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Appleman on Insurance Law and Practice

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APL2 HOLMES' APPLEMAN ON INSURANCE 2d
PART XIII Environmental Insurance
CHAPTER 193 ENVIRONMENTAL INSURANCE

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FOOTNOTES:

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Scope

This chapter examines environmental insurance coverage issues in the context of historical comprehensive general liability (CGL) policies, environmental impairment liability insurance (EIL) policies and various current environmental insurance products or arrangements.

When CERCLA and other environmental legislation were enacted in the late 1970s and early 1980s, policyholders looked to old CGL policies for coverage of their resulting environmental liabilities. After decades of coverage litigation, the framework for analyzing environmental claims remains complicated and nuanced from jurisdiction to jurisdiction.

The first part of this chapter discusses the historical development of the CGL policy and the most commonly raised coverage issues thereunder in the context of environmental claims. Careful consideration must be given not only to the various exclusions for pollution claims, which became prevalent after the early 1970s, but also to the other insuring and exclusionary provisions that can impact coverage for environmental liabilities. Moreover, once the substantive determination of coverage is made, debate and litigation continues over the scope and priority of coverage over a multi-year period of damage or injury. Section one outlines these numerous coverage issues, and others.

The second part of the chapter looks at claims under EIL policies and other various environmental policies and products in the current market, for which the judicial landscape remains relatively untouched. Such policies can be tailored to fund environmental cleanup or otherwise provide needed security in the context of financing real estate transfers and transactions. Understanding the key terms and their nuances is key to procuring a policy that will meet the expectations of both the policyholder and the insurer.

§ 193.01 Environmental Insurance Coverage Under Historic CGL Policies

[A] The CGL Policy's Development and Coverage of Environmental Liabilities

[1] The Creation of Environmental Liabilities

Insurance coverage for environmental liabilities can be properly understood only with an appreciation of the historical context in which the insured liabilities arose.

Hazardous waste disposal in the United States became subject to comprehensive federal regulation only when the 1976 Resource Conservation and Recovery Act (RCRA)¹ was implemented by the United States Environmental Protection Agency's Subtitle C regulations² in 1980. Earlier in the 1970s, hazardous waste disposal was regulated by the states, or not at all. Even state waste disposal regulatory programs were fairly new. Most regulation of waste disposal during the 1960s was by county health departments.

Typical disposal practices reflected the lack of regulation. The use of sanitary landfills in the United States began after World War II, and until the late 1960s, open burning dumps remained the primary disposal method for the vast majority of the nation's municipal solid waste. Throughout most of the 1970s, co-disposal of liquid and hazardous wastes, by mixing them with municipal solid waste in landfills, continued to be a practice recommended by state regulatory agencies.

Imagine, therefore, the surprise of both the manufacturing and insurance industries when, a year after RCRA, Congress enacted the Comprehensive Environmental Response, Compensation and Liability Act (CERCLA),³ an enormous unfunded federal mandate. CERCLA imposed unexpected legal liability for past, entirely lawful waste disposal. Liability under CERCLA is designed to be strict, retroactive, joint and several, unlimited and perpetual. CERCLA is, to borrow from Jeremy Bentham, a "dog law"--the method of behavioral training in which one waits for a canine to engage in undesired conduct, and then kicks it. Neither the manufacturing industry nor the insurance industry was well prepared for the legal risk.

[2] The Development of the CGL Policy

Before 1940, third-party liability insurance policies were sold to cover specific hazards, requiring the insured to purchase multiple liability policies--sometimes up to 20 separate policies⁴--to cover a myriad of potential exposures. Then, in 1940, the CGL policy was introduced by the insurance industry to cover all third-party liability upon the happening of any covered "accident." Most courts analyzing environmental liability claims under these old accident-based policies have found coverage for environmental liabilities, even if they developed gradually.⁵

Then in 1966, the CGL policy began to predicate coverage based on an "occurrence" rather than an "accident." The occurrence-based policy was the standard policy from 1966 through 1985.⁶ Although the "occurrence" definition changed over time, it generally included an accident, or injurious (or continuous or repeated) exposure to conditions that result in bodily injury or property damage (and later, personal injury)⁷ during the policy period, sometimes with the additional requirement that the injury or damage be neither expected nor intended from the standpoint of the insured.⁸ According to certain policyholder advocates, "the 'occurrence' based CGL policy sold between 1966 and 1970 without a 'pollution exclusion' was sold with the

express purpose of providing insurance coverage for 'hidden risks' including environmental risks."⁹

Yet between 1970 and 1985, domestically issued CGL policies began to expressly exclude coverage for pollution liabilities unless they were caused by a "sudden and accidental" "discharge, dispersal, release or escape" of "irritants, contaminants or pollutants."¹⁰ Similarly, coverage placed through the London market at that time began to exclude pollution liabilities under the NMA (Non-Marine Association) 1685 provision, which excepted coverage only for pollution or contamination caused by a "sudden, unintended or unexpected happening during the period of this insurance."¹¹

After 1985, the standard CGL policy was again re-written so that the pollution exclusion became arguably "absolute"¹²--excluding claims for all pollution liabilities regardless of how they were caused.

Given the historical development of the CGL policy, it is not surprising to find that some of the most valuable coverage for insureds may be the older CGL coverage without any form of pollution exclusion. Even so, policyholders and courts have nonetheless found coverage for certain environmental liabilities in all years of CGL policies.

Environmental liabilities can arise through government requests or mandates for cleanup, as well as through private party actions for negligence, strict liability, trespass or nuisance.¹³ Insureds may look to their historic CGL coverage¹⁴ (or to the policies of their predecessor or affiliated entities)¹⁵ for defense and indemnity of such liabilities. Insurance archaeology can assist insureds in finding old and missing policies,¹⁶ which may ultimately provide valuable coverage for an insured's current environmental liabilities.

[B] Choice of Law Is an Important Threshold Consideration

Coverage decisions vary from jurisdiction to jurisdiction on almost every conceivable issue, and the standard CGL policy does not contain a choice of law provision to identify which state's law will apply. As a result, any effective coverage analysis must initially consider choice of law principles. Although a full discussion of choice of law theories is outside the scope of this environmental insurance chapter, the governing law is usually determined by (1) where the contract was made (which, tends to be where the insured is located if the last act of forming the contract is delivery of the policy to the insured);¹⁷ (2) where the insured risk is located (which usually implicates the law of the site and/or the insured's residence);¹⁸ or (3) a combination approach determined by the issue at hand.¹⁹ Figuring out which state law applies, or which state law arguably applies, can make a significant difference when negotiating or litigating a coverage dispute that likely will raise any one or more of the following coverage issues.

[C] Dissecting the "Occurrence" Definition--Expectations and Intentions, Timing and Burden of Proof

In almost any environmental coverage claim, the parties will dispute whether the environmental liability satisfies the "occurrence" definition of the policy. The standard definition usually requires, in part, that the "property damage" or "bodily injury" be "neither expected nor intended from the standpoint of the insured."²⁰ To determine whether the damage or injury was expected or intended, most courts will

look to the subjective expectation or intent of the particular insured--and avoid imposing a "reasonable insured" or objective standard to the inquiry.²¹ Other courts are more willing to infer intent under an objective standard of what a reasonable insured would have expected or intended.²² Additionally, many--but not all--courts will impose the burden of proof on the insured on this issue. As a result, the insured is left proving a negative in its *prima facie* case for coverage, *i.e.*, that the injury or damage was neither expected nor intended, either from the objective or subjective standard adopted by the court.²³ At least some courts have made clear that the relevant inquiry is whether the insured expected or intended the ultimate damage, and not merely the underlying act causing the damage.²⁴

Another frequently analyzed requirement of the "occurrence" definition is what injury, damage, occurrence or event must take place during the policy period. Some occurrence definitions do not incorporate a temporal requirement of any event or damage during the policy period, but their corresponding definitions for "bodily injury" and "property damage" tie in the requirement of "injury" or "occurrence" during the policy period. Other policies define "occurrence" to require injury or damage "result[ing] during the policy period." Other policies somewhat confusingly define occurrence in a circular fashion, such that the definition itself requires an "occurrence which occurs during the policy period." Some London policies more pointedly define "occurrence" to require "one event taking place during the term of this contract."

Courts compare and contrast these various "occurrence" definitions when analyzing the proof requirements in any given case. Where the "occurrence" definition specifically requires an "event" during the policy period, courts are sometimes more willing to require the insured to show a specific release or isolated event during the policy period before environmental coverage is triggered.²⁵ Other courts nonetheless consider such language ambiguous and are willing to find coverage for ongoing gradual damage, even if the occurrence definition purports to require a specific "event" during the contract.²⁶

[D] Determining the Duty to Defend in the Context of Environmental Claims

The duty to defend is broader than the duty to indemnify, such that an insured enjoys broad defense protection for any potentially covered claim. The typical CGL policy requires an insurer to defend any "suit" seeking "damages" on account of covered property damage or bodily injury, but does not always define the term "suit" or "damages."²⁷ A commonly litigated coverage issue in environmental claims is whether a Prospective Responsible Party (PRP) letter from the U.S. Environmental Protection Agency (EPA) or similar state compliance order constitutes a "suit" seeking "damages," such that the duty to defend is triggered.

[1] Most Courts Find a PRP Letter or Compliance Request Constitutes a "Suit" Seeking "Damages," Thus Triggering the Duty to Defend

The majority of courts hold that an EPA PRP letter or similar state order constitutes a "suit" that triggers the duty to defend under a CGL policy. These courts seek to protect the reasonable expectations of the insured, which would not necessarily understand "suit" to mean only court proceedings.²⁸ Although the dictionary definition of the term "suit" includes court proceedings to enforce or recover rights or claims, not every definition of "suit" requires a court or some other similar proceeding. Thus, courts have held that PRP letters and state compliance orders are

also "suits" because they attempt to "gain an end by legal process."²⁹ Indeed, even under policies in which the term "suit" is specifically defined as "a civil proceeding," courts have found EPA PRP letters and state orders nonetheless trigger defense obligations.³⁰

Given the coercive nature of PRP letters and similar state orders, many courts determine they are "functional equivalents" of "suits" or "civil proceedings."³¹ As noted by one court:

The existence of a statutory system designed to forgo litigation, while achieving the same relief, minimizes the distinction between administrative claims and formal legal proceedings. Coverage should not depend on whether the EPA may choose to proceed with its administrative remedies or go directly to litigation."³²

In contrast, mere notification letters with no threat of enforcement, may not be considered coercive enough to constitute "suits" triggering the duty to defend.³³

Other courts may find a duty to defend an environmental claim because insurance policies are contracts of adhesion between two parties of unequal bargaining power and, as a result, ambiguities must be resolved against the insurer.³⁴ Where the meaning of the word "suit" is uncertain or capable of more than one reasonable interpretation, courts typically resolve these doubts against the knowledgeable insurer and in favor of the policyholder in the interest of fairness.³⁵

A related, and equally commonly litigated issue, is whether remedial cleanup costs constitute "damages" so that the insurer is liable for defense or ultimate indemnity. Most courts answer this question in the affirmative under one of four theories.³⁶ First, courts may find that the technical meaning of "damages" in CGL policies refers to relief sought through coercion, and thus, damages include remedial costs because an element of coercion is involved.³⁷ Second, courts may hold that under the plain and ordinary meaning of the word "damages," a reasonable insured would expect coverage for cleanup of hazardous waste unless it was explicitly excluded by the policy.³⁸ A third approach emphasizes "substance over form," and interprets "damages" to include remedial costs because, in substance, the insurer is only concerned with being reimbursed for injury to property.³⁹ Finally, some courts interpret "damages" to include remedial costs because "damages" refers to costs remedying injury for "property damage," and EPA and comparable state authorities only send out PRP letters when "property damage" occurs because of hazardous waste contamination.⁴⁰

[2] A Minority of Courts Take the Contrary View That PRP Letters Are Not "Suits" Seeking "Damages," Thus the Duty to Defend Is Not Triggered

Despite the foregoing lines of authority, at least some courts hold that a PRP letter or comparable compliance order does not constitute a "suit" triggering any duty to defend. These courts generally conclude the term "suit" clearly and unambiguously⁴¹ refers to some type of legal proceeding in a court of law.⁴² These courts may even rely on the fact that there technically is no complaint on file from which the duty to defend can be determined.⁴³

Alternatively, the court that finds no defense obligation may rationalize that, in order