

The California Supreme Court Confirms Vertical Exhaustion Applies for First-Layer Excess Insurers

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In *Truck Ins. Exch. v. Kaiser Cement*, 321 Cal. Rptr. 3d 761, 549 P.3d 781 (2024), the California Supreme Court answered the question left open by *Montrose Chem. Corp. v. Superior Ct.*, 9 Cal. 5th 215 (2020) (*Montrose III*): for a continuous injury or damage spanning multiple policy periods, must an insured exhaust all implicated primary policies spanning the entire period of injury or damage prior to accessing any excess policy during that period.

In *Truck*, the Court answered “no” – an insured is not required to exhaust all implicated primary policies; rather, the insured can access an excess policy simply by exhausting the primary policy directly underlying it. In other words, the Court adopted “vertical” exhaustion.

Where a “continuous” or “long-tail” injury or damage triggers multiple policy periods – implicating primary and excess policies across those periods – there are often disputes over which primary policies must be exhausted before excess policies are triggered. There are generally two arguments asserted in these disputes: (i) “horizontal exhaustion,” which requires the insured to exhaust all implicated primary policies before any excess policies can be triggered; and (ii) “vertical exhaustion,” which requires exhaustion of only the primary policy directly underlying an excess policy before that excess policy can be triggered.

In *Truck*, the California Supreme Court held that the standard language in first-level excess policies requires vertical exhaustion, not horizontal exhaustion.

In *Truck*, the insured (Kaiser) allegedly manufactured asbestos-containing products that caused injuries to more than 24,000 claimants over a multi-year period. Kaiser tendered those claims to Truck, which was one of several primary insurers that had issued Commercial General Liability (“CGL”) policies to Kaiser during that multi-year period.

Truck filed a coverage action to determine its obligations to Kaiser and eventually asserted a contribution claim against several of Kaiser’s excess insurers. Truck sought contribution from the first-level excess insurers that sat above the primary policies not issued by Truck – which had all been exhausted – arguing that their policies had been implicated because the primary policies directly underlying them had been exhausted.

Truck argued that, under *Montrose III*, vertical exhaustion applied and, to access any excess policy, only the primary policy directly underlying that specific excess policy needed to be exhausted. The excess carriers argued that horizontal exhaustion applied and, as a result, all primary policies had to be exhausted before any of the excess policies could be triggered. The Court of Appeal agreed with the excess insurers. This was critical because Truck’s policies lacked aggregate limits and thus had not yet been exhausted.

The California Supreme Court reversed. The Court agreed with Truck that the reasoning of *Montrose III* – which involved a dispute between excess carriers – applied equally to the dispute at hand between a primary insurer and first-layer excess carriers. In particular, the Court held that requiring vertical exhaustion was consistent with the language of standard “other insurance” provisions found in excess policies, which refers to a schedule of specific underlying insurance that must be exhausted before triggering the excess policy.

The Court also concluded that vertical exhaustion was the most practical means of administering coverage for continuous injury or damage claims, as well as consistent with the reasonable expectations of an insured when purchasing coverage for a specific policy period. For those and other reasons, the Court concluded that only vertical exhaustion of the primary policy immediately below a first-layer excess policy is required to trigger that excess carrier’s obligations.

There were, however, two important caveats to the Court’s holding.

First, the Court made clear that excess insurers “remain free to write their future excess policies in a manner that expressly requires horizontal exhaustion.” *Truck*, 549 P.3d at 801. Thus, *Truck*’s holding is arguably limited to the language found in standard excess CGL policies.

Second, the Court’s vertical exhaustion ruling was not dispositive of whether Truck was entitled to contribution from the excess carriers because, under California law, that requires consideration of other equitable factors (not just interpretation of contract language at issue). *Id.* at 802-03. Instead, the Court remanded the case back to the Court of Appeal to decide those issues.

In sum, under *Truck*, when there is a continuous injury or damage across multiple policy periods, the standard language found in CGL first-layer excess policies requires only vertical exhaustion of the underlying primary policy for that specific policy period, not horizontal exhaustion of all primary policies spanning the continuous period of injury or damage.

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