MEALEY'S™ LITIGATION REPORT
Insurance

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A commentary article reprinted from the December 18, 2013 issue of Mealey's Litigation Report: Insurance

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Commentary

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Even a small sampling of 2013's leading insurance coverage decisions in the environmental realm clearly demonstrates the stark differences from state to state as to: whether injury from contaminants is really considered "pollution"; whether total and absolute pollution exclusions are just "kind of total and absolute"; how insurers spread the risk among consecutively triggered policies, and; what type of pollution a reasonable policyholder would expect to be insured. The answers to these questions, and more, are explored below in a synopsis of the leading environmental coverage cases of 2013, and a quick foreshadowing of what to look for in 2014.

I. Cases Interpreting The "Absolute" Pollution Exclusion

In 2013, courts continued to interpret the "absolute" – or "total" – pollution exclusion, often with inconsistent results. Two types of claims resulted in contradictory rulings under the absolute pollution exclusion: carbon monoxide exposure and Chinese drywall. The differing approaches and outcomes for these claims serve as a cautionary tale as to how unpredictable a landscape insureds and insurers face when dealing with "non-traditional" – but increasingly common – pollution or contamination claims.

A. Carbon Monoxide Is Not A Pollutant When It Comes From A Car, But It Is A Pollutant When It Comes From A Boiler

In ***Am. Nat. Prop. & Cas. Co. v. Wyatt*, 400 S.W.3d 417 (Mo. App. 2013)**, the Missouri Court of Appeals concluded that carbon monoxide is not a "pollutant" for purposes of the total pollution exclusion.

In *Wyatt*, the insured left a car running in her garage, resulting in her home filling with carbon monoxide, ultimately killing the insured and her granddaughter, and injuring her granddaughter's friend. The granddaughter's father filed a wrongful death suit against the insured and insurer, who issued a "Missouri Tenant's Homeowner's Policy." The injured friend's father also filed a negligence claim against the insured and insurer. In response, the insurer filed a declaratory judgment action seeking a declaration that its policy excluded coverage for such claims arising from injury caused by a "pollutant".

The court rejected the insurer's argument that the pollution exclusion applied. The court reasoned that a reasonable insured would not believe that carbon monoxide is a pollutant when it is present in typical residential-use settings. The court believed that a reasonable insured would understand the exclusion to apply

only to injury caused by an irritant or contaminant in "an industrial or environmental setting." *Wyatt*, 400 S.W.3d at 426.

By contrast, the Minnesota Supreme Court held in ***Midwest Family Mut. Ins. Co. v. Wolters*, 831 N.W.2d 628 (Minn. 2013)** that an insured's "reasonable expectations" did not apply, and that a plain interpretation of the pollution exclusion meant that carbon monoxide released in a home from a negligently-installed boiler constitutes a "pollutant" under the absolute pollution exclusion, and there is no coverage for such a claim.

In *Wolters*, the insured, a general contractor, connected a boiler to a liquid propane line in a home even though the boiler specifications were that it should operate solely on natural gas. The home's residents suffered carbon monoxide exposure and sued the insured. The trial court ruled that the pollution exclusion did not apply because no "traditional environmental pollution" occurred. However, the appellate court reversed, holding that Minnesota courts take a "non-technical, plain-meaning approach" in interpreting the pollution exclusion and, under this approach, carbon monoxide would be considered a "pollutant," thereby excluding the claim under the pollution exclusion.

On appeal, the Supreme Court of Minnesota affirmed the appellate court's decision and held that under a "plain-meaning" reading of the pollution exclusion, carbon monoxide is a "pollutant" and that the exclusion applies to the indoor release of carbon monoxide. *Wolters*, 831 N.W. 2d at 638. The court specifically refused to base its decision on whether the underlying injuries resulted from "traditional environmental pollution," stating that this approach would yield inconsistent results in determining when (or whether) the absolute pollution exclusion applies. The court further concluded that the "reasonable expectations" test did not apply here because the policy plainly designated the pollution exclusion as an exclusion and was not hidden in another part of the policy, i.e., within a definition. *Id.* at 638-39. *See also* ***Church Mut. Ins. Co. v. Clay Center Christian Church*, No. 8:11CV304, 2013 WL 683519 (D. Neb. Feb. 25, 2013)** (absolute pollution exclusion unambiguous and extends beyond traditional environmental damage under Nebraska law; carbon monoxide is therefore a "pollutant" and the absolute pollution exclusion applies to bodily injury claim, arising from exposure to carbon monoxide through home heating system.)

In summary, the two recent cases emphasize the point that even the absolute pollution exclusion is not very "absolute" in states where the application of the exclusion is measured by the reasonable expectations of an insured. *See also* ***United Fire & Cas. Co. v. Titan Contractors Service, Inc.*, No. 4:10-CV-2076 CAS, 2013 WL 316060 (E.D. Mo. Jan 28, 2013)** (pollution exclusion did not bar coverage for exposure to a chemical concrete sealant under Missouri law; reasonable insured would not expect that fumes from sealant constitute the type of "pollution" intended to be excluded.) However, in states that seek a more uniform and straightforward application of the exclusion – such as Minnesota – the absolute pollution exclusion provides a much broader protection to insurers against claims of contamination, injury, nuisance or property damage arising from "pollutants."

B. Chinese Drywall's Noxious "Off-Gassing" Is Usually Excluded "Pollution," Unless Perhaps The Insured Expected Otherwise

In ***Pro-Build Holdings, Inc. v. Travelers Prop. Cas. Co.*, No. 10-378 (Colo. Dist. Ct., Boulder Co., Oct. 4, 2013)** (Massachusetts law), a Colorado trial judge applying Massachusetts law denied summary judgment to an insurer, refusing to strictly interpret the absolute pollution exclusion and instead found a question of fact as to whether an insured reasonably expected that the gasses emitted from defective Chinese drywall constitute "pollution."

In, *Pro-Build Holdings*, Pro-Build was the successor-in-interest to the insured, who was named as a defendant in underlying lawsuits for property damage and physical injuries following the installation of defective Chinese drywall in Florida homes built by Pulte Homes, Inc. Pro-Build eventually settled with Pulte Homes and, as the successor to the insured, filed suit against the insured's excess insurer, seeking coverage for the underlying Chinese drywall claims.

In analyzing the absolute pollution exclusion under Massachusetts law, the court noted that Massachusetts law requires a fact-intensive analysis to determine

whether a substance, such as the gasses emitted from Chinese drywall, constitute a "pollutant." The court concluded that, whether a substance is a "pollutant" (thereby bringing resulting damages within the pollution exclusion) is not dependent on the substance itself, but rather upon how the substance causes damage or injury and whether a reasonable insured would classify the substance as a "pollutant." In this case, the court held that disputed issues of material fact included whether the Chinese drywall was the "pollutant" or if the "pollutant" was the gas emitted from the drywall (or both), which prevented the court from granting summary judgment in the insurer's favor.

Just six days later, in ***Prestige Properties, Inc. v. National Builders and Contractors Ins. Co.*****, No. 1:12-CV-205-HSO-RHW, 2013 WL 5592453 (S.D. Miss. Oct. 10, 2013)**, the United States District Court for the Southern District of Mississippi ruled that the "total" pollution exclusion barred coverage for claims arising from the insured's installation of Chinese drywall in a home, thereby relieving an insurer's duty to defend and indemnify.

In *Prestige Properties*, the insured was a drywall installer who was sued in 2009 by over 2,000 plaintiffs in a Louisiana class action. The homeowners alleged that the drywall was defective because the chemical components broke down and produced sulfide and noxious gases, causing corrosion and damage to personal property. The homeowners also alleged injuries from exposure to this sulfide and noxious gases, including eye irritation, sore throat, nausea, fatigue, shortness of breath, fluid in lungs and neurological harm. The insurer denied coverage, arguing that the total pollution exclusion applied to preclude coverage for injuries resulting from the drywall "off gassing."

In ruling in the insurer's favor, the court found that the sulfide and noxious gases emitted from the defective drywall were the source of damages, and that these were indeed contaminants excluded from coverage. Thus, the court held that the insurer had no duty to defend or indemnify the insured for these claims. *Prestige Properties Inc.*, 2013 WL 552453 at *7. ***See also Evanston Ins. Co. v. Germano*****, 514 Fed. App'x. 362 (4th Cir. 2013)** (Virginia law) (sulfuric gases released from Chinese drywall were "pollutants" under insurance policy and pollution exclusion applied); ***Granite State Ins. Co. v. American Bldg. Materials, Inc.*****, 504 Fed. App'x. 815 (11th Cir. 2013)** (Massachusetts and Florida law) (sulfide gas released from Chinese drywall fell within definition of "pollutant" because it was a "gaseous . . . irritant or contaminant"); ***Penn. Nat. Mut. Cas. Ins. Co. v. Snead Door, LLC*****, No. 4:12-CV-3731-VEH, 2013 WL 550483 (N.D. Ala. Feb. 12, 2013)** (Chinese drywall claims excluded under pollution exclusion).

There are a few lessons to be learned from the cases above. As demonstrated in *Pro-Build*, choice of law should not be taken for granted in pollution cases, because what may be deemed a certain case of pollution in one court could be subject to the fact-intensive "reasonable expectations" inquiry in another court. In instances where the "reasonable expectations" doctrine is afoot, insurers may find themselves defending matters they intended not to cover, while simultaneously seeking the protection of a declaratory judgment that the claim is indeed rooted in pollution that is precluded from coverage.

C. Cases In 2013 Addressing Whether Pollution Exclusion Is Limited To Only "Traditional Pollution"

A number of other cases addressed and interpreted the "absolute" or "total" pollution exclusion in 2013, including: ***Mountain States Mut. Cas. Co. v. Roinestad*****, 296 P.3d 1020 (Colo. Feb. 25, 2013)** (cooking grease constitutes "contaminant" and is therefore a "pollutant" under absolute pollution exclusion; exclusion clause in policy is in no way limited to "traditional" pollution"); ***Lapolla Industries, Inc. v. Aspen Specialty Ins. Co.*****, No. CV-12-5910, 2013 WL 4516465 (S.D.N.Y. Aug. 29. 2013)** (Texas law) (injuries arising out of installation of spray foam insulation excluded under pollution exclusion; Texas courts construe absolute pollution exclusions "clear and unambiguous in their application to exclude coverage"); ***Farm Family Cas. Co. v. Cumberland Ins. Co., Inc.*****, No. K11C-07-006, 2013 WL 5569214, ** 1, 8 (Del. Super. Oct. 2, 2013)** (lead paint considered a "pollutant" under total pollution exclusion for personal injuries from lead poisoning; "the plain language of the Policy does not expressly limit the application of the policy's total pollution exclusion to situations involving environmental pollution"); ***Village of Crestwood v. Ironshore Specialty Ins. Co.***,

986 N.E.2d 678 (Ill. App. Feb. 22, 2013) (absolute pollution exclusion applied to water contamination claims; the insured's "knowing contamination of the Crestwood water supply . . . and subsequent distribution of that contaminated combination to the community is a textbook example of 'traditional environmental pollution'"); *but see* ***120 Greenwich Development Associates, LLC v. Admiral Indem. Co.*****, No. 1:08-cv-06491 (S.D.N.Y. Sept. 25, 2013)** (underlying bodily injury claims from workers remediating World Trade Center site following September 11 attacks not precluded under pollution exclusion; claims are not environmental pollution, but instead "sound in labor law violations and negligence" and "arguably trigger Admiral's duty to defend").

D. Other Types Of Pollution Exclusions Still Alive In 2013

Not all pollution decisions center on the "total" or "absolute" exclusions. Some policies still present courts with the time-honored question of whether "sudden" means abrupt, or whether "sudden" means unexpected. This issue resides within the exception to many pollution exclusions, which provide that damages arising from pollution are not covered, unless they arise from a "sudden and accidental" discharge.

For example, in ***Narragansett Electric Co. v. American Home Assur. Co.*****, 921 F. Supp. 2d 166, 184-85 (S.D.N.Y. 2013)** (Massachusetts law), the underlying complaint alleged that residential excavation in 1984 released hazardous chemicals given rise to the claim. The court found that the releases during excavation "adequately and plausibly" alleged a "sudden and accidental" release to come within the exception to pollution exclusion under Massachusetts law, and therefore the exception to the exclusion applied and primary insurer thus had duty to defend. *See also* ***Colonial Oil Industries, Inc. v. Indian Harbor Ins. Co.*****, 528 Fed. App'x. 71 (2d Cir. 2013)** (New York law) (fuel oil seller's claim from contaminated oil in storage tank not within scope of pollution and remedial legal liability policy; coverage limited to "discharge, dispersal, release, seepage migration or escape of pollutants," and pollutants were never released into environment); *but see* ***Ross Development Corp. v. PCS Nitrogen Inc.*****, 526 Fed. App'x. 299 (4th Cir. June 6, 2013)** (South Carolina law) (pollution exclusion applied where phosphate fertilizer facility that generated by-products high in lead and arsenic due to the ordinary and routine business operations; in such an instance of routine contamination in the course of operations, the "sudden and accidental" exception to the exclusion did not apply).

II. In 2013, As Usual, Environmental Long-Tail Claims Remained The Standard-Bearer For Issues Of Allocation And Exhaustion

A. In NJ, A Guarantor Of Insolvent Insurers Need Not Participate In Allocation Until Solvent Insurers Pay Their Entire Limits

In ***Farmers Mutual Fire Ins. Co. v. New Jersey Property-Liability Ins. Guaranty Assoc.*****, 74 A.3d 860 (N.J. 2013)**, the New Jersey Supreme Court determined that a New Jersey statute creates an exception to long-established allocation law by requiring solvent insurers in long-tail environmental contamination cases to exhaust all of their own coverage before a state guaranty association for insolvent carriers is obligated to pay anything at all.

In *Farmers*, the solvent insurer, Farmers Mutual Fire Insurance Company (Farmers), paid property damage claims in two cases resulting from soil and groundwater contamination caused by a fuel leak from an underground storage tank. Farmers then sought reimbursement from the New Jersey Property-Liability Insurance Guaranty Association (NJ Guaranty), who had taken over the administration of claims for an insolvent carrier pursuant to the New Jersey Property-Liability Insurance Guaranty Association Act (PLIGA). NJ Guaranty argued that, under the PLIGA, it was not responsible to make any contributions or payments until Farmers had fully exhausted its policies' limits.

Farmers countered that, consistent with the allocation methodology in *Owens-Illinois, Inc. v. United Ins. Co.*, 650 A.2d 974 (N.J. 1994), *Sayre v. Insurance Co. of North America*, 701 A.2d 1311 (N.J. App. 1997), and the PLIGA, NJ Guaranty was required to pay the insolvent carrier's share regardless of whether the Farmers' policies were exhausted. The trial court agreed with Farmers, but the appellate court reversed, holding

that a 2004 amendment to the PLIGA expressly carved an exception under *Owens-Illinois* and overruled *Sayre*. Thus, the PLIGA now requires exhaustion of the solvent insurer's policies before NJ Guaranty is obligated to pay or contribute to the loss.

The New Jersey Supreme Court affirmed the appellate court ruling and explained that, after *Owens-Illinois* and *Sayre*, the New Jersey Legislature amended the PLIGA (and the New Jersey Surplus Lines Insurance Guaranty Fund Act, which was at issue in *Sayre*) by adding a definition of "exhaust" in continuous-trigger cases involving progressive injury and property damage. This definition provided that, in those cases, "exhaustion shall be deemed to have occurred only after a credit for the maximum limits under all other coverages, primary and excess, if applicable, issued in all other years, has been applied . . . " *Farmers*, 74 A.3d at 871. The court in *Farmers* concluded that, pursuant to this new definition, the now-amended PLIGA essentially reversed *Sayre*:

> If the Legislature were content with the *Sayre* decision – a continuous trigger case – in which the [New Jersey Surplus Lines Insurance] Guaranty Fund was required to step into the shoes of the insolvent carrier for proration purposes, there would have been little point to adding the 2004 amendments . . . defining exhaustion in cases of "continuous indivisible injury or property damage occurring over a period of years as a result of exposure to injurious conditions." It is reasonable to conclude based on the statutory language that the Legislature intended to reverse the result in *Sayre*.

Farmers, 74 A.3d at 872. Thus, the court concluded that the definition of "exhaust" as applied to the PLIGA is "clearly intended" to make the NJ Guaranty "the insurer of last resort in triggered years in long-tail environmental contamination claims," *Id.* at 873, and the PLIGA "specifically exempts" the NJ Guaranty "from the *Owens-Illinois* allocation scheme until all solvent insurance companies' policy limits are exhausted." *Id.* at 863.

It is not an uncommon issue in long-tail insurance disputes that there exist some years of insolvent coverage. Whether or not a state guaranty fund participates in an allocation, or whether that fund is a payor of last resort, is a frequent and unclear issue. Courts following the lead of the New Jersey legislature may bring clarity to this issue through statutory amendments, and such clarity may increase the coverage burden on those solvent insurers handling such a claim.

B. In California, The Insured Can Stack Primary Limits, Unless The Primary Policies Prohibit It—Which Could Be Problematic For Excess Insurers

In 2013, appellate courts in Wisconsin and California addressed exhaustion and allocation issues. While both of these cases involved asbestos liabilities, these decisions may have ramifications in many types of long-tail environmental claims.

In ***Kaiser Cement and Gypsum Corp. v. Ins. Co. of the State of Pennsylvania*, 155 Cal. Rptr. 3d 283 (Cal. App. 2013)**, ***rehearing denied*** **(May 1, 2013)**, ***review denied and ordered not to be officially published*** **(Jul. 17, 2013)**, the California appellate court found that: a) while an insured could conceivably "stack" multiple years of primary coverage in California, such "stacking" was not allowed where the primary policies had "anti-stacking language"; and, b) an excess insurer's requirement that it pays only once "all other collectible" insurance is exhausted could find itself robbed of the benefit of horizontal exhaustion if the primary policies contain "anti-stacking" language.

Truck Insurance Exchange (Truck) issued primary coverage to Kaiser Cement and Gypsum Corporation (Kaiser) from 1964 to 1983. Many claimants who alleged exposure to asbestos had 1974 as the common year of exposure, so Kaiser initially selected 1974 as the policy to respond to any claimant because there was $500,000 in coverage per claimant, with no aggregate. Once Truck paid $500,000 for a claimant who was injured/exposed in 1974, it was unclear which insurer was then responsible for the next dollar paid to that claimant: Insurance Company of the State of Pennsylvania (ICSOP), the excess insurer in 1974, or Truck for remaining primary limits existing in years other than 1974?

The appellate court found that the Truck primary policies did have anti-stacking language, because each Truck policy promised to pay only $500,000 per

occurrence – not per year or per policy. The Truck policies also stated that the Truck limits "as respects any one occurrence involving one or any combinations of the hazards or perils insured against shall not exceed the per occurrence limit." The appellate court found that, because of this "anti-stacking language," although many years of Truck primary insurance were triggered by a particular claimant, Truck need only pay one policy's per occurrence limit, which in this case was the selected 1974 year.

The next issue in *Kaiser Cement* was the extent to which the 1974 ICSOP excess policy is impacted by the fact that Kaiser Cement could not stack the available Truck limits for a particular claimant. The ISCOP excess policy stated that it is triggered upon exhaustion of the "retained limit." The "retained limit" includes: a) the limit of the underlying insurance; b) plus any other underlying collectible insurance. This language, coupled with precedent in *Community Redevelopment v. Aetna*, 57 Cal. Rptr. 2d 755 (Cal. App. 1996), led the court to initially conclude that an excess insurer in California is not triggered until all collectible triggered primary coverage is exhausted (i.e. horizontal exhaustion), which is a positive result for excess insurers in California, although not for primary insurers.

The problem that "horizontal exhaustion" created in *Kaiser* was that, when the court examined what other "collectible" insurance existed on the primary level, it seemed that the "anti-stacking" language in the Truck policies made only one single Truck policy truly "collectible." Therefore, the court found that, for any individual claimant, the ICSOP excess policy was required to indemnify once the Truck primary policy in 1974 paid $500,000, because there simply was no other "valid and collectible" insurance available from the other triggered policy years.

While this decision was "de-published" and can no longer be cited as California precedent, this decision demonstrates a problem for excess insurers because an excess insurer's horizontal exhaustion language (i.e. "over all other valid and collectible insurance") can effectively become negated by the anti-stacking language of the underlying primary insurer (i.e. "any of our coverage for this occurrence in other years doesn't count as valid or collectible").

See also ***Cleaver-Brooks, Inc. v. AIU Ins. Co.*****, No. 2013AP203, 2013 WL 5788583 (Wis. App. Oct. 29, 2013)** (under "joint and several" liability and Wisconsin law, insured may choose coverage from multiple insurers "simultaneously" for all triggered coverage for asbestos liabilities, rather than separately, or "sequentially," from each insurer, to maximize coverage for defense and indemnity costs from excess insurers).

C. Allocation: Missouri Leans "All-Sums" In 2013, While Massachusetts Reaffirms "Pro Rata"

On April 16, 2013, the Missouri Court of Appeals in ***Doe Run Resources Corp. v. Certain Underwriters at Lloyd's, London*****, 400 S.W.3d 463 (Mo. App. 2013)** applied Missouri law in concluding that an "all sums" allocation method would apply to environmental claims arising out of the insured's mining, milling and smelting operations at six sites located in and around Missouri. The insured's operations, which started in the late 1800s at one site and early- to mid-1900s at the other sites, generated lead-containing wastes called "chat piles" and "tailings ponds" on each site. Wind and water erosion caused lead and other materials to migrate from these sites onto neighboring properties. The United States Environmental Protection Agency held the insured liable for the waste and required it to investigate and remediate those areas and ultimately prevent further offsite migration.

The insured sought coverage from London Market Insurers (LMI), who had issued seven excess insurance policies covering the period from 1952 through 1961. When LMI did not respond to the insured's request for coverage, the insured sued LMI in Missouri state court. Prior to trial, the court held that New York law would apply, which utilizes a pro rata allocation method. This allocation method would apply to this case over the entire period during active pollution and passive migration occurred. At trial, the jury determined that the period of contamination took place from the time of operation (between 1894 and 1936, depending on the site) through 2011 (time of trial). The jury awarded the insured over $62 million in environmental damages. Pursuant to the pro rata allocation method, LMI's share of the insured's costs totaled just over $5 million, less than ten percent of the total damages.

One issue on appeal was whether the trial court was correct in ruling that "pro rata" allocation would apply

to the insured's environmental response costs. While not citing one allocation decision in rendering its ruling, the Missouri Court of Appeals opined that, under Missouri law, "the plain language of the applicable insurance policies require the adoption of the 'all sums' allocation scheme in this case." *Doe Run*, 400 S.W.3d at 474. The *Doe Run* court focused on the "ultimate net loss" and "occurrence" definitions and the term "all sums" in reaching its decision. Some policies at issue defined "ultimate net loss" as "the *total sum* which the assured . . . becomes obligated to pay by reason of personal injury or property damage claims . . . as a consequence of any occurrence covered hereunder." *Id.* at 474 (emphasis in original). Other policies stated that LMI agreed "to indemnify the insured for *all sums* which the Assured shall be obligated to pay by reason of the liability . . . for damages . . . on account of property damage, caused by or arising out of an occurrence happening during the policy period." *Id.* at 475 (emphasis in original). "Occurrence" was defined as "one happening or series of happenings, arising out of, or due to one event taking place during the term of this policy." *Id.* The court therefore concluded, "This definition does not limit the policies' promise to pay all sums of the policy holder's liability solely to damage during the policy period. We must construe the policy as written and cannot rewrite the policy for the parties." *Id.* at 475.

In other allocation and exhaustion decisions from 2013, two courts applied the Massachusetts Supreme Court's pro rata allocation ruling in *Boston Gas Co. v. Century Indem. Co.*, 910 N.E.2d 290 (Mass. 2009) to reaffirm the state's application of pro rata allocation to environmental claims. In ***Boston Gas Co. v. Century Indem. Co.*, 708 F.3d 254 (1st Cir. Jan. 18, 2013)** (Massachusetts law) the First Circuit Court of Appeals applied the *Boston Gas* ruling to an underlying trial involving manufactured gas plant sites. The appellate court affirmed the district court's determination that property damage was continuous from the beginning of operations through the date of remediation (1886 through 2007), and thus, pursuant to the pro rata allocation ruling in *Boston Gas*, the court would allocate damages evenly over those years. In ***Graphic Arts Mut. Ins. Co. v. D.N. Lukens, Inc.*, No. 11-cv-10460-TSH, 2013 WL 2384333 (D. Mass. May 29, 2013)** (Massachusetts law), the court also held that the pro-rata allocation ruling from *Boston Gas* would apply to underlying toxic tort claims against the insured (asbestos and chemical/toxic metal exposure cases), and that a "continuous trigger" would apply to determine when the injuries occurred, "thereby obligating Lukens to pay its proportionate share of any judgment entered." *D.N. Lukens*, 2013 WL 2384333 at *5.

III. Environmental Cases Addressing Other Significant Issues

Other cases decided in 2013 addressed certain issues that were typical of environmental coverage actions past, present and future. These issues include choice of law, what constitutes an "occurrence," the number of occurrences, and what constitutes "damages." We summarize key decisions below.

A. Choice of Law: Place Of Contracting Or Location Of Contamination?

In ***Northern Assur. Co. of America v. Thomson, Inc.*, 996 N.E.2d 785 (Ind. App. 2013)**, the court found that the most significant contacts test required application of the law where the contaminated sites are located, not where the party making the insurance claim is located.

Although the original insured was located in California, the insured's successor company was located in Indiana, where the insured filed a lawsuit seeking coverage for environmental cleanup costs at three sites – two in California and one in the United Kingdom. The insured's decision to file in Indiana was indeed strategic, given that Indiana law would treat environmental response costs as insurable "damages," whereas California law would likely not treat such response costs as insurable "damages."

In analyzing choice of law, the Indiana appellate court utilized Indiana's choice of law rules, which apply the law of the jurisdiction with the "most intimate contact" or "most significant relationships" to the subject matter of the dispute, pursuant to Restatement (Second) of Conflict of Laws, § 188. Under this approach, the Indiana appellate court concluded that the law of California, where the original policies were issued and where two of the sites were located, had the "most intimate contact" to the action. The court downplayed the factor that the insured's successor company was in Indiana, explaining that the insured's assets (and liabilities) were acquired in 2000, "decades after the policies were issued and years after most of the alleged pollution would have occurred." *Thomson*, 996 N.E.2d at 797.

See also, ***Doe Run Resources Corp v. Certain Underwriters at Lloyd's London*, 400 S.W.3d 463, 472-74 (Mo. App. 2013)** (law of Missouri applied because the insured's operations and the underlying sites were located there); ***Narragansett Electric Co. v. American Home Assur. Co.*, 921 F. Supp. 2d 166, 179-80 (S.D.N.Y. 2013)** (although insured was a Rhode Island public entity with its principal place of business in Rhode Island, primary policy issued to several affiliated corporations identified one Massachusetts address; under New York's choice of law rules, Massachusetts was the principal location of the insured risk and the "balance of contacts" supported the application of Massachusetts law to an environmental coverage action involving contamination at a manufactured gas plant facility).

B. Trigger: Property Damage Triggers Coverage When It Occurs, Not When It Is Discovered

In ***Narragansett Electric Co. v. American Home Assur. Co.*, 921 F. Supp. 2d 166 (S.D.N.Y. 2013)**, the U.S. District Court for the Southern District of New York held that the particular definition of "occurrence" at issue required only for the property damage to be caused during the policy period, and not that the property damage be discovered during the period.

In *Narragansett Electric*, the Commonwealth of Massachusetts filed suit against the insured, the Narragansett Electric Company (Narragansett) in 1987, alleging that Narragansett's predecessor and other defendants were strictly liable for property damage caused by the release of hazardous substances at a site located in Attleboro, Massachusetts. The Commonwealth claimed that the insured's predecessor generated thousands of tons of by-products and wastes from its production of manufactured gas between the 1890s and 1950s.

In its lawsuit seeking coverage from its primary insurer that issued coverage in 1985 for defense and indemnity, and its excess carriers that issued coverage generally between 1945 and 1986 for indemnity, Narragansett argued that property damage occurred at the site during each year between 1945 and 1986. The primary insurer denied coverage, arguing that, even assuming the underlying lawsuit may have alleged damage during its policy period, its pollution exclusion precluded coverage for the underlying lawsuit, and filed a motion to dismiss the insured's amended complaint. The excess insurers also filed a motion to dismiss the insured's amended complaint, arguing that the underlying claim did not constitute an "occurrence" that would trigger their policies' duty to indemnify.

With respect to the primary insurer's duty to defend, the policy defined "occurrence" as "an accident, including continuous or repeated exposure to conditions, which results in bodily injury or property damage neither expected nor intended from the standpoint of the Insured." *Narragansett Electric*, 921 F. Supp. 2d at 181. Analyzing this language with the underlying action's allegations, the court held that, under Massachusetts law, "property damage need not be discovered or manifested during the policy period for there to be an 'occurrence' under the policy language . . . Rather, the inquiry is whether the property damage, as defined in the policy, 'occurred' within the policy period and within the meaning of the word 'occurrence'." *Id.* (internal citations omitted). The court concluded that the primary insurer did not dispute that the underlying action alleged damage occurring during its policy period. *Id.*

Regarding whether the excess insurers had a duty to indemnify, the court noted that these policies defined "occurrence" as "one happening or series of happenings, arising out of or due to one event taking place during the term of this contract." *Id.* at 187. In interpreting this definition, the court determined that the excess policies required the insured to "plausibly allege a causative event, which occurred during an applicable policy period." *Id.* The court noted that under Massachusetts, Rhode Island or New York law, the policy language "requires a causative event other than property damage during the policy period." *Id.* The insured argued that the migration of environmental contamination was due to events, including the release of contaminants, from the following: (1) dissolution and breakdown of the chemical components of waste materials during the policy period; (2) sand and gravel quarry operations during the policy period; and/or (3) residential excavation during the policy period. While the court was not persuaded that the first possibility sufficiently alleged an "event" under the policy period, it was satisfied that "excavation activities" via sand and gravel operations or residential operations were distinct events from property damage. The court therefore concluded that "releases of hazardous substances during excavation

operations plausibly allege events under the [excess insurer] policies at the motion to dismiss phase." *Id.* at 190.

C. An Insured's Institutional Contamination Problem At Multiple Sites, Over Time, Can Constitute A Single "Occurrence"

In ***Certain Underwriters at Lloyd's, London v. Southern Natural Gas Co.*, Nos. 1110698 and 1110769, 2013 WL 3242933 (Ala., June 28, 2013)**, the Alabama Supreme Court held that a single chain of causation, even causing multiple and disparate injuries, constitutes one occurrence.

In *Southern Natural Gas*, the insured learned in 1989 that a lubricating oil used in its air-compressor engines at compressor stations along a natural gas pipeline contained polychlorinated biphenyl, or PCBs. The insured sought coverage from its excess and umbrella insurer, London Market Insurers (LMI), who issued policies from 1949 through 1987. LMI argued, *inter alia*, that the PCB contamination occurring at different compressor stations at different times constituted multiple occurrences under LMI's policies, thereby requiring the insured to satisfy a separate retention for each instance of contamination. The insured argued that, because the pipeline contamination resulted from its "integrated operations" at all the compressor stations, it could all be treated as a single occurrence.

The trial court entered an order finding that, "the PCB-remediation program constituted a single occurrence under the policies." *Southern Natural Gas*, 2013 WL 3242933 at *10. While the court noted that evidence at trial indicated that some compressor stations had traces of PCBs in different places, it also noted that, pursuant to *United States Fire Ins. Co. v. Safeco Ins. Co.*, 444 So.2d 844, 846 (Ala. 1983), the definition of "occurrence" could have "multiple and disparate impacts on individuals and that injuries may extend over time," but unless there is a "separate, intervening cause" to "break the chain of causation," there would only be one "occurrence." *Id.* at *14. The Alabama Supreme Court concluded, "[b]ased on the arguments before us, we cannot say that there was a separate intervening cause" to support a finding of more than one "occurrence." *Id.* at *17.

D. Remediation To Prevent Further Environmental Harm Constitutes Insurable "Damages"

Also in ***Certain Underwriters at Lloyd's, London v. Southern Natural Gas Co.*, Nos. 1110698 and 1110769, 2013 WL 3242933 (Ala., June 28, 2013)**, the court found that the insured's self-imposed remedial activities at the compressor stations to prevent further migration of the PCBs into the groundwater constituted insurable "damages" for which the insured was legally liable.

In *Southern Natural Gas* the insurers, LMI, argued that the insured's self-motivated cleanup costs were not "damages" the insured was legally obligated to pay because the expenditures were not the result of any order by a state or federal agency. The Alabama Supreme Court held that environmental-remediation costs were indeed damages the insured was legally obligated to pay. The court also noted that the insured presented evidence at trial that it was required under federal law to report PCB contamination to the United States Environmental Protection Agency, and that the Mississippi Commission on Environmental Quality had required Sonat to clean up the compressor stations in Mississippi. Additionally, the court noted LMI asserted, as an affirmative defense, that the insured had failed to mitigate or minimize damage, which conflicted with its argument that these remedial costs do not constitute "damages." The court concluded that the insured "presented evidence indicating that it had a legal obligation to remediate the PCB contamination at its compressor sites, and we will not limit its damages to those arising out of a suit, claim or action by a third party." *Southern Natural Gas*, 2013 WL 3242933 at *22.

Other 2013 decisions addressing what expenditures constitute "damages" include: ***Northern Assur. Co. of America v. Thomson, Inc.*, 996 N.E.2d 785, 799 (Ind. App. 2013)** (under California law, "damages" limited to "money damages ordered by a court and do not include expenses incurred as a result of responding to the cleanup orders of an administrative agency;" insurer therefore not required to indemnify insured); *But see*, ***Siltronic Corp. v. Employers Ins. Co. of Wausau*, 921 F. Supp. 2d 1099, 1109 (D. Or. 2013)** (primary insurer's payments to state and federal environmental

agencies are deemed a "payment of judgments or settlements" to exhaust that insurer's policy limits).

IV. Crystal Ball: Environmental Issues To Watch For In 2014

A. Fracking Claims: Fallacy Or Finally Here?

Hydraulic fracturing – or "fracking" – involves the fracturing (drilling) of pressurized liquid into rock, such as shale rock, to release natural gas and oil. The pressurized liquid is a mix of water, chemicals and sand or gravel. With low costs associated with fracking, as opposed to other means to access natural gas, these operations will continue to increase. For example, in 2012, shale gas (i.e., from fracking) accounted for 39% of all natural gas produced in the United States. Additionally, natural gas production in the United States has increased more than 30% since 2005 and this production is estimated to increase by 44% between 2011 and 2040, primarily due to fracking.

As the fracking industry in the United States expands its operations in 2014, the scope of liabilities arising from this activity is expected to increase. Of course, as these liabilities increase, so too will the scope of insurance coverage challenges arising from fracking. We discuss below the types of fracking liabilities we expect to see in 2014, as well as one insurance dispute that already arose and other coverage issues that may be on the horizon.

1. Expected Liabilities Arising From Fracking

Oil and gas companies are the obvious targets of fracking claims and lawsuits, as they are the companies primarily involved in fracking operations. However, it is not only oil and gas companies that face potential liability related to fracking. In addition to oil and gas companies, other parties that may be the target of legal claims arising from fracking include: (1) contractors and subcontractors of the oil companies, for negligent construction or installation of wells and other equipment used in fracking; (2) property owners, lease holders and site operators, for damage or injury on or to the property and lease disputes (including unfair leasing practices, insufficient rent/royalties and lack of protection from lawsuits against property owners); (3) transporters of materials used in fracking, for injuries sustained in or related to transporting those fracking-related materials; and (4) manufacturers of those materials and tools used in the fracking process, for product liability claims. In addition to these typical tort or contact lawsuits arising from fracking operations, we also expect a series of claims alleging the fracking industry of having a significant detrimental impact on the environment.

Although the claims mentioned above are the most common claims expected to arise from fracking, there may be a very significant new type of claim coming to the table. Within recent months, plaintiffs claim to have established a causal link between fracking operations and earthquakes deep below the earth's surface. Of course, these intermittent earthquakes result in property damage and lawsuits. In 2010 and 2011, the town of Greenbrier, Arkansas experienced over 1,000 minor earthquakes, which scientists from the University of Memphis and the Arkansas Geological Survey concluded may have been caused by the disposal of wastewater from fracking into deep underground wells. This conclusion prompted the Arkansas Oil and Gas Commission to shut down several wells in the area, and the earthquakes ultimately ceased. Armed with a potential causal connection, a number of landowners have filed lawsuits in Arkansas federal court alleging property damage to homes in central Arkansas from these earthquakes caused by the disposal of the leftover toxic water.[1] These cases are currently in settlement negotiations, with a trial date scheduled in 2014.

Earthquakes might not be the only new or novel liability associated with fracking in 2014. Other recent fracking-related litigation has seen the oil and gas industry suing local municipalities to challenge those municipalities' constitutional powers to pass ordinances that effectively ban fracking. For example, in the state of New York, anti-fracking resolutions or ordinances have been passed in over 100 municipalities. Elsewhere, large cities such as Pittsburgh and Detroit have banned fracking. Dryden, New York, a town outside of Ithaca, had passed such a zoning ordinance in 2010, which prompted an oil and gas company to file suit challenging the ordinance. To date, the lower courts sided with Dryden, ruling that it is within the town's rights to pass such an ordinance. However, New York's highest court – the Court of Appeals – agreed in August to hear the Dryden case, along with another fracking ban passed in Middlefield, New York. Additionally,

in Mora, New Mexico a community rights ordinance banning oil and gas drilling was recently passed, resulting in private property owners and the Independent Petroleum Producers of New Mexico filing suit in federal district court in November 2013 challenging this ordinance.

2. Coverage Issues Related To Fracking

The interpretation and application of the pollution exclusion is but one example of an insurance coverage dispute that will arise from fracking. The drilling method in fracking injects a mixture of water, chemicals and sand under high pressure to crack shale rock and release the natural gas. To date, the fracking industry has been circumspect regarding the formulation of the chemicals used in the fracking process.

As in other "pollution exclusion"-related cases, parties may soon ask courts to determine whether this fracking mixture is considered a "pollutant" for the pollution exclusion to apply. While the actual chemical component in the drilling mixture is very small, the insurers may be able to convince a court that the pollution exclusion still applies, especially depending on the underlying claim and alleged damage, such as environmental pollution. Additionally, whether the pollution took place suddenly or gradually may determine whether a time-element pollution exclusion applies, as those exclusions bar coverage if an "occurrence" is not reported within a specific time period (i.e., thirty days, ninety days, etc.). *See, e.g.* ***Starr Indem. & Liab. Co. v. SGS Petroleum Serv. Corp.*****, 719 F.3d 700, 705 (5th Cir. 2013) (Texas law)** (insurer absolved of coverage for clean-up costs from an accidental chemical release because insured failed to comply with the thirty-day notice requirement under pollution exclusion endorsement; insurer did not need to show prejudice under this "specifically negotiated" pollution buy-back endorsement).

To date, one insurance coverage lawsuit has been filed related to fracking and the pollution exclusion. In ***Warren Drilling Co., Inc. v. Ace American Ins. Co.*****, No. 2:12-cv-425 (S.D. Ohio, filed Apr. 13, 2012)**, the insured, a drilling company, sued its insurer for refusing to defend or indemnify the company after drilling activities allegedly contaminated a nearby homeowner's water well. The policy at issue was a standard Commercial General Liability (CGL) policy that also included an Energy Pollution Liability Extension (EPLE) endorsement and an Underground Resources and Equipment Coverage (UREC) endorsement. Although the CGL policy in question excluded coverage for bodily injury or property damage caused by "pollutants," the EPLE endorsement reinstated coverage for a pollution incident where certain conditions are met, such as the discharge of pollutants being unexpected and unintended; the discharge commencing abruptly and instantaneously and at or from a site owned/occupied by or where the insured was performing operations; the insured knowing within 30 days of the commencement of the discharge; and the insured reporting to the insurer within 60 days of the commencement of the discharge. Citing to both of these endorsements, the insured argued that the insurer breached its contract and acted in bad faith by denying coverage for the underlying claim. Although the insurer and insured ultimately settled their dispute in early 2013 before the parties litigated any coverage issues, this scenario is ripe for similar litigation.

In addition to the pollution exclusion, other general liability insurance coverage issues that may involve fracking claims include whether the claim constitutes an "occurrence" (including whether the claim was "expected or intended," or an "accident" or "event"), whether an owned-property exclusion applies, and the timing and notice of these fracking claims to insurers. Future coverage issues that will likely arise under general liability long-tail environmental claims related to fracking include the number of occurrences, trigger and allocation. Other than general liability insurance, fracking claims may also implicate workers' compensation insurance, first-party/business interruption insurance, and directors and officers insurance. As fracking claims for coverage develop in 2014 and beyond, there may be a response by underwriters by drafting and issuing endorsements limiting or barring such coverage in the future, as was the industry's response to previous claims such as mold and Chinese drywall.

B. Other Environmental Decisions On The Horizon For 2014

The United States District Court for the Southern District of New York heard arguments in 2013 regarding whether a pollution exclusion for underlying chemical exposure claims applies in ***Ace American Ins. Co. v. GrafTech International Ltd.*****, No. 1:12-cv-6355**

(S.D.N.Y.). The insurers filed a motion for summary judgment, arguing that they have no duty to cover these underlying claims because the damages would never reach the insurance policies at issue, and that the claims are barred under a pollution exclusion. The insured countered that only one policy period is at issue, and the pollution exclusion applies to "traditional environmental pollution," which is not the case here.

The insured, GrafTech International Ltd. (GrafTech), sought coverage from its insurers for costs in defending numerous cases alleging hazardous toxic and chemical exposure from GrafTech's products at various smelting facilities between 1942 and 2012. The insurers first argued that, under either New York or Connecticut law, pro rata allocation would spread GrafTech's damages over a 70-year period, and that GrafTech has not proven that it has exhausted its deductibles or underlying insurance to trigger the insurers' policies, which were issued between 1991 and 2007. Alternatively, the insurers argued that each of the policies issued between 1997 and 2007 contain an "absolute" pollution exclusion that would preclude coverage for the underlying claims. The exclusion bars coverage for claims arising out of the "actual, alleged or potential presence in or introduction into the environment of any substance if such substance has, or is alleged to have, the effect of making the environment impure, harmful or dangerous." The policies further define "environment" as "any air, land, structure or the air therein, watercourse or water, including underground water."

Another highly anticipated ruling in 2014 with possible nationwide significance to environmental law and subsequent insurance coverage litigation is in the matter, ***Chubb Custom Insurance Co. v. Space Systems/Loral Inc.*** Chubb Custom Insurance Company (Chubb) filed a Writ of Certiorari to the United States Supreme Court in September, requesting the Court to hear arguments related to an insurer's right to seek recovery via subrogation lawsuits under the Comprehensive Environmental Response, Compensation and Liability Act (CERCLA). Chubb seeks reversal of a Ninth Circuit dismissal of Chubb's claims for damages against Ford Motor Company, Chevron Corp. and other former owners of a contaminated parcel of land that Chubb paid to remediate on behalf of its policyholder, Taube-Koret Campus for Jewish Life.

In its writ, Chubb contends that the Ninth Circuit erred in dismissing its subrogation claims under CERCLA, arguing that its insured would have been entitled to sue the other parties had it not received payment from Chubb. The Ninth Circuit affirmed the district court's dismissal of Chubb's lawsuit, claiming that Chubb did not directly incur environmental response costs and that subrogation law does not apply to the section of CERCLA Chubb sued. Chubb argues in its Writ that the courts failing to recognize insurer's subrogee rights will force environmental remediation litigation to take longer and become more complicated.

V. Conclusion

The year 2013 has been another busy year with significant decisions affecting both policyholders and insurers alike. States continue to diverge on issues such as what constitutes a "pollutant," and whether a "pro rata" or "all sums" allocation method is appropriate in spreading a risk in long-tail environmental claims. These issues are not disappearing in the near future, and courts may soon be interpreting these same policy terms in different arenas, such as fracking. Once again, the area of environmental coverage allows claims personnel and coverage counsel alike to learn from the past lessons of case law, which continue to be applied to form and shape the future.

Endnote

1. *See, e.g.*, *Miller, et al. v. Chesapeake Operating Inc., et al., Case No. 4:13-cv-131 (E.D. Ark)*; *Thomas, et al. v. Chesapeake Operating Inc., et al., Case NO. 4:13-cv-182 (E.D. Ark.)*; *Sutterfield, et al. v. Chesapeake Operating Inc., et al., Case No. 4:13-cv-183 (E.D. Ark.)*; and *Mahan, et al. v. Chesapeake Operating Inc., et al., Case No. 4:13-cv-184 (E.D. Ark.)*. ■

MEALEY'S LITIGATION REPORT: INSURANCE
edited by Gina Cappello
The Report is produced four times a month by

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Email: mealeyinfo@lexisnexis.com
Web site: http://www.lexisnexis.com/mealeys
ISSN 8755-9005