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Case No. S244737

IN THE SUPREME COURT OF THE STATE OF CALIFORNIA

MONTROSE CHEMICAL CORPORATION OF CALIFORNIA,
Petitioner,

v.

SUPERIOR COURT OF THE STATE OF CALIFORNIA,
COUNTY OF LOS ANGELES,
Respondent;

CANADIAN UNIVERSAL INSURANCE
COMPANY, INC., et al.,
Real Parties in Interest.

**After a Decision by the Court of Appeal,
Second Appellate District, Division Three
Civil Case No. B272387**

**After Grant of Review and Transfer to Court of Appeal to Vacate Order
Denying Writ of Mandate and Order to Show Cause
Supreme Court Case No. S236148**

**After Denial of Petition for Writ of Mandate by the Court of Appeal,
Second Appellate District, Division Three
Civil Case No. B272387**

**Petition from the Superior Court of the State of California
for the County of Los Angeles
Case No. BC 005158, Honorable Elihu Berle, Presiding**

MONTROSE CHEMICAL CORPORATION OF CALIFORNIA'S OPENING BRIEF ON THE MERITS

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I. ISSUES RAISED IN PETITION FOR REVIEW

1. In a complex multi-year, multi-insurer, multi-layer comprehensive general liability ("CGL") program, does the standard "other insurance" condition in CGL policies dictate when an excess insurer's obligations to its policyholder are triggered, or are such provisions relevant only to contribution disputes between insurers, as this Court held in *Dart Industries, Inc. v. Commercial Union Ins. Co.* (2002) 28 Cal.4th 1059 ("*Dart*") and the Fourth District Court of Appeal recently confirmed in *State of California v. The Continental Ins. Co.* (2017) 15 Cal.App.5th 1017 ("*Continental II*")?

2. Despite policy language stating that an excess policy attaches upon the exhaustion of a defined amount of immediately underlying insurance in the same period, does the mere presence of an "other insurance" provision override the agreed attachment point and obligate the policyholder to first pursue and exhaust coverage under excess policies issued in every other potentially triggered period spanning the years of continuous damage (including policies with more onerous terms and conditions), thereby effectively imposing mandatory horizontal exhaustion of excess coverage, in contravention of *State of California v. Continental Ins. Co.* (2012) 55 Cal.4th 186 ("*Continental*"), *Aerojet–Gen. Corp. v.*

Transport Indemnity Co. (1997) 17 Cal.4th 38 ("*Aerojet*"), and *Montrose Chemical Corp. v. Admiral Ins. Co.* (1995) 10 Cal.4th 645 ("*Montrose*")?

II. INTRODUCTION

The insurance industry has long searched for ways to curtail CGL insurers' obligations to policyholders in connection with large-scale environmental and similar property damage claims. Over the last twenty-five years, as a result of its significant historic liabilities, Montrose Chemical Corporation of California ("Montrose") has been forced to the forefront of these disputes as a frequent party to seminal insurance coverage decisions by this Court.

In *Montrose v. Admiral*, this Court held that "where successive CGL policies have been purchased, bodily injury and property damage that is continuing or progressively deteriorating throughout more than one policy period is potentially covered by all policies in effect during those periods." (*Montrose*, *supra*, 10 Cal.4th at pp. 686-687.) This principle was reaffirmed by this Court just two years later in *Aerojet*. (*Aerojet*, *supra*, 17 Cal.4th at p. 57 & n.10 ["In *Montrose*, we also made plain that 'successive' insurers 'on the risk when continuous or progressively deteriorating [property] damage or [bodily] injury first manifests itself' are ***separately and independently*** 'obligated to indemnify the insured'[.]" (emphasis added)].)

Building on this precedent, in *State v. Continental*, this Court rejected the insurance industry's proposed rule of "pro rata" exhaustion of excess insurance policies, and declared that California law entitles policyholders facing continuous damage liabilities to obtain coverage from any triggered policy under an "all sums with stacking" interpretation. (*Continental*, *supra*, 55 Cal.4th at pp. 200-201.)

To counter these decisions, the insurance industry has seized on the concept of mandatory "horizontal exhaustion" in hope of achieving the "pro rata" result through other means. Insurers now seek to compel policyholders to horizontally exhaust all lower-level excess coverage across ***all*** triggered years before calling upon individual higher-layer excess policies triggered by their plain terms. This requires the Insurers to distort policy language and California law, and argue that the boilerplate "other insurance" clauses of standardized CGL excess policies rewrite and greatly multiply the policy's attachment point. However, as this Court has ruled, the "other insurance" provision serves no such function. Its purpose is merely to prevent double recovery and to permit insurers who cover the same loss to equitably allocate responsibility for the policyholder's claim, after the policyholder has been fully indemnified. (See *Dart*, *supra*, 28 Cal.4th at p. 1080.)

Nevertheless, at Insurers' behest, Respondent Superior Court ruled that the standard "other insurance" provisions contained in *all* of

Montrose's policies obligate Montrose to exhaust its excess coverage horizontally before tapping any other triggered excess policies. In doing so, Respondent relied on a Court of Appeal decision pre-dating *Continental* and *Dart—Community Redevelopment Agency v. Aetna Casualty & Surety Co.* (1996) 50 Cal.App.4th 329 ("*CRA*"). Although *CRA* had required horizontal exhaustion of primary policies providing defense coverage, Respondent expanded this older decision to ***indemnity*** coverage under ***excess*** policies, with no substantive analysis of the conflict with this Court's more recent precedent. In fact, Respondent's decision did not even attempt to reconcile its ruling with this Court's interpretation and application of "other insurance" provisions in *Dart*.

After the Second District Court of Appeal ("DCA") initially declined to review Respondent's erroneous decision, this Court granted Montrose's Petition for Review and directed the DCA to consider the merits of Montrose's position. On remand, the DCA effectively reached the same result as Respondent by concluding that standard "other insurance" language compels horizontal exhaustion, regardless of insuring language providing that the Policies attach "after other ***identified*** insurance is exhausted." (*Montrose Chemical Corp. v. Superior Court* (2017) 14 Cal.App.5th 1306, 1333 ("Opinion") (emphasis added); cf. *id.* at p. 1328 [recognizing Montrose's position is premised on "the insuring agreements and declarations"—i.e., the provisions specifying the policies' attachment

points].) The DCA recognized that the result of its "other insurance" analysis is "mandatory horizontal exhaustion" for any policy containing that standard condition. (*Id.* at pp. 1335-1336.)

If left uncorrected by this Court, mandatory "horizontal exhaustion" would require policyholders like Montrose to first exhaust numerous separate excess policies spread across all coverage years before obtaining benefits under any single policy triggered by its own insuring language. Such a rule would allow Insurers to re-write their basic coverage obligation and attachment point, despite the fact that the selected policy does not mention (much less require) exhaustion of adjacent years—separate and independent coverage which may not even have existed at the time the policy in question was written. This contrived obligation would even require exhaustion of unrelated policies with different or potentially greater coverage restrictions before broader excess coverage may be tapped. Ultimately, this scheme improperly would allow insurers to defeat coverage that plainly exists and convert policyholders' insurance assets into their own, benefiting from policyholders' prudent decision to obtain coverage in other years, even though the insurers did not bear the cost of that purchase.

Montrose's position rests instead on the plain language of each individual policy, and on insurance coverage principles long declared by this Court: Policyholders should not have their coverage rights truncated

by any artificial, extra-contractual allocation scheme, much less a "mandatory horizontal exhaustion" rule fundamentally at odds with the "all sums with stacking" interpretation recognized in *Continental.* Rather, California law enforces the policyholder's right to call upon any of the insurance contracts it purchased according to the contract's express individual terms. (See *Aerojet, supra,* 17 Cal.4th at p. 57 & fn. 10 ["'successive' insurers 'on the risk when continuous or progressively deteriorating [property] damage . . . first manifests itself' are separately and independently 'obligated to indemnify the insured'" (citing *Montrose, supra,* 10 Cal.4th at pp. 686-687)]; *Continental, supra,* 55 Cal.4th at pp. 200-201 ["***each policy*** can be called upon to respond to the claim up to the full limits of the policy," and once "the policy limits of a given insurer are exhausted, [the insured] is entitled to seek indemnification from ***any*** of the remaining insurers [that were] on the risk" (emphases added; alteration in original)].)

The issues of exhaustion, allocation, and horizontal and vertical stacking in continuous damage cases involve literally ***billions*** of coverage dollars. Accordingly, the insurance industry fiercely litigates these questions with a strong incentive to avoid, or at least significantly delay, costly coverage obligations by shifting the burden of insurance recovery onto the backs of policyholders. Coverage delayed (or too burdensome to enforce) is often coverage denied, which prejudices not only policyholders,

but the claimants to whom insurance proceeds are ultimately directed. To balance these competing concerns, this Court has called for "immediate" indemnification, not protracted policyholder litigation in inter-carrier insurance battles over contribution. (*Continental*, *supra*, 55 Cal.4th at p. 201; *Dart*, *supra*, 28 Cal.4th at p. 1080.) Once again, the Court should resolve this weighty dispute, confirming that policyholders cannot be forced into a mandatory horizontal allocation and exhaustion scheme, but must instead be permitted to select the triggered policy(ies) under which to exercise their independent contractual rights in accordance with the policy terms.

III. STATEMENT OF THE CASE

A. Factual Background

Montrose was formerly the world's largest producer of DDT, a pesticide and anti-malarial agent. In 1990, various government plaintiffs sued Montrose, seeking damages arising from alleged releases of hazardous substances into the environment as a result of Montrose's operations at its former manufacturing facility in Torrance. (4PA17 at pp. 928-48.) Pursuant to partial consent decrees with the government plaintiffs, Montrose already has incurred damages of more than $100 million, and its anticipated future liability could approach or exceed that amount. (2PA12

at pp. 303-568.) These damages must be paid to fund environmental cleanup.

Between 1961 and 1985, the 40 defendant Insurers issued over 115 excess CGL policies (the "Policies") providing coverage to Montrose. (4PA17 at pp. 865-69; see 1PA5 at p. 99.) Each of the Policies provides that coverage thereunder attaches in excess of a ***predetermined*** amount of underlying insurance.[1]

Each Policy describes the applicable underlying coverage in one of four ways:

1. A schedule of underlying insurance listing all of the underlying policy(ies) in the same policy period by insurer name(s), policy number(s), and dollar amount(s).[2]

2. Reference to a specific dollar amount of underlying insurance in the same policy period and a schedule of underlying insurance on file with the insurer, *i.e.*:

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[1] Cf. *Commercial Union Assurance Cos. v. Safeway Stores, Inc.* (1980) 26 Cal.3d 912, 919 ["The object of the excess insurance policy is to provide additional resources should the insured's liability surpass a ***specified sum***." (emphasis added)]; *Wells Fargo Bank v. Cal. Ins. Guarantee Assn.* (1995) 38 Cal.App.4th 936, 940, fn. 2 ("*Wells Fargo*") ["[W]e use the terms 'excess coverage' or 'excess policy' to mean insurance that begins only after a ***predetermined amount*** of underlying coverage is exhausted . . . ." (emphasis added)].

[2] See 1PA10, p. 279 at ¶ 14 (listing 25 Policies employing this method).

Underlying Insurance Limit of Liability
$31,000,000 each occurrence
$31,000,000 aggregate" . . .

Schedule of Underlying Insurance: As on File with Company.[3]

3. Reference to a specific dollar amount of underlying insurance in the same policy period and identification of one or more of the underlying insurers, *i.e.*:

Underlying Umbrella Policies:
American Centennial Insurance Company . . .

Underlying Umbrella Limits:
$19,000,000.00.[4]

4. Reference to a specific dollar amount of underlying insurance that corresponds with the combined limits of the underlying policies in that policy period, *i.e.*:

Underlying Insurance: $20,000,000 each occurrence and aggregate.[5]

Therefore, each of the Policies expressly provides that coverage attaches in excess of a specific, predetermined amount of underlying coverage ***in the same policy period***.[6] Importantly, the Policies' attachment

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[3] *Id.*, p. 278 at ¶ 12 (listing 13 Policies employing this method).

[4] *Id.*, pp. 276-77 at ¶ 10 (listing 35 Policies employing this method).

[5] *Id.*, p. 275 at ¶ 8 (listing 35 Policies employing this method).

[6] The DCA did not reconcile its ruling with this attachment language, instead claiming (falsely) that, "while Montrose repeatedly asserts that the excess policies attach upon the exhaustion of lower layer policies

language does ***not*** reference coverage available under policies in prior or subsequent years.

Other provisions of the Policies—such as the condition mandating that the underlying insurance "shall be maintained in full effect" during the policy period—corroborate the parties' understanding that coverage attaches upon exhaustion of the predetermined amount of coverage provided by the underlying policies in the same policy period. (See generally 1PA10 at p. 282-84, ¶ 18 [listing policies with comparable language].) The "maintenance of underlying insurance" condition ensures that the amount of underlying coverage taken into account by the underwriters in calculating an excess policy's premium is eroded only by the payment of covered losses. Notably, this provision does ***not*** require that the policyholder "maintain in full effect" coverage for other policy years, since that separate insurance—which the insured may or may not purchase—is not taken into account during the underwriting process.

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within the same policy period, ***it does not identify the provisions that supposedly have that effect.***" (Opinion at p. 1327 (emphasis added).) To the contrary, Montrose cited the above provisions multiple times in its briefs. (See Montrose's Petition For Writ of Mandate (filed May 23, 2016) ("Writ Petition") at pp. 19, 36, 59-60; Montrose's Combined Reply to Oppositions to Petition For Writ of Mandate (filed Dec. 15, 2016) at pp. 29-30.)

Finally, each of the Policies also contains or incorporates "other insurance" language, consistent with all standardized CGL policies. The standard language typically provides:

> 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 the insurance afforded by this policy, the insurance afforded by this policy shall be in excess of and shall not contribute with such other insurance.

Approximately 90 of the Policies contain this formulation of the "other insurance" provision. The other Policies contain similar variations. (See generally 1PA6 at pp. 118-166, ¶¶ 1-21.)

Based on this boilerplate "other insurance" language, the Insurers asserted that Montrose cannot access coverage under any single excess Policy unless and until Montrose not only exhausts up to the express attachment point, but also ***all*** "underlying coverage" ***in every policy period across the decades of its insurance portfolio***.

B. Procedural History

Montrose amended its operative Complaint to assert a stand-alone cause of action to resolve this dispute, which the parties agreed was a critical threshold legal issue necessary to structure the litigation. (4PA17 at pp. 900, 914.) The parties filed cross-motions for summary adjudication of Montrose's Thirty-Second Cause of Action. Montrose's motion sought a

declaration that it was not obligated to horizontally allocate its liabilities across all policy periods:

> [I]n order to seek indemnification under the Defendant Insurers' excess policies, Montrose need only establish that its liabilities are sufficient to exhaust the underlying policy(ies) in the **same policy period**, and is not required to establish that all policies insuring Montrose in **every** policy period (including policies issued to cover different time periods both before and after the policy period insured by the targeted policy), with limits of liability less than the attachment point of the targeted policy, have been exhausted; and Montrose may select the manner in which [to] allocate its liabilities across the policy(ies) covering such losses.

(4PA17 at pp. 900, 914 (emphasis in original).)

Conversely, the Insurers' cross-motion argued that Montrose was obligated, as a matter of law, to allocate its losses evenly across all periods. (See 8PA32 at p. 1998 ["All underlying policy limits across the years of continuing property damage must be exhausted by payment of covered claims before any of the Insurers' excess policies have a duty to pay covered claims."].)

The Insurers joined Montrose in representing to the Superior Court (and later to the DCA) that the detailed policy language stipulations entered by the parties contain the language necessary to resolve the legal issue presented. (See 1PA6 at pp. 118-200; 1PA7 at pp. 208-234; accord Montrose's Request for Judicial Notice in Support of Reply in Support of Petition for Review (granted Nov. 29, 2017), Ex. 1 at 28:7-9 [Continental's

counsel: "The parties categorically agreed that this is the relevant language that the Court has to make the decision on."]; *id.* at 27:9-16 [Continental's counsel: "The parties stipulated to the relevant policy language . . . that language is in the record and it's quoted in the various statements of undisputed fact."].)

Respondent Superior Court denied Montrose's motion and granted Insurers' cross-motion, concluding that "the parties ***must employ a horizontal exhaustion approach***, whereby the aggregate limits of underlying policies for the applicable policy periods must first be exhausted before any excess policies incur a duty to indemnify Montrose for its liabilities[.]" (1PA1 at pp. 59:28-60:5 (emphasis added).) Respondent reached this result by concluding that there is a "***well-established rule*** that horizontal exhaustion should apply in the absence of policy language specifically describing and limiting the underlying insurance." (*Id.* at p. 54:14-17 (emphasis added).)

After finding that the Policies contain "some form of the [ ] standard [other insurance] language," Respondent held that:

> [T]he 'other insurance' provisions contained in the present excess policies must be read to require the exhaustion of all underlying insurance before their obligations to indemnify Montrose attach. The presence of 'other insurance' clauses would preclude the use of a vertical exhaustion approach even for those excess policies specifically [identifying] a

> particular underlying policy that must first be exhausted.

(See 1PA1 at pp. 55:26-56:6; *id.* at pp. 58:16-23.)

Notably, Respondent completely failed to address this Court's decision in *Dart* concerning the limited role of "other insurance" provisions, despite noting Montrose's reliance on that case. (*Id.* at 56:11-18.)

Montrose timely petitioned the DCA for writ review, which was denied summarily on July 13, 2016. On October 12, 2016, this Court granted Montrose's petition for review and transferred the case back to the DCA, with directions to vacate the order denying Montrose's petition and to issue an order to show cause why the relief Montrose sought should not be granted. Following additional briefing and oral argument, the DCA issued its Opinion on August 31, 2017.

The DCA's Opinion ignored the express language of the Policies stating that coverage attaches upon the exhaustion of a specified amount of underlying insurance in the same policy year, instead exalting the "other insurance" provisions and holding that these conditions actually define the amount of coverage that must be exhausted before an excess policy is triggered. (See Opinion at p. 1333 ["[A]n 'other insurance' clause may define the insurance ***that must be exhausted before the excess insurance***

attaches[.]" (emphasis added)]; *id.* at p. 1334 ("'[O]ther insurance' clauses may be relevant to determining . . . the order in which excess policies attach."]; contra *Dart, supra,* 28 Cal.4th at p. 1080.) The DCA recognized that the result of its "other insurance" analysis is "mandatory horizontal exhaustion" for any policy containing the standard "other insurance" language, as all standardized CGL policies do. (Opinion at pp. 1335-1336.)[7]

Respondent Superior Court's ruling and the misguided decision of the DCA improperly restrict Montrose's right to enforce the plain policy language of each individual policy and subvert numerous insurance principles long declared by this Court.

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[7] The DCA also ruled that further examination of the Policies' "other insurance" provisions should be conducted because "Montrose has not demonstrated [] that each of the policies at issue has an 'other insurance' clause[.]" (*Id.* at p. 1334, fn.7.) However both Montrose ***and the Insurers*** expressly recognized that ***all*** of the Policies contain standard "other insurance" provisions. (See, e.g., Continental's Opposition to Montrose's Petition For Writ of Mandate (filed Nov. 23, 2016) ("Writ Opposition") at p. 28 ["***[E]ach of the excess insurers' policies*** either itself contains or follows form to and incorporates language that makes the policies excess of vertically underlying coverage and excess of all 'other insurances,' 'other collectible insurance' or 'other valid and collectible' insurance." (emphasis added)].) Similarly, Respondent Superior Court found that the Policies contain standard "other insurance" provisions. (See 1PA1 at pp. 55:26-56:6 ["The 'other insurance' provisions in the policies generally include some form of the following standard language . . . ."].)

IV. ARGUMENT

Over the last two decades, this Court repeatedly has declared the fundamental principle that a policyholder has the contractual right, under any insurance policy(ies) triggered by a covered loss, to obtain immediate indemnification of its liabilities. (E.g., *Aerojet*, *supra*, 17 Cal.4th at p. 57 & fn. 10.) Most recently, the Court held that when a continuous injury triggers multiple policies, "***each*** policy can be called upon to respond to the claim up to the full limits of the policy." (*Continental*, *supra*, 55 Cal.4th at p. 200 (emphasis added).) Once "'the policy limits of a given insurer are exhausted, [***the insured***] is entitled to seek indemnification from ***any*** of the remaining insurers [that were] on the risk.'" (*Ibid.* (citation omitted; alterations in original; emphasis added).) This rule safeguards the insured's right to "immediate access to the insurance it purchased." (*Id.* at p. 201.)

"Other insurance" provisions have ***no impact*** on the insured's coverage rights for continuous damage losses. (*Dart*, *supra*, 28 Cal.4th at p. 1080.) Instead, "other insurance" provisions govern inter-insurer allocations ***after*** the policyholder has been fully indemnified. (*Ibid.*) That "apportionment, however, has ***no bearing*** upon the insurers' obligations to the policyholder." (*Ibid.* (emphasis added); see also *Armstrong World Industries, Inc. v. Aetna Casualty & Surety Co.* (1996) 45 Cal.App.4th 1,

106 ("*Armstrong*") ["allocation among insurers 'does not reduce their respective obligations to their insured'" (internal citation omitted)].)

These governing rules recently were applied by the Court of Appeal in *Continental II.* The Fourth District recognized that (1) this Court's decision in *Dart* establishes that "other insurance" provisions do not impact the policyholder's right to recovery under triggered excess insurance policies; and (2) the horizontal exhaustion principle discussed in *CRA* is applicable only to primary insurance. (*Continental II*, *supra*, 15 Cal.App.5th at pp. 1032, 1034.)

Respondent and the DCA diverged sharply from this approach, turning this Court's rules on their head by concluding that standard "other insurance" provisions function as coverage-limiting devices. According to the courts' novel interpretation, these provisions obligate policyholders to pursue and exhaust separate coverage in other policy periods, even though the policies contain materially different provisions affecting the scope of coverage. This result negates policyholders' right to call upon independent contracts according to their terms and disregards the clear guidance from both *Continental* and *Dart*.

A. Mandatory Horizontal Exhaustion Contradicts Established California Law By Artificially Restricting Policyholders' Rights

Prior to the decisions of Respondent Superior Court and the DCA, no California court had ruled that a policyholder must exhaust its