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All Sums or Pro Rata: Did You Get the Coverage You Bought?

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In recent decades, liabilities stemming from long-term bodily injury or property damage—as from exposure to asbestos or contamination of the environment—have presented a variety of new challenges for policyholders seeking to recover from their insurers under comprehensive general liability ("CGL") policies. Injury or damage involved in such "long-tail" claims typically touch multiple policy periods. Most CGL policies are implicated or "triggered" if injury or damage happens during the policy period, regardless of when the claim is made. An employee's inhalation of asbestos fibers may lead to injury that occurs over many decades, as might contamination from a leak of hazardous material. This is quite unlike more traditional and instantaneous "slip and fall" type bodily injury and property damage claims, which only trigger a single liability policy because they happen instantaneously and the resulting claim follows quickly.

While claims involving long-term injury present many complex factual issues, a critical legal issue raised by long-tail claims is the scope of an insurer's obligations once an insurance policy has been triggered. A policyholder that faces liability claims implicating multiple years may find that the claim is covered under many, if not all, of its insurance policies, yet later learn that it is entitled to receive significantly less than full coverage for the claim. Resolution of this issue, known as the "allocation" issue, varies greatly from state to state. In one recent decision, an Indiana appellate court reached the opposite conclusion of the state's highest court on questionable grounds. The question is how much coverage a policyholder can obtain from a triggered policy.

This article describes the issue and the different legal standards that courts have applied to the scope of coverage issue. It then discusses how to argue for the most favorable result of the issue. Finally, the article discusses how to negotiate the settlement of a claim when the law of the relevant state on the issue is favorable to the policyholder.

Allocation—A Divisive Issue

Courts have split on resolution of the allocation issue. Those that adopt a standard favorable to policyholders focus on the policy's opening grant of coverage, in which the insurer promises to pay "all sums" relating to the policyholder's liability. The courts that adhere to an "all sums" approach find that the insurer is fully liable, up to the policy limits, for the entire sum of damages owed by the policyholder. If the claim exceeds the policy limits, the policyholder can access the excess policies in the same year, and some courts allow the policyholder to "stack" policies from other years. An insurer's obligation to pay all sums generally is subject to its right to seek contribution from other insurers whose policies also were triggered by the same claim.

Courts adhering to this approach rely on the plain language of the opening insuring agreement in liability policies, which in varying forms often states that the insurer will "pay on behalf of the insured ***all sums*** which the insured becomes legally obligated to pay as damages because of bodily injury or property damage." Among those courts that have adopted the all sums approach are the highest state courts in California, Delaware, Illinois, Indiana, Ohio, Pennsylvania, Texas, Washington, and Wisconsin.[1]

Other courts focus on the definitions of "bodily injury" and "property damage" and the requirement that injury and damage must happen "during the policy period."[2] These courts generally allocate a portion of the costs to each different policy period in which the triggering injury or damage occurred, and often to the policyholder for years in which there was no applicable coverage. Under this "pro rata" approach, each policy in effect during a period triggered by long-term bodily injury or property damage is responsible for a share of the resulting indemnification and/or defense costs incurred, and the policyholder may not look to any single policy or policy period to cover the total amount of such costs. Among those courts that have adopted pro rata allocation are the highest state courts in Colorado, Connecticut, Georgia, Hawaii, Kansas, Kentucky, Louisiana, Massachusetts, Minnesota, Nebraska, New Hampshire, New Jersey, and New York.

Notably, there are different types of pro rata allocation. Massachusetts allocates damages evenly across all triggered policy years, with the policyholder paying for those years in which it has no coverage. *Boston Gas Co. v. Century Indem. Co.*, 910 N.E.2d 290 (Mass. 2009). The U.S. Court of Appeals for the Second Circuit, however, does not allocate damages to the policyholder for periods in which coverage was not available to the policyholder in the insurance market. *Stonewall Ins. Co. v. Asbestos Claims Mgmt. Corp.*, 73 F.3d 1178 (2d Cir. 1995); *see also Wooddale Builders, Inc. v. Md. Cas. Co.*, 722 N.W.2d 283, 297-98 (Minn. 2006) (holding, under Minnesota law, that "the total period over which liability is allocated must include any times during which damages occurred but [the policyholder] was *voluntarily* self-insured") (emphasis added). New Jersey, based on "public interest" considerations, allocates damages among different policy periods according to the proportional amount of coverage provided in each triggered year. *Owens-Illinois, Inc. v. United Ins. Co.*, 650 A.2d 974, 992 (N.J. 1994). New York's highest court is alone in agreeing that damages should be allocated among multiple periods, but it states that the method of allocation should be separately decided based on the unique facts of each case. *See Consolidated Edison Co. of NY, Inc. v. Allstate Ins. Co.*, 774 N.E.2d 687 (N.Y. 2002).

The Flaw in the Pro Rata Approach

Whether to allocate costs among different policy periods is a legal issue and to be decided by a court, not a jury, because it involves the construction of policy language. For a policyholder, the manner in which the court decides to approach the allocation of damages among different policies often means the difference between being made whole and receiving mere cents on the dollar. A policyholder litigating in an "all sums" jurisdiction may choose which of the triggered policies will be required to cover the total loss incurred. Assuming that the policyholder has enough solvent coverage, the all sums approach guarantees that the policyholder will successfully recover the total amount of its insured loss. Alternatively, a pro rata allocation often results in a policyholder receiving only a small portion of the costs it expected to recover when it purchased insurance.

The authors believe that a pro rata allocation is contrary to the policy language and incorrect as a matter of law. Most courts that allocate pro rata in the face of the "all sums" language of the policies confuse the event

[1] *State of California v. Continental Ins. Co.*, 281 P.3d 1000 (Cal. 2012); *Hercules Inc. v. AIU Ins. Co.*, 784 A.2d 481 (Del. 2001); *Zurich Ins. Co. v. Raymark Indus., Inc.*, 514 N.E.2d 150 (Ill. 1987); *Allstate Ins. Co. v. Dana Corp.*, 759 N.E.2d 1049 (Ind. 2001); *Goodyear Tire & Rubber Co. v. Aetna Cas. & Sur. Co.*, 769 N.E.2d 835 (Ohio 2002); *J.H. France Refractories Co. v. Allstate Ins. Co.*, 626 A.2d 502 (Pa. 1993); *Lennar Corp. v. Markel Am. Ins. Co.*, 413 S.W.3d 750 (Tex. 2013); *American Nat'l Fire Ins. Co. v. B & L Trucking & Const. Co.*, 951 P.2d 250 (Wash. 1998); *Plastics Eng'g Co. v. Liberty Mut. Ins. Co.*, 759 N.W.2d 613 (Wis. 2009).

[2] Policyholders take the view that this language tells you what must happen to trigger coverage—injury or damage during the policy period—but once triggered, the policy must pay "all sums."

that *triggers* the coverage with the insuring agreement that defines *how much* coverage is provided. The policies are *triggered* by injury or damage "during the policy period"; once coverage is triggered, the policy obliges the insurer to pay "all sums" associated with the loss. Courts that conflate these two concepts, limiting coverage to the portion of the loss occurring during the policy period, effectively read the phrase "all sums" out of the policy, ignoring the opening grant of coverage and violating the principle that all parts of a policy must be given effect.

As set forth in those cases that correctly recognize the import of the all sums language, "the question of trigger and the question of allocation are separate . . . ." *American Nat'l Fire v. B&L Trucking*, 951 P.2d 250, 255 (Wash. 1998). The question of trigger only addresses whether or not a policy has been activated to provide coverage for the insured. The question of allocation, however, only arises *after* the policy is triggered. Thus, whereas a policy may not be triggered unless the injury or damage occurs "during the policy period," once that policy is triggered, the express language of the insuring agreement obligates that policy to pay all sums—regardless of the extent to which damages accrued during that policy period. *See, e.g.*, *Monsanto Co. v. C.E. Heath Compensation & Liab. Ins. Co.*, 652 A.2d 30, 34-35 (Del. 1994) ("A policy is activated by bodily injury or property damage that takes place 'during the policy period.' The triggering language in the Monsanto insurance policies does not define the extent of coverage. Once a policy is on the risk, the unambiguous policy language requires the insurance company to pay 'all sums' for which the policyholder shall become liable, up to the policy limits."); *Plastics Eng'g Co. v. Liberty Mut. Ins. Co.*, 759 N.W.2d 613, 626-27 (Wisc. 2009) ("[The insurer] argues that the definition of 'bodily injury' supports its pro rata argument. 'Bodily injury' is defined as 'bodily injury, sickness or disease sustained by any person which occurs during the policy period, including death at any time resulting therefrom.' As a result, [the insurer] argues that the policy only covers bodily injury that occurs during a policy period. However, bodily injury during the policy period is what triggers the policy; the definition of 'bodily injury' is not a limitation of liability clause.").

Some courts appear to have manufactured reasons to allocate on a pro rata basis—even in established all sums jurisdictions. The Indiana Court of Appeals decision in *Thomson Inc. v. Ins. Co. of N. Am.*, No. 49A05-1109-PL-470, 2014 WL 2772834 (Ind. Ct. App. June 19, 2014), is an example; that court ignored state supreme court precedent and applied a pro rata allocation to claims involving injury from toxic substances. The insurance policies stated that:

a) We will pay those sums that the insured becomes legally obligated to pay as damages because of "bodily injury" or "property damage" to which this insurance applies . . . .

b) This insurance applies to "bodily injury" or "property damage" only if:

    1. The "bodily injury" or "property damage" is caused by an "occurrence" that takes place in the "coverage territory"; and

    2. The "bodily injury" or "property damage" occurs during the policy period . . . .

The appellate court recognized that in *Allstate Ins. Co. v. Dana Corp.*, 759 N.E.2d 1049 (2001), the Supreme Court of Indiana applied an all sums result to environmental contamination claims. The appellate court also noted that "those sums" (as used in the Thomson policies) is synonymous with "all sums." The court nonetheless applied a pro rata allocation. It distinguished *Dana* based on the language: "This insurance applies to 'bodily injury' and 'property damage' only if . . . [t]he 'bodily injury' or 'property damage' *occurs during the policy period* . . . ." (Emphasis added.) The court determined that, unlike in the policies at issue in *Dana*, the phrase "occurs during the policy period" qualified the insurers' indemnity obligations such that they were only obligated to indemnify Thomson for the prorated portion of damages that were incurred during the policy period.[3] The *Thomson* court in effect read the acknowledged "all sums" concept out of the policy.

[3] The outcome in Thomson may be reversed on appeal before the Supreme Court of Indiana.

How to Argue for All Sums

The *Thomson* court plainly was troubled by the all sums approach and apparently was looking for an excuse to allocate on a pro rata basis. Courts that have applied pro rata allocation in the face of all sums policy language often perceive unfairness in holding an insurer responsible for the entire amount that an insured is liable to pay, when only a portion of the damages were incurred during each particular policy period. Policyholders litigating in a jurisdiction where the law regarding allocation is undecided (or as *Thomson* shows, even in an established all sums jurisdiction) should be aware of this perception of unfairness and tailor their arguments to alleviate the court's potential concerns.

First, the policyholder should highlight the fact that it was the insurer who drafted the policy and included a promise to pay "all sums." The "all sums" language was the basis on which it offered insurance to the policyholder, who had no part in negotiating this standard form term, and who paid premiums expecting *complete* coverage for any potential loss. As the Supreme Court of Washington noted: "Insureds are not purchasing 'almost comprehensive' coverage. CGL policies are marketed by insurers as comprehensive in their scope and should be strictly construed when the insurer attempts to subtract from the comprehensive scope of its undertaking." *Olds-Olympic, Inc. v. Commercial Union Ins. Co.*, 918 P.2d 923 (Wash. 1996).

Second, the policyholder should stress that, in fact, no single insurer will actually be left with an obligation to cover all sums for which the insured is held liable. The insurer ordinarily has contribution rights against other insurers whose policies were also triggered by the same occurrence. The insurer likely has purchased reinsurance to cover its liabilities. The insurer is only liable for all sums up to the policy limits, and coverage only kicks in once the policyholder has paid any applicable deductible. Further, the policy contains exclusions designed to protect the insurer and limit the risk it assumed. This is how insurance coverage is designed to work—the policyholder purchased *comprehensive* insurance, and the insurer can act to make certain the assumed risk is shared with other insurers or reinsurers or that it is otherwise protected after fulfilling its obligations to the policyholder.

Some courts have supported their adoption of pro rata allocation upon the hypothetical that a policyholder that purchases just one year of coverage would be treated the same as one that purchased thirty years of coverage, if the insurer is obligated to pay all sums. But the theoretical purchaser of a single year of comprehensive general liability insurance is mere hyperbole, except in the extraordinary circumstance where the policyholder goes bankrupt before it can purchase coverage for the subsequent year.

Policyholders should also argue that the policy must be construed to give each provision meaning, a rule of construction that exists in every jurisdiction. Courts that allocate pro rata fail to do so. The *Thomson* court claimed that its interpretation "gives effect to the plain meaning of the limiting phrases 'those sums' and 'during the policy period' and does not render any of the remaining language meaningless." This was not accurate. The *Thompson* court failed to give meaning to the phrase "those sums," which it acknowledged is a synonym in the policy for "all sums," rendering that phrase mere surplus. Rather, the court construed the phrase "during the policy period" to serve two distinct functions: to establish the trigger of coverage and to establish a method of allocation among triggered policies.

Finally, policyholders need to remind courts that it is a universal tenet of policy language construction that the policyholder is entitled to the most favorable reasonable construction of the policy. That the highest courts in numerous states have construed the all sums language to mean what it says demonstrates that an all sums interpretation is reasonable. Because an all sums result is the most favorable reasonable interpretation for the policyholder, the policyholder is entitled to that interpretation.

Settling Claims in an All Sums State

A policyholder engaged in settlement negotiations in an all sums jurisdiction must also be creative. It must recognize that the insurer ultimately will not pay 100% of its claim, even if a judicial award would so require. To effect a settlement, the insurer must be provided a discount for its contribution rights. The policyholder should be willing to accept a reduced sum in recognition of the fact that the insurer normally would turn to its fellow insurers for contribution in litigation. But in negotiating such a discount, the policyholder also should understand that the insurer will almost never benefit from full contribution.

In essence, the insurer stands in the shoes of the policyholder when it seeks to obtain contribution and will face many of the same obstacles to recovery as the policyholder. For each potential obstacle that an insurer would encounter, the discount afforded to the insurer in settlement should be reduced. For example, the insurer may find that one or more of its fellow insurers is insolvent and will not contribute to coverage. The insurer will have to pay the cost of litigating with insurers who will not voluntarily contribute. The insurer also will have to pay the amount of the deductible in other policy periods and will run up against the limits of other policies. Each of these obstacles reflects money that should not be deducted from the total claim. Thus, the policyholder should factor in some form of contribution discount and an appropriate litigation discount.

Conclusion

A policyholder is entitled to the coverage for which it has paid, but the reality is that many courts are allocating costs in a manner inconsistent with all sums policy language. The prudent policyholder must be conscious of this, both in litigation and in settlement negotiations. There are convincing arguments to be made that "all sums" does, in fact, mean "all sums"—and exploiting those arguments may be the difference between receiving cents on the dollar and being made whole.