analysis includes an examination of the underlying facts and the law in a particular state. Because of the challenge of determining when property damage and bodily injury occur in continuous damage/injury claims, various trigger theories have developed. The impetus for these theories actually preceded the proliferation of construction defect claims. Asbestos and environmental claims provided fertile ground for controversies concerning when injury and damage actually occur, so these trigger theories evolved in an attempt to defuse these controversies.

Brief descriptions of the major trigger theories follow. There are also variations of these theories. But, while useful, these theories are not definitive and do not relieve the claim professional from examining the defect/damage process. Whether a particular trigger theory should apply in the first place depends on the underlying facts and the prevailing case law.

To facilitate an understanding of these theories, our focus is on the insured's work and one identifiable cause, or faulty work. The typical construction project and the claims that arise, however, are not so neat and clean. The insured is frequently not alone on the project so an analysis is complicated by the existence of multiple parties and multiple causes.

The Theories

Before tackling the trigger theories, when analyzing the underlying facts, it is quite useful to create a chronology of construction events. When property damage occurs may not be known exactly, but a good chronology can help narrow down when property damage may have occurred. Specific dates and activities can not only define the parameters of when property damage may have occurred, they can also rule out when property damage definitely did not occur. A chronology generally, however, cannot determine *how much* property damage occurred at a particular point in time, only when property damage may have occurred.

For example, the date of the insured's construction contract, the dates of work, including completion and acceptance dates, the certificate of occupancy date, etc., should generally be available. These dates, and the dates insurance coverage are available to the insured, can aid in the establishment of a chronology that narrows down the triggered periods. The following simple chronology illustrates the point:

Date	Activity/Event
5/1/04	Date of subcontract
8/1/04	Date insured's work completed/accepted
11/1/04	Date of substantial completion
12/1/04	Certificate of Occupancy issued
6/1/05 – 6/1/06	Insurer A policy
6/1/06	Insurer B policy begins
12/1/06	First documented complaints of water intrusion
6/1/07	Insurer B policy ends
6/1/08	Lawsuit filed

Manifestation

The manifestation trigger holds that the policy in effect at the time the property damage becomes apparent, either subjectively or objectively, is activated. A subjective manifestation occurs when the property damage actually becomes apparent and is discovered. On the other hand, an objective manifestation is one in which the property damage should have become apparent and discovered. For example, an inadequately designed foundation on expansive soil, i.e. soil that expands and contracts, will start to fail

before the symptoms become apparent and eventually are discovered. In either case only one policy is triggered.

Exposure

The exposure trigger requires that all policies in effect during the period that the property is exposed to the harmful, damage-causing agent be activated. Consequently, more than one policy can be triggered. For example, in the case of a defective foundation, all policies are triggered from the moment of installation through the period during which the office building is exposed to the defective foundation and is damaged.

Continuous Injury or Damage

The continuous injury trigger, the broadest trigger, begins with the time of the defective work through to when the work manifests or is discovered, and possibly beyond. More than one policy is triggered.

Injury-In-Fact

Injury-in-fact stays true to the policy requirement that only property damage that occurs during the policy period is covered, whether detectable or not. In the context of latent, continuous and progressive damage, more than one policy can be triggered.

When Does a Construction Defect Cause Property Damage?

Until property damage is discovered, has it occurred? A manifestation or discovery jurisdiction would say no.

The CGL policy requires that property damage occur during the policy period. It does not say that the property damage has to be seen, heard, or discovered. So, it must be conceded that property damage can begin before it is discovered or becomes manifest. But what does the law of a particular state say? In other words, while it is easy to conceptualize that property damage can begin the moment of the creation of the defect and continue undetected, it is necessary to determine when the law says the property damage occurred.

One cannot forget logic and common sense, however, when analyzing when property damage occurred. For example, suppose a roof is installed but flashing at the chimney is not. Three months later water damage is discovered. The damage occurred before discovery but did it occur during the entire three months? Suppose it did not rain for the first two months.

Care must be taken to avoid being so mired in theories and legal concepts that logic and common sense are trumped by an automatic, mechanistic approach to coverage for a claim.

Number of Occurrences

Given the nature of latent, progressive, and cumulative injury or damage, and in the context of the definition of occurrence, it is frequently challenging to determine how many occurrences you are dealing with in a construction defect claim, providing a lot of fertile ground for controversy. This is important because the limits of liability and deductibles or self-insured retentions are impacted by the number of occurrences at issue. In addition, more than one occurrence can complicate an already-challenging allocation scheme (among the carriers and potentially the insured with respect to defense cost and indemnity sharing).

The "cause and effect" paradigm is useful, and, in fact, forms the basis of much case law to determine how many occurrences there are in a construction defect claim. But it must be applied with flexibility given the variety of fact situations in construction defect claims.

The "cause test" determines the number of occurrences by focusing on the specific cause of property damage, and not on the number of effects of the cause. A defective roof that is leaking, for example, can cause damage to attic insulation and personal property. Using the "cause test", there is one occurrence. On the other hand, the "effects test" bases the number of occurrences on the number of effects. In our example, the damaged insulation and personal property may constitute two occurrences.

Most jurisdictions look to the cause to determine number of occurrences but what constitutes a particular cause is highly fact-specific and not without controversy, the controversy existing generally in the application of the definition of occurrence to the underlying facts. ("Cause" can mean a couple of things. The *physical cause*, or *cause-in-fact*, with a nearness, or not, in time or space to its effect, is distinguished from the *legal or proximate cause*. We are concerned with the former.)

In the CGL policy, "occurrence" is defined as, "…an accident, including continuous or repeated exposure to substantially the same general harmful conditions." Some questions to consider:

- Are the effects, e.g. property damage, the result of the same or substantially the same conditions?

- Is the exposure of the property to these conditions repeated or continuous, and not unbroken by an intervening cause or causes?

- Are the exposures, while substantially similar, separated by time or distance to such an extent that to conclude that there is one occurrence pushes the envelope of reason?

Furthermore, there is a result-oriented consideration, the result being maximizing coverage:

> The overwhelming majority rule is that the number of occurrences is determined by focusing on the cause or causes of injury and not the effects, such as the claims or injuries. However, application of this rule can produce drastically different results, depending on what the court finds is the underlying cause. Moreover, notwithstanding the general rule, some courts appear to decide their cases in such a way as to maximize coverage. In such instances, where there is a large number of relatively small individual claims and the policy contains a per occurrence deductible that exceeds the amount of the claim, some courts tend to find a single occurrence, to avoid the limiting effect of the deductible. On the other hand, if the case involves per occurrence liability limits, some courts find multiple occurrences.[5]

CGL Coverage – Known Loss and *Montrose*

Our focus is the Supreme Court of California's July 3, 1995 (modified August 31, 1995) ruling in *Montrose Chemical Corporation v. Admiral Insurance Company*, 10 Cal.4th 645. Its impact was, and still is, felt well beyond California's borders.

Montrose significantly impacted the principle of known loss and caused the insurance industry to react with a variety of "Montrose Exclusion" endorsements and the Insurance Services Office[6] changing the insuring agreement in the CGL policy.

A unique feature of construction defect claims (and other long-term exposure or continuous damage claims) is the continuing/progressive dynamic of the property damage beginning at the time or after the faulty work is done and until the defect and/or property damage manifests or is discovered.

Recall that the Insuring Agreement in the CGL policy requires that the occurrence must cause property damage during the policy period. Recall, further, the various "trigger" theories, i.e. manifestation, exposure, continuous, and injury-in-fact. The reason for these theories can be found in the controversy as to when damage occurs in a continuous damage situation.

Known Loss

The concept of fortuity is the cornerstone of insurance and its operation:

> … "fortuity" simply means by chance. A fortuitous circumstance may sometimes be lucky and sometimes will be disastrous, but it will always be unpredictable and by chance. Insurers will usually be successful only if they are writing coverage for fortuitous events.[7]

A fortuitous loss is unpredictable but fortuitous losses can be predicted:

> If an insurer is providing coverage only for random losses, it can make rough actuarial calculations as to the risk of loss based on past claims experience. If it takes advantage of sound underwriting practice through the law of large numbers (the larger the sample, the closer its experience will parallel reality) by writing policies for a large uncorrelated risk pool, the insurer can profit. If the insurer provides coverage for non-fortuitous events, an intended or nonrandom set of losses could ripple through its entire risk pool.[8]

Unless a loss is fortuitous, it is not insurable. Otherwise, those that knew a loss would occur or somehow influence the occurrence would buy insurance and those who knew that a loss would not occur would not buy it. This is the epitome of "adverse selection" and plays havoc with sound actuarial predictions.

It is that simple. Or is it?

Montrose v. Admiral

In July 1995 (modified August 31, 1995), the California's Supreme Court turned the concept of fortuity on its head and compelled the insurance industry to respond with significant policy modifications.

Montrose involved environmental contamination claims and insurance coverage. The Court's rulings cast a wide net that impacted construction defect claims, not only in California but elsewhere as well. The underlying case involved several contamination claims against Montrose, "The Stringfellow cases" and the "The Levin Metals cases".

Stringfellow

The Montrose Chemical Corporation manufactured DDT, dichloro-diphenyl-trichlorethane, a very effective pesticide, at its plant located in Torrance, CA, from 1947

until 1982. In August 1982, the company received a "PRP (potentially responsible party) letter" from the Environmental Protection Agency, followed by a lawsuit, with respect to contamination and response costs at the Stringfellow Acid Pits site.[9] The Admiral policies commenced in October 1982 and expired in March 1986.

> The Stringfellow waste disposal site opened in 1956 and closed in 1972. Chemical wastes generated by Montrose were deposited there between 1968 and 1972, when Montrose paid a hauling company to transport byproducts of its DDT manufacturing process to the state-approved and licensed disposal facility. As early as 1970, toxic wastes were detected seeping from the site, and in 1975 the Santa Ana Regional Water Quality Control Board declared the site a public nuisance... *Montrose* 657
>
> According to the allegations in the CERCLA complaint, the property damage commenced in 1956 and continued throughout the periods when Admiral's CGL policies issued to Montrose were in effect… *Montrose 657*

The following chronology (and Levins Metal Chronology as well) includes the effective dates of the Admiral policies.

1947	Montrose began manufacturing DDT
1956	Stringfellow opened; bodily injury and property damage alleged to have commenced.
1968	Montrose began depositing DDT wastes
1970	Toxic wastes seeping from site detected
1972	Stringfellow closed
1975	Santa Ana RWQCG declared site a public nuisance
1982	Montrose ceased manufacturing DDT; wrongful deaths began
8/31/82	**EPA notified Montrose that it was a PRP**
10/13/82	First Admiral policy commenced
2/82 – 2/83	Concentration of trichloroethylene tripled in groundwater

3/20/83	First Admiral policy expired
3/20/83 – 3/20/86	Subsequent Admiral policies
1986	27 wrongful deaths, between ’82 and ’86, occurred

Levin Metals

The Levin Metals cases involved alleged soil, groundwater, and surface water contamination related to property sold by Parr-Richmond to Levin Metals. The CERCLA claim against Montrose was based on its shipment of DDT to the facility where it was used in the manufacture of chemical products. It was alleged that chemical waste products, include elements of DDT, caused/contributed to the contamination. The Levin Metals chronology follows:

1947	Montrose began manufacturing DDT
Pre- ‘64/’65	Montrose shipped chemicals to Parr Richmond
1964(5)	Chemical processing at Parr Richmond ceased
1981	Parr Richmond sold property to Levin Metals
No later than 8/82	**Contamination discovered**
10/13/82 – 3/20/86	Admiral policies

Beginning in January 1960 through March 1986, seven insurers, including Admiral, provided CGL policies to Montrose.

Trigger

The policies obligated Admiral to cover property damage and bodily injury that occurred during the policy periods.

Explaining the significant difference between the trigger of coverage in property insurance policies (previously ruling in *Prudential-LMI Com. Insurance v. Superior Court* (1990) 51 Cal. 3d 674, that manifestation was the appropriate trigger of coverage) and liability insurance policies, and citing some drafting history, the Court ruled that it is not the cause that determines when a policy is triggered. Rather, it is when the effect, e.g. property damage occurs, that triggers the policy in force at the time. In the case of continuous and progressive property damage or bodily injury, all of the policies in effect at the time the damage or injury occurs are triggered:

> California courts have long recognized that coverage in the context of a liability insurance policy is established at the time the complaining party was actually damaged... *Montrose* 669
>
> The *Remmer*[10] formulation…distinguishes between a wrongful act and the injurious result of that act, and holds that the triggering of liability coverage under a CGL policy is established at the time the complaining third party was actually damaged… *Montrose* 670

Furthermore, in the case of continuous and progressive property damage or bodily injury all of the policies in effect at the time the property damage or bodily injury occurs are triggered:

> *The continuous injury (or multiple) trigger*. Under this trigger of coverage theory, bodily injuries and property damage that are continuous or progressively deteriorating throughout successive policy periods are covered by all policies in effect during those periods. The timing of the accident, event, or conditions *causing* the bodily injury or property damage, e.g., an insured's negligent act, is largely immaterial to establishing coverage; it can occur before or during the policy period. Neither is the date of discovery of the damage or injury controlling: it might or might not be contemporaneous with the causal event. It is only the *effect*--the occurrence of bodily injury or property damage during the policy period, resulting from a sudden accidental event or the "continuous or repeated exposure to conditions"--that triggers potential liability coverage… *Montrose* 675
>
> …
>
> We therefore conclude that the continuous injury trigger of coverage should be applied to the underlying third party claims of conditions or progressively deteriorating damage or injury alleged to have occurred during Admiral's policy periods. Where…successive CGL policy periods are implicated, bodily injury and property damage which is continuous or progressively deteriorating throughout several policy periods is potentially covered by all policies in effect during those periods.[11] *Montrose* 689

Loss-in-Progress

A continuous trigger was applied in the case, and the issue was the termination of the trigger period. Given the dates of operations, the termination of which occurred before the first Admiral policy, and the manifestation of the contamination occurring before the Admiral policy (certainly no later than Montrose's receipt of the PRP letter) it seemed reasonable that any trigger period should not extend beyond the date of the PRP letter. At that point the loss became known and was not insurable.

But the Court disagreed:

> **According to Admiral, Montrose's knowledge of the problems at the Stringfellow site defeats coverage. In particular, Admiral points to the fact of Montrose's receipt of the PRP letter from the EPA on August 31, 1982, prior to the inception of the first of Admiral's four successive CGL policies issued to Montrose. Admiral misses the point. The PRP notice is just what its name suggests--notice that the EPA considered Montrose a "potentially" responsible party.** While it may be true that an action to recover cleanup costs was inevitable as of that date, Montrose's liability in that action was not a certainty**.** There was still a contingency, and the fact that Montrose knew it was more probable than not that it would be sued (successfully or otherwise) is not enough to defeat the potential of coverage (and, consequently, the duty to defend).[12] **(Emphasis added)** *Montrose* 690

Citing the "loss-in-progress rule as codified in sections 22 and 250", the Court posited that the loss in question in a liability policy is legal liability and that known liability is not insurable. When liability is known occurs when liability is "established" with certainty.

> We therefore hold that, in the context of continuous or progressively deteriorating property damage or bodily injury insurable under a third party CGL policy, as long as there remains uncertainty about damage or injury that may occur during the policy period and the imposition of liability upon the insured, and no legal obligation to pay third party claims has been established, there is a potentially insurable risk within the meaning of sections 22 and 250 for which coverage may be sought. Stated differently, the loss-in-progress rule will not defeat coverage for a claimed loss where it had yet to be established, at the time the insurer

> entered into the contract of insurance with the policyholder, that the insured had a legal obligation to pay damages to a third party in connection with a loss.
>
> Montrose's receipt of the PRP letter prior to its purchase of Admiral's policies did not establish any legal obligation to pay damages or cleanup costs in connection with the contamination at the Stringfellow site, such as would implicate the loss-in-progress rule and preclude Montrose from seeking to obtain the liability coverage sought. The PRP letter did no more than formally place Montrose on notice of the government's asserted position and initiate proceedings that could result in subsequent findings and orders. *Montrose* 693

California's Insurance Code, Sections 22 and 250, states:

> 22. Insurance is a contract whereby one undertakes to indemnify another against loss, damage, or liability arising from a **contingent or unknown event**.[13]
>
> 250. Except as provided in this article, any **contingent or unknown event,** whether past or future, which may damnify a person having an insurable interest, or create a liability against him, may be insured against, subject to the provisions of this code.[14]
>
> (Emphasis added)

The Court pushed the envelope in its interpretation of what constitutes a contingent or unknown event in the context of liability.[15] Arguably, the Court could be accused of judicial activism in the sense that it appears to have rewritten California's insurance code, amounting to the corruption of a fundamental requirement in insurance that losses must be fortuitous in order to be insurable. The lack of insurance coverage for environmental contamination losses in California undoubtedly would put a tremendous strain on its taxpayers who would have to shoulder the burden of paying the response costs, absent any outside assistance from others, like the federal government.

The Court concedes that "an action to recover cleanup costs was inevitable" at the time Montrose received the PRP letter, yet defines the contingency underlying the fortuity principle only in the context of a finding of legal liability and not the happening of the event, i.e. Montrose's receipt of the PRP letter.

The insurance policies at issue provide coverage for damages the policyholder is *legally obligated to pay.* If the analysis were to stop here, one could understand the Court's depiction of the contingency that underlies fortuity and insurability as the finding of liability. However, the analysis cannot stop here. In addition to coverage for the legal liability of the insured to pay damages, the policy also provides another vital type of coverage, and that is defense. The insurer's obligation to defend *does not* depend on a finding of legal liability. Rather, it is "triggered" when there is a *potential* that an insured can be found legally liable, and the defense obligation commences when a suit, or its equivalent, is served upon the insured.

So, if an *action* to recover cleanup costs was inevitable and defense expenses are covered regardless of a finding of liability, shouldn't the contingency requirement apply to defense coverage as well? In other words, Montrose received a PRP letter prior to the inception of the Admiral policy. With respect to defense coverage, there was no longer a contingency. The obligation to defend existed prior to a finding of liability, i.e. at the time Montrose received the PRP letter which, again, occurred prior to the inception of the Admiral policy.

CA Ins. Code, § 22, defines "insurance" as a "contract whereby one undertakes to indemnify another against loss, damage, or liability arising from a contingent or unknown *event***."** CA *Ins. Code, § 250*, provides that "any contingent or unknown *event*, whether past or future, which *may damnify* a person having an insurable interest, or create a liability against him, may be insured against, subject to the provisions of this code."[16] (emphasis added)

The *Montrose* Court rewrote the law by restricting, in a liability policy, the contingent or unknown event to a finding of legal liability, despite the fact that insurance defense coverage is triggered long before a finding of liability. The subject of the codes, the event, is the receipt by Montrose of the PRP letter. This is what has to be contingent or unknown on the date of the inception of the policy in order for it to be insurable.

In an arguably inconsistent penultimate paragraph, the Court also commented that "factual questions remain surrounding the circumstance of Montrose's receipt of the PRP letter and its alleged failure to advise Admiral of the same. An insured must make all required disclosures at the time it applies for coverage; the fact that the loss-in-progress rule does not defeat coverage does not itself obviate the possibility of a finding of fraudulent concealment." *Montrose* 694 Fraudulent concealment of a potential in California can be grounds for rescinding a policy, but does not constitute a known loss because legal liability has not been established, notwithstanding that an event, otherwise triggering a duty to defend, occurred prior to the inception of the policy.

"*Montrose* Exclusions"

The Court cast its net broadly and brought construction defect claims within its decision by nullifying the previously applied manifestation trigger in such claims. The industry first reacted with a variety of so-called "*Montrose* exclusions" and ISO subsequently amended

the insuring agreement in the CGL policy. The manuscripted exclusions varied but the common thrust was that losses in progress (known and, sometimes, unknown) were not covered.

ISO modified the insuring agreement to preclude coverage for known losses and was less draconian than the "known and unknown" version of the "*Montrose* exclusions." As to the former, the burden is on the insured to demonstrate that the loss was not known. On the other hand, in the case of the exclusion the insurer has the burden to demonstrate that the loss is excluded.

The intent of the "*Montrose* exclusions" was simply to limit coverage in the case of one occurrence to the first policy during which the property damage or bodily injury first began.

Neither the manuscripted exclusions nor the ISO modification are a "one size fits all" remedy to the *Montrose* Court's corruption of the fundamental insurance principles of fortuity and known loss. Application of either requires a (very) fact-intensive analysis within the context of the duty to defend ("potential" criterion) versus the duty to indemnify ("actual" criterion), and the differences between them.

Some factors to consider:

- What are the underlying facts? What is the insured's role in the cause of the injury or damage?

- Bodily injury or property damage? What is the injury or damage process? For example, the injury process of asbestos is different than the damage process of construction defects.

- What is the trigger of coverage? Continuous, exposure, injury-in fact, and their variations?

- Number of occurrences? Is it the cause or the effect that determines the number of occurrences? Are there additional factors that impact a cause application, i.e. timing of the injury or damage, number of products, trades, homes, claimants, etc.?

- Are there multiple effects of the same cause or are the effects the same? Does the "sameness test" impact the number of occurrences even if there is a single cause and the loss occurred in a "cause state"? For example, water infiltration due to one defect that causes damage to wood and growth of mold…one occurrence or two?

- While injury or damage may precede the policy inception did the insured's product or work contribute to the existing injury after policy inception?

CGL COVERAGE
OTHER INSURANCE AND ALLOCATION

Allocation

How indemnity or expense is to be allocated depends on the jurisdiction, the policy, the characteristics of the damage, and its cause.

Allocation in continuous damage claims refers to the process of allocating indemnity and expense to more than one "period" of time, generally corresponding to insured policy periods, or uninsured periods. This could involve one insurer with more than one policy in play, more than one insurer, or the insured that is uninsured ("bare") or self-insured for a part of the time in question.

Part of the difficulty in allocation is the variety of approaches that exist, and can be particularly frustrating in a jurisdiction where there is no definitive authority to rely upon.

Continuous Damage Claims

A dichotomy exits between damage that occurs over a long period of time and that remains hidden, along with its cause, and visible damage that can be traced to a specific cause at a single, identifiable point in time.

For example, a "slip and fall" in a supermarket is specific as to time and place, including both the cause, e.g. a discarded banana peel on the floor, and the effect, or injury. It is, therefore, fairly easy to identify the liability insurance policy that should respond. Not so in continuous damage claims.

In continuous damage claims, damage occurs over an extended period of time and, for our purpose, over more than one policy period, insured and uninsured. Latent, continuous, and progressive injury or damage claims can trigger or activate more than one policy. For example, in a construction defect claim it may be alleged that the foundation in a building was defectively designed and/or constructed. The defect exists from the moment of construction. However, a failure in the foundation may cause property damage at any time from the initial installation through the first perceptible symptoms of the failure, such as significant cracking in a basement wall, and thereafter.

Continuous damage claims typically include environmental claims involving damage caused by contamination, and toxic tort claims arising out of exposure to asbestos, silica, latex gloves, lead, benzene, and other toxins. Construction defect claims, as we have seen, also fit squarely within the reach of continuous damage claims. Such claims encompass

premises and operations, and products and completed operations hazards that are covered by the CGL policy.

But not all continuous damage claims are created equal so different creative and convenient theories have developed to determine not only when the damage occurs, to satisfy the insuring agreement provisions and the definitions of property damage, bodily injury, and occurrence in the CGL policy, but also to allocate or apportion financial responsibility in an equitable manner. Not only are different theories found among the states, but also which theory is applied in a given state is fact-sensitive and depends on the characteristics of the underlying cause and damage.

For example, pollution claims, because of the long-term and hidden nature of the damage, are conducive to a continuous trigger, pro-rata allocation approach, which will be explained later. The premise is that because it is virtually impossible to determine when damage occurred, to assume that it occurred continuously and in equal amounts over a period of time is not unreasonable.

Concurrent v. Continuous Other Insurance

Our focus is on the allocation of defense costs and indemnity payments related to continuous damage claims to multiple periods involving multiple policies or uninsured periods…a "continuous other insurance" approach. In other words, at issue is the availability of more than one policy to a loss resulting in property damage or bodily injury over an extended period of time.

In contrast, a "concurrent other insurance" situation refers to the availability of more than one policy in the same policy period. In this instance, allocation generally depends on the policies' other insurance clauses that contains specific rules and formulas.[17] (A fertile source of controversy is the priority of coverage between the other insurance clauses of an GC-additional insured's policy and that of the subcontractor-named insured's policy.)

The importance for such a differentiation between continuous and concurrent situations is demonstrated by the Supreme Court of Utah in *Ohio Cas. Ins. Co. v. Unigard Ins. Co*., 2012 UT1 (Utah 2012). The Court took on the question of whether defense costs should be allocated between two carriers according to the parameters set forth in their respective other insurance conditions, or whether the calculation should be based on an equitable time-on-risk approach.

The Court differentiated successive insurers from concurrent insurers, ruling that in the case of successive insurers, the other insurance clause and its formulae are not applicable: "Courts have recognized that the 'other insurance' clauses 'serve to prevent multiple recoveries' when 'two or more policies provide coverage ***during the same period***.'" (emphasis added) *Ohio Cas. Ins. Co.* P19

In continuous other insurance situations, issues concerning equity generally come into play (but that is not to say that the other insurance condition in a policy is never included in the analysis). Like the trigger of coverage, various allocation methods are in use throughout the U.S. Determining the appropriate allocation is fact-sensitive.

It is important to differentiate concurrent from continuous loss scenarios.

Underlying Concepts

Duty to Defend v. Duty to Indemnify

First, recall that the duty to defend is broader than the duty to indemnify. If there is a reasonable potential for coverage under the policy (the benefit of the doubt accrues to the insured), there is a duty to defend a suit. In many instances, particularly continuous damage claims, the duty to defend is more valuable than the duty to indemnify. Defense costs can be enormous because of the complexity of the claim. While indemnity is subject to limits, supplementary payments, which include defense expenses, typically have no limit, terminating only when the indemnity limit is paid.

The duty to indemnify, on the other hand, requires more than just a potential for coverage. There has to be actual coverage for the loss. In other words, it must be demonstrated that the loss is *actually* covered, not just *potentially* covered.

Defense and indemnity, as we shall see, may be treated differently as to allocation.

It is important to distinguish the duty to defend from the duty to indemnify.

Trigger of Coverage

There would be no need for a discussion of allocation in continuous damage claims if multi-triggered policy approaches did not exist and only one policy was activated for these loss situations.

Recall that in the CGL occurrence-based form property damage or bodily injury must occur during the policy period, as explained in the Insuring Agreement. (Contrast this with the claims-made policy wherein the activating event is when the claim is first made subject to a retroactive date, which is the date on or after which the property damage or bodily injury must occur.)

In construction defect claims, the damage and defects are routinely initially latent and are characterized by continuous and progressive process. And there can be multiple defects

and multiple types of damage. Building foundation failures causing damage to the structures, contamination of underground water due to leaking underground storage tanks, damage to copper pipes and electrical wiring caused by tainted drywall from China, and exposure to benzene-containing products causing disease are just a few examples.

Because of the challenge in determining when property damage or bodily injury occurs in continuous damage situations, various trigger theories, previously discussed, have developed. Major theories include manifestation or discovery, exposure, continuous trigger, and injury-in-fact.

It is important to determine the appropriate trigger of coverage.

Known Loss

Recall our discussion of "known loss" and the impact of the *Montrose* case. In that case, California's Supreme Court determined that a loss is insurable until legal liability is established. When that happens remains to be seen but it is arguable that legal liability is established when there is a verdict. It can be further argued, then, that the triggered period of coverage continues beyond the filing of the lawsuit.

It is important to determine when the trigger period begins and ends.

Number of Occurrences

Given the nature of latent, progressive, and cumulative injury or damage, and within the context of the definition of occurrence, it is frequently challenging to determine how many occurrences you are dealing with in a continuous damage claim. Recall the discussion of number of occurrences in a previous chapter.

This determination is important because the limits of liability and deductibles or self-insured retentions are impacted by the number of occurrences. In addition, more than one occurrence can complicate an already-challenging allocation scheme (among the carriers and potentially the insured with respect to defense cost- and indemnity- sharing).

Recall that most jurisdictions look to the cause to determine number of occurrences, but what constitutes a particular cause is highly fact-specific.

Suppose that hazardous substances are migrating from a landfill to adjoining properties and into groundwater, and this has been occurring for 30 years. Suppose further that the migration has been intermittent, and at its most intense during periods of heavy rainfall. Recall that occurrence means "…an accident, including continuous or repeated exposure to substantially the same general harmful conditions". Does an interruption in the

migration constitute the end of one occurrence and the beginning of another? Are the heavy rainfalls intervening causes or superseding causes and, therefore, new occurrences? What about the contamination to the groundwater and contamination to neighboring property? Is each the result of the same or substantially the same conditions, or different conditions?

The point is that while the cause determines the number of occurrences in a particular jurisdiction, the following question must also be addressed: are the effects, e.g. property damage, the result of the same or substantially the same conditions? Is the exposure of the property to these conditions repeated or continuous, and not unbroken by an intervening or superseding cause or causes? Are the exposures, while substantially similar, separated by time or distance to such an extent that to conclude that there is one occurrence pushes the envelope of reason?

It is important to determine whether you are dealing with one occurrence or multiple occurrences.

Allocation Law and Methodology

How are indemnity and defense allocated among several parties, insurers and insured, in continuous damage claims?

Here are some key questions to consider:

- What multi-trigger theory applies? Exposure? Continuous? Injury-in-fact?
- When does the triggered period begin and end? First exposure to manifestation? Diagnosis date? Filing of lawsuit? Date liability is established?
- How many occurrences are there? Is it the cause or effect that determines the number? If the former, are there intervening or superseding causes?
- Does allocation differ between the duty to defend and the duty to indemnify?
- Does the amount allocated to a party depend on its position in the coverage continuum? For example, does an insurer at the beginning of the continuum have more exposure than an insurer at the end of the continuum?[18]
- How are indemnity and/or defense allocated to insurers participating on a named insured and additional insured basis?
- Does the other insurance clause in a policy apply, or is allocation a matter of equity? Is there a different basis for allocating among continuous period policies as opposed to concurrent policies?

- Does allocation depend on the extent of coverage available in a particular year, including excess coverage?

- How do vertical and horizontal exhaustion fit in? In other words, in a multi-trigger approach does an excess carrier participate when the direct underlying insurer exhausts (vertical) or only when all underlying insurance in every period exhausts (horizontal)?

- How are deductibles handled? Self-insured retentions?

- Does the insured participate in bare years? Does the reason for lack of insurance matter? Is the insured's participation different as between indemnity cost-sharing and defense cost-sharing?

- How is allocation calculated when a claims-made policy is involved with occurrence-based policies?

- Can the limits in triggered policies be stacked, i.e. added together in a continuous loss? Can deductibles and/or SIRs be stacked?

The Approaches

> Allocation among consecutive insurers allows courts to be creative because most policies, being contracts between insurers and policyholders, seldom specify the rights of nonparties (other than through limited "other insurance" clauses…). This issue has recently been reduced to a struggle between variations of the "pro rata" allocation method and the "joint-and-several" approach. According to a recent nationwide survey of all American jurisdictions to have addressed the issue, fifteen states have adopted the pro rata (or "horizontal exhaustion") allocation theory, while eight states have adopted the rival "joint and several" allocation theory.[19]

Joint and Several [20]

Also known as the "All Sums" approach, the premise is that a carrier's obligation is joint and several if its policy is triggered. In other words, the insuring agreement obligates the insurer to respond in full if the policy is triggered. ("All sums" has since been replaced by "those sums" in the CGL Insuring Agreement.)

> The rationale behind this approach is that each policy promises indemnification to the insured for *"all sums"* for which the insured is legally obligated to pay as damages. Further, this method comports with the insured's reasonable expectations in purchasing insurance: "that it was covered for all future liability, except liability for injuries of which [the insured] could have been aware prior to its purchase of insurance." *Keene* 1044.[21]

Pro Rata

Conversely, the pro rata approach recognizes that the insurer should only be responsible for the damage occurring during its policy period. Which approach is preferred depends on one's perspective:

> Insurers prefer pro rata allocation because it limits their responsibility to only liability incurred during their policy period, above all applicable deductibles. However, some courts have applied joint-and-several allocation instead. This method allows policyholders to select one particular insurer on the risk and hold it liable for the entire loss up to the limits of that insurer's policy limits. The insurer "elected" by the insured then has the burden of collecting contribution from other insurers on the risk. Policyholders prefer joint-and-several allocation because it gives them control, allows less finger-pointing among potentially liable insurers, and permits an insured to avoid problematic terms in one insurer's policy (e.g., exclusions, conditions, and especially deductibles) by relying in full on another insurer's nonproblematic policy.[22]

The difficulty in determining when property damage occurs and how and what to allocate to a specific period does not trump the need or the ability to at least stay loyal to the policy requirement that property damage must occur during the policy period and that an insurer should only be responsible for the damage that occurs during its policy period.

Methodology

Generally the approach, i.e. pro-rata or joint and several, will determine which method of calculation is used and whether the insured will participate in bare years, or years for which coverage was not available.

Should the insured contribute in years that it has no insurance, either in part or total? For example, the insured's policy may not afford coverage, or perhaps the limits are exhausted. The insurance carrier may be insolvent. Or the insured carries a self-insured retention.

> The most significant difference between joint-and-several and pro rata allocation variations is the treatment of uninsured time periods. If joint-and-several allocation is used, the insured can escape some or all liability by forcing an insurer to pay the entire loss. If pro rata allocation is used (especially strict "time on the risk" allocation), the insured could be left exposed for the proportion of liability incurred during uninsured periods.[23]

Equal Shares

The joint and several approach is conducive to an equal share allocation among insurers whose policies are triggered, without any contribution from the insured in bare years. Many practitioners interpret Equal Shares to mean that each carrier must share on an equal basis regardless of the number of policies in play. For example, Insurer A has nine policies, Insurer B, one. Equal Shares is interpreted to mean that each carrier shares on a 50% basis, i.e. two carriers, two shares.

The better approach is that the basis for equal shares is still preserved if each *policy* shares on an equal basis. In other words, Insurer A has an equal share times nine and Insurer B has an equal share times one, or 90% and 10% respectively.

Time-On-Risk

This approach requires that the specific policy period be compared to the total triggered period of time, and the loss is then shared based on the proportion of the specified period compared to the total period. In this approach, the insured is responsible for bare years, i.e. years for which insurance was not applicable. It is important to determine whether the lack of insurance is voluntary, for example, the policyholder decided to self-insure, or involuntary, for example, the carrier goes bankrupt, and whether the jurisdiction permits allocation to the insured in either instance. Furthermore, defense and indemnity may be treated differently.

> Several courts also have applied pro rata allocation to defense costs as well as to indemnity payments. The contractual language provides less support for pro rata allocation of defense costs because, whereas insurers promise to indemnify for "bodily injury" or "property

> damage" that occurs within their policy period, the duty to defend is broader and (under the law of almost all states) applies to noncovered claims if covered claims also are raised. Nevertheless, it has been seen as more equitable to enforce sharing of this cost as well.[24]

Time-On-Risk Times Limits

Some courts may include the amount of limits available in the time on risk allocation, the premise being that there is a greater assumption of liability by the policy with higher limits. While this can be justified in a concurrent loss situation (as provided for in the other insurance condition in the policy), in a continuous loss case such an approach fails to recognize the fundamental premise that it is damage, and the amount of such damage, that occurs during the policy period that is covered or potentially covered for which the insurer should pay. The limits are relevant only to the extent that the amount of damage that is covered is finite. To include limits as a factor creates the inequitable result of one insurer paying more than another when their time on risk is the same, and the damage is assumed to have occurred equally over a specified period of time.

Other Methods

Another method, "Flexible" or "Weighted" Pro Rata Allocation, recognizes that there may be other factors that require a non-linear approach to when damage occurs. In other words, it may be reasonable to assert that property damage occurred in different amounts at different times.[25] This approach recognizes that these cases are very fact-sensitive and the differences in facts must be taken into account to achieve an equitable apportionment. A landfill, for example, may be experiencing a steady, slow migration of pollutants onto adjoining property except at times of unusually heavy rainfall when the amount of contamination accelerates.

The Tier Approach, often used in construction defect claims, is to allocate defense and indemnity based on the extent to which a particular trade has contributed or is alleged to have contributed to the loss. For example, a roofer may be judged to be 20% responsible/potentially responsible and, therefore, should pay 20% of the defense and/or indemnity. This 20% share then would be further shared by the roofer's insurers based on equal shares or a pro rata approach.

In the Premium Paid Approach, it is argued that the amount of premium received determines the extent to which a carrier should participate in a given period. For instance, if the carrier receives a higher premium a higher amount of indemnity and defense should be allocated to it. A lower premium received should result in a lower allocation. This approach suffers from the same flaw as the limits approach, namely that an insurer should only be responsible for the amount of the damage or injury that occurs during the policy period. Otherwise, the same inequity as the limits approach would result. Furthermore,

while the amount of coverage purchased, both as to terms and limits, certainly is a major factor, premium is often a function of what the market will bear. A soft market will yield lower premiums and higher premiums will be paid in a hard market.

Other Issues

How are deductibles handled? The insured, of course, will only want to pay one deductible. A joint and several approach would support this approach. It is important to note, however, that not every deductible in the triggered policies may be the same. A deductible could be applied on a per claim basis, per occurrence basis, include expenses, or apply to indemnity only.

Should the insured contribute to defense? In most jurisdictions, the duty to defend is complete. In other words, if there is a potential for coverage then the lawsuit must be defended by the insurer in total, notwithstanding the fact that the complaint includes uncovered allegations as well as covered allegations. (In this instance, in some jurisdictions that insurer has the right to reimbursement for those claims that are not even potentially covered.)

When does excess insurance participate? The answer…"it depends".

> With some exceptions, courts that apply pro rata allocation tend to exhaust a policyholder's insurance program "horizontally," i.e., exhausting all primary policies, then all first-layer excess policies, and so on. Conversely, courts that apply joint-and-several allocation tend to apply "vertical" exhaustion, looking to all policies in one "policy period" at a time before moving to policies covering other periods.
>
> Courts are much more likely to apply horizontal exhaustion when allocating the costs of defense counsel.[26]

In a recent California case, the appellate court considered the issue of whether all primary insurance must be exhausted before an excess insurer must respond. In *Kaiser Cement & Gypsum Corp. v. Insurance Co. of Pennsylvania*, 2013 Cal App. LEXIS 269 (Cal. App. 2d Dist. Apr. 8, 2013, an asbestos case, the Court ruled, *based on the language of the excess policy***,** that all collectible primary insurance, in addition to the direct underlying insurance, must be exhausted before the excess policy is triggered. "Although the primary policy may be consulted in interpreting an excess policy, each policy is a separate document and is interpreted separately." *Kaiser*

The Court made clear that horizontal exhaustion is appropriate but it must be based on the language of the excess policy which provides that all primary insurance must be exhausted.

Note that "horizontal exhaustion" for the purposes of determining when an excess carrier steps in is not the same as "stacking" of insurance coverage. "Stacking" 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." *Kaiser* Whether stacking will be allowed depends on the language of the policy.

The following exhibit illustrates the different approaches to other insurance and allocation:

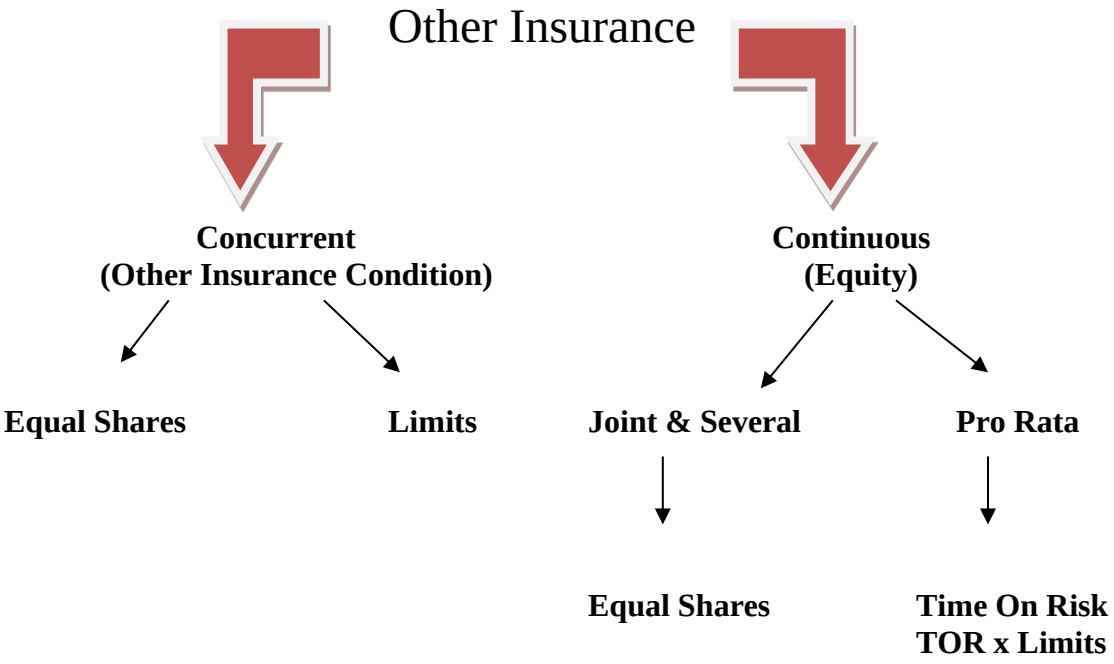

Exhibit D. Allocation Methods

Allocating costs among carriers is endemic to continuous damage claims. It requires time, effort, a fundamental grasp of the issues, and the ability to apply a set of specific facts to a constantly changing and sometimes hazy landscape, and in a consistent manner. To achieve an equitable apportionment in this context is quite a challenge. Fortunately, in the majority of cases insurers are able to work together and achieve a result that everyone can live with. However, in my opinion there is still far too much litigation, with its attendant transaction costs, to resolve disputes.

The Way It Is – Selected California Case Law

***Armstrong* - California**

Armstrong World Industries, Inc. v. Aetna Casualty & Surety Co., et al., 45 Cal.App.4th 1 (Cal. App. 1st Dist. 1996) involved the trigger of coverage and allocation among the carriers and the policyholder as to third parties' asbestos bodily injury claims.

The Court ruled as follows:

1. The continuous trigger will apply.

2. One triggered policy, selected by the policyholder, will pay with allocation to the other triggered policies. The allocation would be based on time on risk and the limits of each policy.

3. The policyholder will not be required to contribute for any uninsured periods based on the premise that the "all sums" language requires the triggered policy to respond in full, with only the ability to obtain contribution from the other triggered policies, and not the policyholder for any uninsured years.

***Centennial* – California**

In March 2001, the Court of Appeal, First District, in *Centennial Ins. Co. v. United States Fire Ins. Co.,* 88 Cal. App. 4th 105 (Cal. App. 1st Dist. 2001), addressed the allocation of defense between two insurers. The Court ruled that the sharing of defense costs on a time on risk basis was more equitable than equal shares. The focus of the Court was on equity based on the specific facts before it:

> On the facts before us, we have no difficulty concluding that in this particular case, the time on the risk method was more equitable than the equal shares approach. U.S. Fire was responsible for insuring Lincoln for a period of less than six months between January 19, 1982, through July 1, 1982, only a small fraction of the total insurance coverage period of four and one-half years provided to Lincoln by Centennial, Travelers and U.S. Fire together. In order to adopt the equal shares method of allocation advanced by Centennial, the trial court would have been required simply to ignore the **…** relative length of time each of the several insurers was actually responsible for insuring the acts of Lincoln and was receiving insurance premiums for bearing that risk. Had the trial court applied an equal shares allocation, U.S. Fire would have had exactly the same liability for defense costs as Centennial and Travelers, even though the latter two insurers had covered Lincoln for nearly 90 percent of the duration of the combined policy period and had also collected premiums for that longer period of

> coverage accordingly. Such a result would have been patently arbitrary and inequitable. *Centennia*l 105, 113-114

The Court went on to make clear that the facts dictate that no “bright line” rule of allocation can be made:

> There is no reason for adoption of the kind of "bright line" rule urged by Centennial, much less one requiring application of an "equal shares" approach in every case. As seen, the California courts have expressly and repeatedly refused to formulate a definitive, rigid rule establishing a single method of allocating defense costs in every case. The reason for the courts' refusal to establish such a bright-line rule is the existence of differing factual circumstances varying from case to case, which unavoidably give rise to different equitable considerations that must be taken into account. Among other things, these considerations include the particular terms, exclusions and limits of the respective insurance policies in effect; the time each co-insurer is "on the risk"; the nature of the given claim; the relation of the insured to the several insurers; and the relative amount of premiums paid. In order to avoid the inequities that would inevitably result from application of a single rigid rule in all cases, the courts in California have consistently held that trial courts must maintain equitable discretion to fashion a method of allocation suited to the particular facts of each case and the interests of justice, subject to appellate **…** review for abuse of that discretion. A single bright-line rule to be applied in every instance would be the very antithesis of such an equitable approach. *Centennial* 105, 115-116

Endnotes

[1] Randy Maniloff and Jeffrey Stempel, General Liability Insurance Coverage/Key Issues in Every State (New York, NY, Oxford University Press, Inc. 2011) p. 70.

[2] Policy language throughout this paper is from ISO's form CG 00 01 12 04, ©ISO Properties, Inc., 2003. The focus here is on the "occurrence-based" policy as opposed to claims-made coverage that requires that a claim be first made during the policy period and is usually subject to a retroactive date, or the date on or after which property damage must occur.

[3] Merriam-Webster Online, http://www.m-w.com/dictionary/accident.

[4] For instance, see *Lennar Corporation v Great American Insurance Company*, 2006 WL 406609 (Tex. App.-Hous. (14 Dist., Pet. Filed): "Accordingly, finding no occurrence for defective construction resulting in damage to the insured's work would render the subcontractor exception superfluous and meaningless."

[5] Richard M. Shusterman, Anthony L. Miscioscia, Peter F. Rosenthal, Liability Insurance Coverage for Construction Defect Claims (FDCC Quarterly/Summer 2005) 503 – 504.

[6] "Since 1971, ISO has been a leading source of information about property/casualty insurance risk…provide(s): statistical, actuarial, underwriting, and claims information; policy language; information about specific locations; fraud-identification tools; technical services." http://www.iso.com/About-ISO/Overview/About-ISO.html

[7] Jeffrey W. Stempel, Stempel on Insurance Contracts, Third Edition (New York: Aspen Publishers, 2009, 2008-2006) Vol.1, 1-35.

[8] Jeffrey W. Stempel Vol.1, 1-36.

[9] The Stringfellow Site has an interesting history. "In 1955, a state geologist determined that a Riverside County quarry was a suitable location for the disposal of industrial waste. According to the geologist's report, the site was a canyon lined on its bottom with impermeable rock. The geologist advised the State to build a concrete barrier dam to close a 250-foot gap in the canyon's natural walls. He claimed that, once the dam was in place, 'the operation of the site for industrial wastes [would] not constitute a threat of pollution.' The State subsequently developed the facility, which went into operation in 1956, and eventually received more than 30 million gallons of industrial waste.

In reality, the site suffered from three major flaws that made it ill suited to serve as an industrial waste facility. First, the state geologist had failed to identify an underground aquifer located 70 feet below the canyon floor that facilitated the movement of groundwater into and out of the site. Second, the rock underlying the canyon floor was fractured, so it allowed waste to leak into the groundwater system and escape the facility. Third, the barrier dam proved ineffective. It permitted contaminants to escape the facility during heavy rains in 1969 and again in 1978. The severity of the latter event forced the State to conduct a 'controlled discharge' of contaminants into Pyrite Channel. The ensuing plume of waste extended for miles. The State closed the facility in 1972 after discovering the groundwater contamination.

In 1998, a federal court found the State liable for, inter alia, negligence in investigating, choosing, and designing the site, overseeing its construction, failing to correct conditions at it, and delaying its remediation. The State was held liable for all past and future cleanup costs." *State of California v. Continental Ins. Co.*, 55 Cal. 4th 186, 192-193 (Cal. 2012)

[10] *Remmer v. Glens Falls Indem. Co*. (1956) 140 Cal. App. 2d 84.

[11] Noteworthy is Footnote 19 that addresses whether a carrier is jointly and severally liable for all damage that occurs, including damage that begins prior to a specific policy "We do not endorse that aspect of the *California Union* court's holding that both insurers in that case were *jointly and severally* liable for the full amount of damage occurring during the successive policy period. Allocation of the cost of indemnification once several insurers have been found liable to indemnify the insured for all or some portion of a continuing injury or progressively deteriorating property damage requires application of principles of contract law to the express terms and limitations of the various policies of insurance on the risk." *Montrose* 681

[12] Interestingly, the Court concedes that "an action to recover cleanup costs was inevitable" yet defines the contingency only in the context of legal liability. The CGL policy provided both defense and indemnity, not just indemnity. In other words, if an action to recover cleanup costs was inevitable and defense expenses are covered shouldn't the contingency requirement also apply to defense coverage?

[13] http://www.leginfo.ca.gov/cgi-bin/displaycode?section=ins&group=00001-01000&file=1-48.

[14] http://www.leginfo.ca.gov/cgi-bin/displaycode?section=ins&group=00001-01000&file=250-253

[15] It would appear, according to *Montrose*, that liability is established with certainty when a verdict is rendered. One could argue that liability is established **at the time the act causes damage**…all that remains, notwithstanding that sometimes the "guilty" go free and vice versa, is the "formality" of a trial.

[16] www.leginfo.ca.gov

[17]The CGL policy contains the following Other Insurance Condition, in part:

4. Other Insurance

If other valid and collectible insurance is available to the insured for a loss we cover under Coverages **A** or **B** of this Coverage Part, our obligations are limited as follows:

a. Primary Insurance

This insurance is primary except when **b.** below applies. If this insurance is primary, our obligations are not affected unless any of the other insurance is also primary. Then, we will share with all that other insurance by the method described in **c.** below.

b. Excess Insurance

This insurance is excess over:

(1) Any of the other insurance, whether primary, excess, contingent or on any other basis:

(a) That is Fire, Extended Coverage, Builder's Risk, Installation Risk or similar coverage for "your work";

(b) That is Fire insurance for premises rented to you or temporarily occupied by you with permission of the owner;

(c) That is insurance purchased by you to cover your liability as a tenant for "property damage" to premises rented to you or temporarily occupied by you with permission of the owner; or

(d) If the loss arises out of the maintenance or use of aircraft, "autos" or watercraft to the extent not subject to Exclusion **g.** of Section **I** – Coverage **A** – Bodily Injury And Property Damage Liability.

(2) Any other primary insurance available to you covering liability for damages arising out of the premises or operations, or the products and completed operations, for which you have been added as an additional insured by attachment of an endorsement.

When this insurance is excess, we will have no duty under Coverages **A** or **B** to defend the insured against any "suit" if any other insurer has a duty to defend the insured against that "suit". If no other insurer defends, we will undertake to do so, but we will be entitled to the insured's rights against all those other insurers.

When this insurance is excess over other insurance, we will pay only our share of the amount of the loss, if any, that exceeds the sum of:

(1) The total amount that all such other insurance would pay for the loss in the absence of this insurance; and

(2) The total of all deductible and self-insured amounts under all that other insurance.

We will share the remaining loss, if any, with any other insurance that is not described in this Excess Insurance provision and was not bought specifically to apply in excess of the Limits of Insurance shown in the Declarations of this Coverage Part.

c. Method Of Sharing

If all of the other insurance permits contribution by equal shares, we will follow this method also. Under this approach each insurer contributes equal amounts until it has paid its applicable limit of insurance or none of the loss remains, whichever comes first.

If any of the other insurance does not permit contribution by equal shares, we will contribute by limits. Under this method, each insurer's share is based on the ratio of its applicable limit of insurance to the total applicable limits of insurance of all insurers.

[18] To illustrate, it is well established that property damage beginning during a policy period and that progresses/continues after the policy expires does not relieve the insurer at the time the damage begins of responsibility for the entire loss. Conversely, should the insurer later in the continuum be responsible for property damage that begins prior to the inception of the policy?

[19] J. Stephen Berry and Jerry B. McNally, Allocation of Insurance Coverage: Prevailing Theories and Practical Applications, Tort Trial & Insurance Practice Law Journal Summer, 2007, American Bar Association.

[20] "The term 'joint and several' is a misnomer. While each insurer is fully responsible for indemnifying its policyholder, this result does not stem from any kind of shared duty to the policyholder as the term might suggest in a tort setting. Rather, the duties of each insurer are contractual in nature, and are defined by the terms of each policy." *Crossman Cmtys. of N.C. v. Harleysville Mut. Ins. Co*., 395 S.C. 40, 51 (S.C. 2011) However, the term is useful to explain the "all sums" allocation approach.

[21] R. Steven Rawls and Rebecca Appelbaum, Allocation of Damages for Ongoing Losses over Multiple Policies: Who Pays and How Much? January 2006 (http://www.irmi.com/Expert/Articles/2006/Rawls01.aspx).

[22]J. Stephen Berry and Jerry B. McNally.
[23]J. Stephen Berry and Jerry B. McNally.

[24]J. Stephen Berry and Jerry B. McNally.

[25]J. Stephen Berry and Jerry B. McNally.

[26] J. Stephen Berry and Jerry B. McNally.