

NY Ruling Curtails Insurers' Environmental Cleanup Exposure

By Jeff Sistrunk

Law360 (March 28, 2018, 9:25 PM EDT) -- New York's high court ruled Tuesday that a Chubb Ltd. insurer doesn't have to cover a gas company's environmental remediation costs for years when no pollution insurance was available in the marketplace, a decision that limits carriers' exposure to cleanup coverage claims by forcing policyholders to pick up the tab for such periods.

The New York Court of Appeals unanimously affirmed a state appellate panel's ruling rebuffing National Grid PLC subsidiary KeySpan Gas East Corp.'s call to apply a so-called unavailability exception to the pro rata insurance allocation formula, which is often used to sort out coverage for environmental contamination, asbestos personal injury and other "long-tail" claims implicating many policy periods.

In a pro rata scheme, a policyholder must generally pay a share of its own long-tail liability costs for years when it had no policies in place. But if an unavailability exception is applied, the policyholder doesn't have to cover costs incurred during periods when it was unable to buy a specific type of insurance in the marketplace; instead, those costs are spread among the company's insurers.

The New York justices agreed with KeySpan's insurer, Chubb unit Century Indemnity Co. that the unavailability exception is incompatible with insurance policy terms mandating pro rata allocation—namely, language limiting the insurer's liability to losses and occurrences happening "during the policy period."

Attorneys who represent insurance companies praised the high court's ruling as a well-reasoned opinion curbing policyholders' efforts to put insurers on the hook for more risk than they anticipated when issuing their policies.

"The New York Court of Appeals slammed the door shut on policyholders seeking to hoist upon their insurers losses for periods in which insurance is unavailable in the marketplace, delivering a significant victory to insurers in the allocation war," Hinshaw & Culbertson LLP partner Scott Seaman said, characterizing the unavailability exception as "utter lunacy."

But lawyers who counsel policyholders were quick to point out that many policies don't require a pro rata allocation method. Pursuant to the Court of Appeals' landmark 2016 decision in a case known as Viking Pump, "non-cumulation" or "prior insurance" policy provisions support the imposition of "all sums" allocation, under which an insurer can be held liable for a policyholder's entire loss up to the applicable policy limits.

If all sums allocation is applied in a case, the unavailability exception is a nonissue, according to attorneys.

"In many cases, I think Viking Pump will ultimately be the decisive case in this area, not KeySpan," Pillsbury Winthrop Shaw Pittman LLP partner David Klein said. "Once a policyholder has one policy with a [non-cumulation] clause, they can take advantage of the all sums allocation provided for in Viking Pump."

The coverage battle stems from the New York Department of Environmental Conservation's 1995 order directing KeySpan to clean up contamination at manufactured gas plants in Rockaway Park, Queens, and Hempstead, Long Island, where hazardous waste had seeped into the soil and groundwater. According to court papers, the pollution occurred gradually over many decades beginning in the early 1900s, but it is not possible to precisely determine how much of the environmental damage occurred in a given year.

KeySpan filed suit to pursue indemnification for its cleanup costs from Century, which issued a series of successive general liability policies between 1953 and 1969. KeySpan, however, asserted that Century should also cover its costs attributable to periods when no insurance covering pollution risks was available.

Applying a pro rata allocation scheme, state Judge Saliann Scarpulla held that, with the exception of a span from 1971 to 1982 when the New York Legislature barred insurers from selling pollution liability insurance, Century's share of KeySpan's cleanup costs should include a proportion of periods when such insurance was otherwise unavailable.

But in September 2016, a panel of the New York Appellate Division's First Department disagreed with Judge Scarpulla's conclusion, saying the state high court's seminal 2002 pro rata allocation decision in a case known as Consolidated Edison left open the question of whether a policyholder's risk during periods when it couldn't have obtained insurance — even if it wanted to — can be allocated to its existing, triggered policies.

The appeals panel ultimately found that Century doesn't have to indemnify KeySpan cleanup costs attributable to times when pollution liability coverage was unavailable, which was the case for the years before 1953 and after 1986.

In Tuesday's opinion, the Court of Appeals likewise agreed with Century's position that requiring an insurer to assume liability for damages resulting from occurrences outside its policy period "would contravene the very premise underlying pro rata allocation." Unlike courts that have endorsed an unavailability rule, the New York justices refused to consider public policy concerns, such as the "desire to maximize resources available to claimants against the policyholder."

"It follows from our holding in Consolidated Edison that the unavailability rule is inconsistent with the contract language that provides the foundation for the pro rata approach — namely, the 'during the policy period' limitation — and that to allocate risk to the insurer for years outside the policy period would be to ignore the very premise underlying pro rata allocation," Associate Judge Leslie Stein wrote.

The high court noted that the insurer-policyholder relationship functions in accordance with the setting and payment of appropriate premiums "consistent with the parties' forward looking assessment of what that risk might entail." If insurance for a certain risk is unavailable, the mere principle of spreading risk

"should not by itself serve as a legal basis for providing free insurance to an insured,'" the court found, quoting from the Appellate Division panel's opinion.

Crowell & Moring LLP partner Laura Foggan, who represents insurers, said the New York justices' ruling properly "recognizes the fact that insurers are making a calculated choice about the risks they will assume."

"To then assign that risk back to them despite the fact that they elected not to insure a company for that exposure is fundamentally unfair and inconsistent with the contracting terms," Foggan said.

Clark & Fox partner Michael Savett voiced a similar sentiment, saying it was significant that the Court of Appeals looked to the "fundamental nature" of insurance — the coverage of foreseeable risks — in reaching its decision.

"An insurance underwriter is looking at a business's potential and assessable risks that could occur over a particular period of time, and based on those risks the insurer charges the business accordingly," Savett said. "Viewing coverage through that lens, the Court of Appeals here was not going to force an insurer to indemnify a risk that did not occur during the agreed-upon period."

On the other hand, attorneys who counsel policyholders say the ruling will unfairly require companies embroiled in long-tail coverage battles to pay out of pocket for costs attributable to huge chunks of time during which no coverage was available for the relevant risk.

"To me, this means that policyholders will be left holding the bag on long-tail claims even when they thought they had insurance and did the right thing economically," said Walter Andrews, head of Hunton & Williams LLP's insurance coverage practice. "This is not the situation in which the court should provide a disincentive — in which a policyholder chooses to go uninsured. Here the policyholder had no choice."

Anderson Kill PC managing shareholder Bob Horkovich noted that the Court of Appeals didn't address how a pro rata allocation method without an unavailability exception will work in practice. In theory, the policyholder's share of its long-tail liabilities will continue to increase with each passing year, while the insurer's share will continue to shrink, attorneys say.

"The decision formulates a rule which is unworkable in that the end date for the allocation to periods in which such insurance is unavailable is undefined and could stretch out to infinity, making coverage illusory — which cannot be," Horkovich said.

Jenner & Block LLP partner Matthew L. Jacobs said the decision "effectively creates an incentive" for insurers to delay resolving coverage disputes. The longer a carrier delays a final determination, Jacobs said, the more periods of unavailability will be allocated to the policyholder.

"Henceforth, it becomes a liability of the policyholder as opposed to a liability of the insurer," he said.

However, attorneys say, the Court of Appeals' rejection of the unavailability exception won't be a concern if an insurer's policies contain non-cumulation or prior insurance provisions requiring all sums allocation. As the high court noted in its Viking Pump opinion, such provisions mandate an all sums approach because they "plainly contemplate that multiple successive insurance policies can indemnify the insured for the same loss or occurrence."

According to Klein, the Court of Appeals also left open other doors for policyholders to avert an unfavorable outcome in long-tail coverage disputes. While the high court found it was impossible to decipher what portion of the environmental contamination at KeySpan's sites occurred in any given year, that may not always be the case, Klein said.

"In some instances it may be possible, through expert testimony, to establish how much of the loss is attributable to different policy periods, and thus to avoid having to apply the legal fiction of pro rata allocation," he said.

--Editing by Pamela Wilkinson and Breda Lund.

All Content © 2003-2018, Portfolio Media, Inc.