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Identifying, Avoiding, Mitigating, and Insuring Environmental Risk in Construction

Common Environmental Hazards in Real Estate and Development Projects

The construction industry is fraught with environmental hazards that can expose owners, developers, and contractors to unexpected loss. These risks are not limited to remediation firms or work on Brownfields sites. Environmental risks exist on all construction projects. Over the past 50 years, as the construction industry had continuously faced new environmental exposures insurers have continuously developed new policy language to limit coverage. Recently, the market has changed and environmental products are available, but they differ in many areas. Understanding the environmental insurance coverage options available on the market today is a crucial step towards maximizing insurance recovery when faced with these exposures.

Many of today's environmental exposures have been continuously litigated between the construction industry and insurers since the beginning of environmental insurance coverage law. Asbestos, for example, is still common in environmental insurance coverage litigation, regularly appearing in demolition and renovation projects. Polychlorinated Biphenyls ("PCBs"), a toxic compound that has been found to cause cancer, were extremely common in many facets of construction, including such foundational components as caulk, and continue to be a subject of litigation today. Legionella and mold, which are implicated any time a worker opens a wall or works on a water, heating, or cooling system, have both been a major insurance coverage issue for decades. Numerous occupational hazards have, and will likely always constitute, common environmental exposures in the construction industry. These can include incidents involving things like airborne contaminants, lead poisoning, Chinese drywall, and fume inhalation. Although all of these problems have been litigated for decades now, there are still new issues arising from them with respect to insurance coverage.

Ultimately, the massive amount of possible environmental exposures create too many unknowns. Construction industry players should always consider what coverage they have and what coverage they need.

Development of Environmental Insurance Coverage

As of the late 1960s, Comprehensive General Liability ("CGL") policies generally covered any unintended pollution damage, subject to minimal exclusions. That changed dramatically with the passage of the Resource Conservation and Recovery Act (RCRA) and the Comprehensive Environmental Response, Compensation and Liability Act (CERCLA). Together, these laws essentially imposed joint and several liability for cleanup costs on anyone involved, regardless of fault or cost. This meant that anyone involved could be held responsible for the entire cleanup cost.

Insurers were obviously shocked when they started getting claims from policyholders for costs of cleaning up their mess after getting away with doing so for nearly a century. Still, the CGL policy at the time appeared to grant coverage for these costs. The first attempt to limit this coverage quickly appeared in the form of the "standard pollution exclusion," which eliminated coverage for a significant portion of environmental exposures, but permitted coverage when the pollution-related loss was "sudden and accidental." Although it was welcome news to policyholders, insurers were quickly dismayed when they found out that many courts found this "sudden and accidental" language to be ambiguous, thereby granting coverage.

The insurers were distraught to figure out what to do with so much exposure, so they made a second attempt to limit coverage, called the "absolute pollution exclusion." The most significant difference was the elimination of the "sudden and accidental" exception to the exclusion. This blow to coverage obviously created significant coverage gaps for policyholders, who subsequently demanded a product that would cover their environmental exposures. Insurers responded with stand-alone policies that could pick up the excluded coverage, resulting in the development of the Pollution Liability policy. The absolute pollution exclusion is still found in the CGL today.

General Liability Insurance Coverage for Environmental Hazards

Although environmental coverage law has evolved significantly, the General Liability policy continues to be a major source of recovery for policyholders. General Liability policies begin with a first-page coverage grant for, essentially, any accident that causes bodily injury or property damage, followed by 14 pages of exclusions and conditions. Historically, as insurers have been faced with new events that cause a major shift in claims, they have added exclusions to bar coverage for these events and then eventually modified them as actuaries figured out how to better manage coverage in that area. The development of the pollution, absolute pollution, and total pollution exclusions are perfect examples of this practice. Understanding these exclusions is a crucial first step in determining what coverage you have and what additional coverage you may need.

The pollution exclusion, in its original form, states that:

> the policy does not apply to: bodily injury or property damage arising out of the discharge, dispersal, release or escape of smoke, vapor, soot fumes, acids, alkalis,

> toxic chemicals, liquids or gases, waste materials or other irritants, contaminant or pollutants into or upon the land, the atmosphere or any water course or body of water, but this exclusion does not apply if such a discharge, dispersal, release or escape is sudden and accidental.

The "sudden and accidental" language at the end of the exclusion has led to a significant body of litigation over its lifetime. Courts were unsettled with regards to whether the language meant "unintended and unforeseen" or "abrupt," in a temporal sense.

In 1970, the insurance industry proposed the pollution exclusion to states' insurance officials as a way to clarify the definition of occurrence with respect to polluting and make it clear that intentional polluters were not covered under General Liability policies. This original proposition clearly did not stand the test of time, as insurers quickly moved to use the exclusion as broadly as possible, particularly with the advent of the RCRA and CERCLA and the massive claims that resulted from them. When insurers realized they could not exclude coverage as broadly as they wished they overhauled the exclusion, developing the absolute pollution exclusion in its place.

The absolute pollution exclusion, which is standard on all post-1986 ISO CGL forms, is something of a misnomer. It does not exclude all pollution coverage and, therefore, is obviously not "absolute." It is, however, more limiting than the standard pollution exclusion. Although it is more limited than the original, this exclusion, found as exclusion f in the ISO CGL, actually has five components that limit the bar it places on coverage. These include exceptions, wording nuances, and various requirements for the exclusion to operate.

Primarily, there must be an actual "pollutant." This has been a major source of litigation surrounding the exclusion. Many jurisdictions have considered a very wide variety of substances and their statuses as pollutants, but there is still an extremely vast array of jurisdictions and substances that have not crossed paths. With few exceptions, almost anything you can think of as a form of pollution has probably been ruled a "pollutant" by a court somewhere in this country. Perhaps the better question to ask is "what is not a pollutant?"

It may also be important whether the pollutant caused damage in its capacity as a pollutant. For example, in Incorporated Village of Cedarhurst v. Hanover Ins. Co., damage was caused by a pollutant, but not in its capacity as such. There, a "rush of water and sewage" from the town sewage system caused "massive flooding" to a town resident's basement. The plaintiff alleged that a flooding overflow was the cause of the damage, as opposed to the sewage itself. The court held the exclusion did not apply.

Another issue stemming from the absolute pollution exclusion that has surfaced in litigation is whether the insured has to be the party that is the actual polluter. In Town of Harrison v. National Union Fire Ins. Co., the New York Court of Appeals determined that "the language of the pollution exclusion[] does not require that the insured town be the actual polluter in order for the exclusion to apply." The insured was denied coverage for failing "to prevent and abate the illegal disposal of noxious waste on [landowners'] land by an excavation contractor

retained by [those] landowners to regrade their properties." Denying coverage for such passive behavior is a large blow to policyholders.

Since there is really no instance where an insurer would say there is too little coverage for something, insurers also developed a total pollution exclusion. This exclusion "[e]liminates virtually all coverage for pollution incidents." This exclusion has three variants. Each is based on a removal of coverage for bodily injury or property damage that "would not have occurred, in whole or in part, but for" a pollution incident. The first, which states simply that, should be avoided at all costs, as should the second, which contains a minor exception for damage caused by smoke, heat, or flames from a hostile fire. Although all three should be avoided, if the insurer insists on the inclusion of one, the third, which has the hostile fire exception as well as an exception for bodily injury from defective heating equipment, is slightly better than the other two.

In short, since the standard pollution exclusion is unlikely to be available at this point, a CGL policyholder in the construction industry should look to avoid the total pollution exclusion endorsement at all costs, in favor of the regular absolute pollution exclusion found in the body of the policy. The policyholder should then supplement coverage with a complementary pollution policy to avoid coverage gaps.

Standalone Insurance Coverage for Environmental Hazards

The Contractor's Pollution Liability (CPL) policy is a standalone pollution policy that can be used to fill the coverage gap created by the pollution exclusions. Since the introduction of the policy, the CPL's popularity has risen significantly. As of 2006, the CPL policy accounted for 30 to 40 percent of the entire environmental insurance marketplace, an industry which incurred approximately $2,000,000,000 in premiums that year. This percentage has likely grown since.

There are several components to a CPL policy of particular importance to policyholders. In particular, insureds should be aware of their policy's insuring agreement, as well as its definitions of "loss," "pollution event," and "claim."

The following is an example of a standard CPL insuring agreement.

> We will pay on behalf of an 'insured' any 'loss' an 'insured' is legally obligated to pay as a result of a 'claim' caused by a 'pollution event' resulting from 'covered operations' or 'completed operations' of the 'covered operations.' The 'bodily injury' or 'property damage' must occur during the 'policy period.'

Savvy policyholders will probably notice the similarities between this and the standard CGL's insuring agreement. If you replace "pollution event" with "occurrence" they are functionally the same.

Typically, "loss" is defined along the lines of the following language: "compensatory damages or legal obligations arising from bodily injury or property damage and related claims expense." Although this is an example of a common definition, some policies may contain

narrower definitions. For example, some policies limit loss to only hazardous remediation and natural resources damage. Policyholders need to be alert when putting together a policy to make sure they know what coverage they are getting from their CPL policy.

With occasional slight variations, the standard definition of "pollution event" is "the discharge, dispersal, release, or escape of any solid, liquid, gaseous or thermal irritant, contaminant or pollutant including smoke, vapor, soot, fumes, acids, alkalis, chemicals and waste." Once again, those familiar with CGL language will notice that this is nearly identical to that of the absolute pollution exclusion in the CGL policy. Policyholders may also notice that this language invites the same litigation as the absolute pollution exclusion over the meaning of "pollutant."

Considerations for Maximizing Environmental Insurance Coverage

As a policyholder considering your environmental coverage needs there are several things you should keep at the front of your mind. Primarily, you should work with a team comprised of specialists in the environmental insurance coverage arena. This team may include, but is not necessarily limited to, risk managers, environmental remediation experts, and environmental insurance coverage specialists. Ideally, the group should have experience in putting an environmental coverage policy together, submitting environmental claims, and handling insurance companies if environmental claims are denied.

Second, remember that the law in nearly every area of this field is unsettled and differs greatly from one jurisdiction to the next. Someone experienced in the field, who can guide you through the intricacies of the jurisdiction you will be working in, is a good resource in this situation. Consider having your policy reviewed by someone in your team who knows what legal exposures you may have based on the operational footprint of your company.

Third, policyholders should always aim for their CGL and CPL policies to mirror each other. Where something is excluded by the CGL's pollution exclusion, you should try to have your CPL pick that coverage up. The primary benefit is that you will avoid coverage gaps. Beyond that, however, some overlap between the policies may be doubly beneficial. The duty to defend on the CGL policy is extremely broad, so a keen policyholder may be able to utilize the duty to defend from the CGL, have the actual loss covered by the CPL, and use the savings from the defense to offset the Self-Insured Retention (SIR) on the CPL.

Ultimately, policyholders should always remember that insurance coverage litigation is extremely technical, which gives insurers a huge advantage. Although companies with risk management teams generally have a better understanding of their coverage needs, it is always safest to rely on someone with knowledge of insurance coverage law. This is particularly true in a field like environmental coverage, where different jurisdictions have such wildly different approaches to many major issues.