

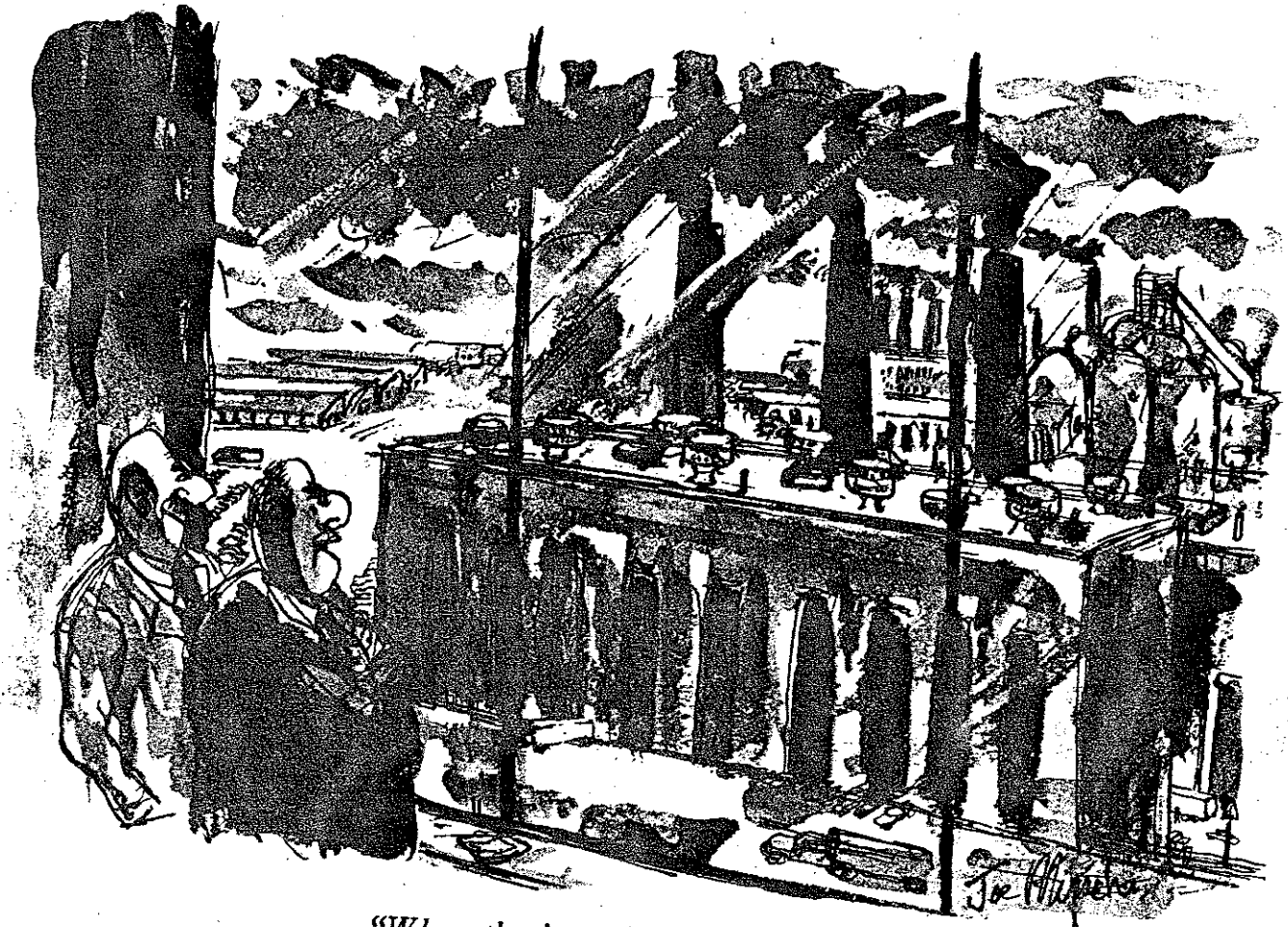
POLLUTION AND PROPERTY POLICIES

**Skeptical (Possibly Even Dissenting)
Queries and Some Simple-Minded Questions**

(LATE 1980S, I THINK

Michael Sean Quinn
ZELLE & LARSON
1201 Main Street
Suite 3000
Dallas, Texas 75202

Observations, arguments, opinions, views, conclusions, and even some of the questions, discussed and expressed in this paper are not necessarily those of Zelle & Larson, any partner therewith, or any client thereof. As for Patricia Heitmann, Liz Scurlark, and Karen Sherrill: Thank you! Thank you! Thank you!



"Where there's smoke, there's money."

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POLLUTION AND PROPERTY POLICIES

Skeptical (Possibly Even Dissenting) Queries and Some Simple-Minded Questions

I. Do property policies cover pollution?

- A. Coverage. Some property policies sometimes do. Allstate Ins. Co. v. Quinn Constr. Co., 713 F. Supp. 35 (D. Mass. 1989) (a property insurer paid for the cost of cleaning up gasoline contamination that originated on its insured's property).
- B. Potential Dangers. Some knowledgeable observers think that coverage for pollution insurance will be one of the main types of insurance disputes in the 1990s. Knoll & Arthur, Property Insurance: No Solution for Pollution, 17 Environmental Affairs 231 (1990) ("Knoll"); Miller, Erickson & Joy, in Environmental Claims and Litigation Involving First Party Property Policies: Recent Developments and Principal Exclusions, Environmental Claims And Property Insurance Coverage (ABA Torts & Insurance Practice Section 1989) ("Miller"), and T. Mallin, Pollution And Contamination: How Will Property Insurers Respond? (1987) ("Mallin"). Knoll and Arthur, for example, state that "[p]roperty insurance policies . . . are fast becoming a new target for claims to recover losses caused by contamination." Knoll at 232. For a very interesting speech-outline on this matter, see Wilson & Arthur, The Question of Coverage for Contamination and Pollution Losses Under Property Insurance, in Insurance Coverage For Environmental Claims G-1 (Defense Research Institute, 817C, Chicago, IL, Nov. 17-18, 1988). Hickman & DeYoung, Allocation of Environmental Cleanup Liability Between Successive Insurers, 17 N. Ky. L. Rev. 295 (1990).
- C. Asbestos. Asbestos liability insurance litigation is similar, in some ways, to environmental and pollution insurance litigation. For a discussion of asbestos-inflicted property damage in the context of liability policy disputes, see Arness & Eliason, Insurance Coverage for "Property Damage" in Asbestos and Other Toxic Tort Cases, 72 Va. L. Rev. 943 (1986).
1. Some building owners are seeking recovery from their property insurers for the presence of asbestos in their buildings. Sunset-Vine Tower, Ltd. v. Commerce and Indus. Ins. Co., No. C-738-874 (Cal. Super.--Los Angeles, filed July 31, 1990). See 4 Mealy's Litigation Reports: Insurance 8, A-1

(Sept. 5, 1990). The Superior Court dismissed the plaintiff's First Amended Complaint for failure to state a cause of action under the relevant insurance policies. The plaintiff filed a Second Amended Complaint on August 6, 1990.

2. Several commentators have considered the use of property insurance in asbestos property damage cases. The most comprehensive paper is that of Paris, Asbestos In Buildings: Property Coverage Claims, in Asbestos Property Damage Claims M-1 (Defense Research Institute, 906, Chicago, IL, June 8-9, 1989) ("Paris"). Anderson, Property Damage Liability Coverage for Asbestos Removal and Hazardous Waste Cleanup Costs, CPCU J. 8 (March 1989).
3. Many coverage issues are superficially similar. The issues raised by the pollution exclusion, the intended and expected clause, and the nature of property damage which come up in liability policy litigation somewhat resemble issues which come up under property policies. But the resemblance is to some degree misleading. See Paris at M-2. The nomenclature of property policies, the concepts of property policies used, and the conceptual nature of a property policy are all different from liability policies.

D. Skepticism. Insureds will have a difficult time establishing pollution coverage under many different types of property policies.

1. For the most part, property policies did not intend to cover what we now think of as pollution or environmental losses.
2. Moreover, property policies are designed to have short tails, whereas liability policies (at least those which do not utilize the "claims made" insuring agreement) have long tails.
3. Moreover, the insureds went to a great deal of trouble to introduce pollution change endorsements and environmental impairment insurance. In the absence of a conspiracy theory, it is difficult to see why they would have done this if pollution losses were always intended to be within coverage. (Innovative pollution insurance coverages did not prove to be popular with consumers, either individual or business. They were simply too expensive.) See D'Arcy & Herricks, Pricing Insurance for Pollution Damage, CPCU J. 74 (June 1989).

4. This section is intended to express my skepticism. Pollution losses will be covered here and there because of particular wordings. However, I am inclined to doubt that what has happened on the liability side will happen on the property side.

II. What is pollution? What's in a name? Terminology is important for three reasons. First, courts categorize insurance cases almost unconsciously. Pollution and environmental cases are treated differently than fender-benders, slip and fall cases, and the like. Second, legal disputes essentially involve words. Stories cannot be told without words. Documents cannot be interpreted without words. What words are used, therefore, are important. Third, some policies utilized--whether in their provisions, titles, or subtitles--words like "pollution," "pollutants," "environmental impairment," and so forth. Nevertheless, in the area of property insurance, patterns of usage, and resultant judicial interpretation, are yet to be developed areas.

A. Notes & Nomenclature. "Pollution" and its equivalents are not legal terms of art, although the term "pollutants" appears in a number of insurance policies, and pollution is a frequent source of nuisance litigation. Fulbright & Jaworski, Texas Environmental Law Handbook at 357 (Government Institutes, Inc., Rockville, MD, April 1989) ("Fulbright & Jaworski"). Pasich, Insurance Coverage for Environmental Claims, Los Angeles Lawyer 22 (Jan. 1989). "Pollution" is a popular term of ordinary and political discourse, and it means many things. There is equivalent, less familiar verbiage, sometimes encountered in insurance contracts. For example, there is "environmental damage," "environmental impairment," and "injury from hazardous [or "toxic"] waste." Nomenclature could, conceivably, make some difference. This is true of the policy, obviously, and it is also true of the rhetoric used in the litigation.

B. Paradigms of Pollution. The courts have yet to bill consistent definitional patterns for words like "pollution." Nevertheless, everyone has certain images and ideas in mind when terms like "pollution" are used.

1. Air. The standard image of air pollution is smog. However, smoke could be air pollution, odors could be air pollution, and vapors could also be air pollution. (Indeed, at least one court has held that some vapors are smoke. Henri's Food Prods. Co. v. Home Ins. Co., 474 F. Supp. 889 (E.D. Wisc. 1979). Is the stink from a rendering plant air pollution? Does it matter?

2. Water. Streams and ponds are said to be polluted. Sometimes these belong to the sovereign; sometimes not. Similarly, groundwater and water wells are said to become polluted. Other subterranean liquid pools can become polluted.
 3. Earth. Gunk can get in the ground, stinking it up, cause it to lose soil strength or stability, and affect subjacent or lateral support. Substances in the earth can seep into buildings.
- C. Pollution and the Legal Literature. There is an enormous amounts of legal, quasi-legal, public policy, polemic, and political-ideological literature on pollution, waste regulation, environmental impairment, and the like. The literature cannot be "mastered"; it is simply too large. However, there is no point in mastering it, because it is superficial and redundant. On the other hand, hardly any proposition is so outlandish as to lack an advocate, so if you need "authority" you can find it.
1. National Legal Literature. The legal literature on the regulation of pollution is absolutely enormous. One good starting place is the essay entitled Developments--Toxic Waste Litigation, 99 Harv. L. Rev. 1459 (1986). Of course, there are substantial developments since then. Legal developments are reviewed on an annual basis in the Annual Survey of Tort & Insurance Law which is published in the winter issue of the Tort & Ins. L.J., a publication of the American Bar Association.
 2. Public Policy Literature. The literature on environmental problems and legal aspects of environmental problems is enormous. One helpful source is D. O'Brien, What Process Is Due? Courts And Science-Policy Disputes (1987). The best single essay on pollution and insurance is Abraham, Environmental Liability and the Limits of Insurance, 88 Colum. L. Rev. 942 (1988) ("Abraham, Limits"). Similarly, the best single source on insurance, legal theory, and public policy is K. Abraham, Distributing Risk (1986) ("Abraham, Risk").
 3. Texas Literature. A good starting point for reviewing pollution law in Texas is Fulbright & Jaworski, Texas: Environmental Law Handbook (1989). This book is available from the Government Institutes, Inc., 966 Hungerford Drive, #24, Rockville, MD 20850.
 4. Case Studies. There are fairly recent case studies which are especially interesting. Emphasis in

these studies on bodily injury, but property damage is in the background. M. Cherniack, The Hawk's Nest Incident America's Worst Industrial Disaster (1986) (the silicosis disaster at Gauley Bridge, West Virginia in the 1930s); P. DiPerna, Cluster Mystery Epidemic and the Children of Woburn, Mass. (1985); P. Schuck, Agent Orange on Trial (1986).

D. Pollution and Insurance.

1. Insurance, and the risk transfers that insurance involves, are key elements in the American economic and social system. See Abraham, Limits.
2. Naturally, when business entities sustain economic losses as the result of pollution or environmental impairment, they look for risk (now, loss) transferees. Homeowners are no different.
3. Sometimes, the insured is also a tort-feasor. When he is, there is often liability insurance. Contracts of property insurance transfer risk for many instances of the insured's own negligence, as well as that of others. Many CERCLA-mandated clean up costs result from the negligent and even reckless conduct of the insured. It is for these kinds of costs that large pollution/property insurance disputes are most likely to arise. "Environmental cleanup liability is usually the result of waste disposal activities. Environmental claims generally share several characteristics. These include: (1) the damage arises from the insured's regular (and in most cases legal) activities at the facility during the ordinary course of its business; (2) the damage takes place over an extended period of time; (3) the damage remains unrecognized during most of that period of time; (4) the damage is cumulative; (5) multiple, successive policies of insurance were issued to the insured over the period of time damage was developing; and (6) the amount of the claim exceeds the liability limits available under any single [liability] policy, and may exceed the limits of [all liability] policies [whether primary or excess] combined." Hickman & DeYoung, Allocation of Environmental Cleanup Liability Between Successive Insurers, 17 N. Ky. L. Rev. 292 (1990). Hence, all the interest generated toward property insurance policies.
4. What if the economic loss involves the insured's property only, and there is no tort-feasor, and hence no access to liability insurance? Can the

subject of such an economic loss recover from his property insurer? See Abraham, Limits.

5. The quest for coverage and the route to resistance begin not with general considerations of economic and social policy, but with the insurance contract itself. In analyzing a property insurance contract for pollution coverage (or the lack thereof) the lawyer must ask six crucial questions. Those questions are the theme of this discussion.

III. How should property policies be conceived?

A. Conceptual Organization: Introduction. In order to think about pollution claims in any particular way, whether from the policyholder's or the insured's point of view, the conceptual organization of property policies must be kept in mind. Property policies are, in general, quite different from liability policies. Garvey v. State Farm Fire & Casualty Ins. Co., 48 Cal. 3d 395, 770 P.2d 704, 257 Cal. Rptr. 292 (1989), and they vary amongst themselves quite a bit. It is somewhat misleading to group all insurance on property together. For example:

1. The property section of homeowners' policies are theoretically similar to commercial property policies, but the judicial attitudes towards homeowners' policies are quite different.
2. Boiler and machinery policies, while they are insurance policies insuring property and typically issued by property carriers, are quite different in concept from other property policies.

B. Categories Listed. Property policies should be conceived in the terms of the following conceptual categories:

- types of property expressly covered
- types of property expressly not covered
- property which is neither expressly covered nor expressly not covered
- perils expressly insured against (and this may include "all risks of physical loss")
- extensions of coverage (if the policy is not an all-risk policy, but instead names particular perils insured against)
- monetary limits on coverage
- express exclusions from coverage
- "implied" exclusions from coverage
- relevant conditions
- questions of trigger
- notice requirements
- suit requirements

- C. Other Properties. Property policies involve all sorts of other provisions, but these are the starting places. (Other important provisions include the price term, contractual provisions regarding misrepresentations, deductibles, co-insurance clause, the cooperation clause, salvage clauses, and so forth.)
- IV. What property is covered? This is the first crucial question a lawyer must ask when considering coverage. Most property insurance policies expressly list categories of property for which there is coverage.
- A. Buildings. Buildings are the paradigm of the type of entity covered under a property policy. Thus, prima facie, if the building sustains pollution damage, it is the sort of thing for which there may be coverage.
- B. Personalty. Certain types of personal property is frequently covered in property policies.
1. Under homeowners' policies, the contents are usually covered property.
 2. In commercial property policies, frequently, equipment which is outside of, but close to a building is expressly said to be covered property.
- V. What property is expressly not covered? This is part of the first crucial question. Most property policies include a section listing categories of objects for which coverage is not provided. These vary substantially with the policy; however, growing crops, trees, pets, outdoor signs, water craft, and many other entities are usually excluded.
- A. Land. One of the most important types of property which might suffer pollution damage is land. Many newer property policies expressly state that land is not covered. Query: Are natural resources (for example, mineral deposits) different from land? Is groundwater part of the land or distinct therefrom?
- B. Interpretation. Questions of construction may arise. For example, if water is property which is expressly not covered, is the contamination of a well excluded? (One would think so, unless it is the well itself--as opposed to the water--which is contaminated.) Is the pollution of groundwater excluded, if water is explicitly not covered property--but land is not excluded? (This is a much more difficult question.)
- C. Locus of Exclusion. Sometimes, property is excluded from coverage in odd places. For example, some types, and some parts of some types of property are not covered for wind or hail damage. This fact is often to be found in

the perils section of the policy, rather than in the property section.

VI. What property is neither listed as covered property nor listed as property not covered? Many categories of property are not listed either way.

A. Land. One of the most significant types of property which is frequently not listed either way is land. Obviously, much pollution is inflicted upon land. Many CERCLA-mandated "response costs" have to do with cleaning up polluted land. When land is not listed, one can easily imagine the following legal antinomy:

1. Land is not listed under the heading "Covered Property." Hence, there is no coverage for injury to land. After all, the function of the "covered property" section is to list all the types of property which are covered.

2. Land is not listed under "Property Not Covered." Hence, there must be coverage for land. Exclusions are to be read narrowly, and insuring clauses broadly. Besides, the "Covered Property" section of the policy does not say that no property is covered unless it is specifically said to be "Covered Property."

B. Land & Buildings. It is not always clear what constitutes part of a building and what constitutes land. At least one case has held that the term "dwelling" encompasses some land. Pfeiffer v. General Ins. Co., 185 F. Supp. 605 (N.D. Cal. 1960) ("[L]and underlying the house must be encompassed within the word 'dwelling' unless the policy is to be interpreted as illusory." Id. at 608. One wonders if the court would have reached the same result for a commercial building.)

Of course, CERCLA is not always involved and there is not always a tort-feasor.

VII. Are the terms of the insuring agreement satisfied? This is the second crucial question a lawyer must consider when evaluating coverage under a property policy.

A. Elements. There are three key requirements in most property insuring agreements.

1. There must be physical loss, and it must fall under certain categories.

2. The insured type of loss must be caused by a peril insured against.

3. The peril insured against must really cause the loss.

B. Central Idea. The intuitive idea behind property insurance is this. Insureds are protected against the sudden and unanticipated damage which can be done by active forces of nature and people.

1. At its core, and from its inception, it was not insurance against substandard performance (for example, in the design of buildings) substandard products, antecedently existing problems or gradual and creeping wear and tear. (In Falcon Prods., Inc. v. Insurance Co. of Pa., 615 F. Supp. 37 (E.D. Mo. 1985), the case which involved radiation contamination to personalty, an insured loss--in part--because the contamination complained of was already in the raw material which he utilized to make his product. In other words, his product was afflicted before he owned property. Id. at 39.)

2. Some property insurance has become elaborated to include some of these things and to exclude some sudden acts of nature.

C. Agenda. The main components of the insuring agreement of the property policy will now be considered in reverse order.

VIII. What perils are insured against? The concepts of peril is central to the insuring agreement of a property policy. It will contain a designation of the perils insured against. They may be named, individualized and listed, or they may be clumped together under broad phrases like "all risk of physical loss" or "risk of physical loss."

A. History. Non-maritime property policies began as narrowly conceived named-peril policies.

1. The central named-peril was usually fire. New perils were added to old policy forms; this was frequently done through a clause extending the list of named perils. Lecomte, The History of the Property Insurance Policy, in The Creation And Implementation Of Good Faith In The Property Insurance Policy 1 (ABA Torts & Prac. Sec. 1987).

2. Eventually, named-peril policies were transformed into all-risk policies, where much of the real work was done by the exclusions.

3. Recently, the property insurance industry has become dissatisfied with the over-broad way in

which the courts have treated the phrase "all risk," and have deleted "all." Garvey, 770 P.2d 704; Aetna Casualty & Sur. Co. v. Yates, 344 F.2d 939 (5th Cir. 1965) (Friendly, J.) (Texas law). See Employers Casualty Co. v. Holm, 393 S.W.2d 363 (Tex. Civ. App.--Houston 1965, no writ).

4. It is not clear that the courts will agree with the insurance industry that the policy which covers "risks of physical loss" rather than "all risks of physical loss" is any narrower. Brodkin v. State Farm Fire & Casualty Co., 217 Cal. App. 3d 210, 265 Cal. Rptr. 710 (1990).

B. Current Circumstances. All risk, quasi-all risk, newly all risk, and physical risk policies are available today. So are named peril policies. Almost all named peril policies involve extensions of coverage, i.e., "new" or additional named perils. This is not true for all named peril policies. In some part of the country, there are policies simply covering wind damage, and so forth.

IX. What caused what? This question is part of the second crucial question.

A. Conceptual Structure. Property policies insure covered property against losses caused in certain ways, namely, caused by perils insured against. This is an important analytical point. Thus, in determining whether a pollution loss is arguably covered under a property policy, the lawyer must ask: Was this (pollution) loss caused by a covered peril? This question implies two further questions.

B. Causation. Causation is a very slippery idea. Every event has many causes; some events are over-determined; and the concept of causation itself is, to some degree, pragmatic human construction. H. Hart & T. Honore, Causation In The Law (2 ed. 1985). See W. Landes & R. Posner, The Economic Structure Of Tort Law 228 (1987).

1. The concept of causation in insurance and tort law is similar. Garvey, 770 P.2d 704. But see Great N. Ins. Co. v. Dayco Corp., 637 F. Supp. 765, 779 (S.D.N.Y. 1986) (a contributing--even though proximate--cause is insufficient to trigger an exclusion).

2. The standard for proving causation in insurance law is not always the same as it is in tort law. the majority rule, however, is that in order for a peril to be the cause of an insured loss, it must be a proximate cause of the loss.

- a. The concept of proximate causation is itself policy-laden, even accordion-like and perhaps obscure. (Some say it is actually archaic or downright meaningless.)
- b. Usually, what constitutes a cause under property policies is a matter for the jury, when it is an issue in dispute. Howell v. State Farm Fire & Casualty Co., 218 Cal. App. 3d 1446, 267 Cal. Rptr. 708 (1990). (In Howell, there was a landslide. The cause of the landslide was a fire which destroyed vegetation permitting the surface water to cause erosion, thereby setting up the landslide. In post-Garvey, the court held that there was a jury issue on what constituted the officiant proximate cause. This seems dead wrong to me. The landslide was the cause of the loss. The action of the surface water was the cause of the landslide. The fire burning away the vegetation was the cause of the surface water having the effect that it did. The trial court was right in summary judgment, and the appellate court was wrong to send it to the jury.)
- c. Ambiguity. Curiously, courts do not seem to suggest that the term "cause," and its cognates, is subject to the contra-insurer ambiguity rule. This seems to me to demonstrate that the rule is more a cloud of smoke for the convenience of the courts, than it is a genuine rule. Arness & Eliason criticize the concept of causation as follows: "A contract of insurance written to cover future unknown events cannot speak in anything but general terms. One can always claim that such a document is 'ambiguous' in a complex fact situation--if predisposed to do so--because language meant to cover unforeseen events is inherently capable of more than one interpretation. Although in the age of legal formalism it might have been thought possible to draft a document whose terms would always be clear, fixed, and unambiguous to future interpreters, few still adhere to this optimistic view of the nature of language. As a principle of construction, therefore, the doctrine of ambiguity 'usually serves to describes a result rather than to assist in reaching it.'" See Arness & Eliason at 949.
- d. Concurrent Causation. Under the law of California, formerly, and some other states, still, if Event-#1 (an excluded peril) and Event-#2 (a named peril or peril not excluded) both cause a loss, there was coverage, even if Event-#2 were a minor, merely contributing, or indeed remote, cause of the loss.

1. This is called the doctrine of concurrent causation.
2. This doctrine never caught on in Texas. National Fire Ins. Co. v. Valero Energy Corp., 777 S.W.2d 501 (Tex. App.--Corpus Christi 1989, writ denied) ("Generally, if loss occurs as a result of two concurring perils, one insured and one not, then the loss is covered only to the extent it can be traced to the covered peril." Id. at 505.); Auten v. Employers Nat'l Ins. Co., 722 S.W.2d 468 (Tex. App.--Dallas 1986), writ denied, 749 S.W.2d 497 (Tex. 1988).
3. Obviously, this doctrine creates extraordinary opportunities for creative lawyering and semantical gamesmanship.
4. The doctrine of concurrent causation is on the wane. California recently abolished it for property policies. Garvey, 770 P.2d 704. Finn v. Continental Ins. Co., 218 Cal. App. 3d 69, 267 Cal. Rptr. 22 (1990). See Houser & Kent, Concurrent Causation in First-Party Insurance Claims, in The All-Risk Policy: Its Problems, Perils, And Practical Application 35 (ABA Tort & Ins. Prac. Sect., 1986). See also Rudy, Concurrent Causation: Making Sense of the All-Risk Policy. Id. at 75. Other jurisdictions have rejected it as well. See Falcon, 615 F. Supp. 37, 39.
5. Some property policies now exclude losses caused by any cluster of causal factors, which involves an excluded causal antecedent.
 - a. Does this mean that if an excluded causal antecedent is one of the remote (as opposed to proximate) causes of covered loss, then there will be no coverage? (Probably not, even though there is no tradition of cases on this point. Probably only excluded causal antecedents, which are also proximate causes, will result in the exclusion of the entire loss.)
 - b. Obviously, this provision in the policy creates a new semantical game, which is the mirror-opposite of what we had under the doctrine of concurrent causation. A California intermediate appellate court has said "No," at least where a coverage mandating statute is involved. Howell, 267 Cal. Rptr. 708.

- c. There is no way out of this situation, since the concepts of causation and proximate causation are as obscure as they are common.

X. Is a covered peril a (proximate) cause of the (pollution) loss?

- A. All Risk Policy. "Under an all risks policy, the insured has the burden to establish a prima facie case for recovery. The insured need only prove the existence of the all risks policy, and the loss of the covered property. The very purpose of an all risk policy is to protect the insured in cases where it is difficult to explain the disappearance of the property; thus, the insured need not establish the cause of the loss as part of its case (citation omitted)." Dayco Corp., 637 F. Supp. 777. So, how should one think about an environmental pollution case? Pollution constitutes a risk, hence it is prima facie covered. Remember, this prima facie answer is very tentative because in interpreting an all-risk policy, nothing can be established about covered perils without studying the exclusionary clauses.
- B. Named Peril Policy. In a named peril policy, the central perils are fire, lightning, wind, storm, and hail, explosion, and a few others.
- C. Fire. Fire could be the cause of a pollution loss, if the fire proximately (although indirectly) led to an event which created pollution. The same point is true for other named perils.
1. Of course, even the presence of centrally named perils is not always completely clear. Whether the events leading to the loss constituted a fire, for example, was the issue in H. Schumacher Oil Works v. Hartford Fire Ins. Co., 239 F.2d 836 (5th Cir. 1957) (Texas law).
 2. Other nomenclature used in named peril policies is similarly not completely clear. There is litigation, for example, as to what counts as an "explosion," which is usually a named peril. American Casualty Co. of Redding, Pa. v. Myrick, 304 F.2d 179 (1962).
- D. Smoke. A peril frequently named is smoke. One policy form names "sudden and accidental damage from smoke, other than smoke from agricultural smudging or industrial operations" as a peril insured against, while another names "smoke causing accidental loss or damage." The second policy notes that "This cause of loss does not

include smoke from agricultural smudging or industrial operations.

1. These seemingly identical clauses are conceptually quite different.

a. The first clause refers to sudden and accidental smoke, whereas the second clause refers to sudden and accidental losses.

b. The phrase "sudden and accidental" is a frequently litigated phrase in liability policies, and it is even more obscure than the concept of causation. This will create enough trouble by itself. Valero, 777 S.W.2d at 506. (In Valero, the court utilized the phrase "sudden and unexpected," even though no such phrase appeared in the exclusions under consideration.) But there is more.

c. It is possible that a continuous stream of smoke might suddenly cause an accidental loss. (Stranger things have happened under liability policies in the environmental area.)

d. The concept of smoke is itself subject to some ambiguity. Vapors which are neither black or particulate can qualify as smoke. Henri's, 474 F. Supp. 889.

e. Finally, the range and meaning of the phrase "from industrial operations" is subject to some range of interpretation. In fact, all three terms in this phrase have some "give" in them.

(1) Obviously, smoke from an industrial fire is not smoke from an industrial "operation."

(2) What about smoke damage caused by a sudden and accidental plant failure which releases smoke into the air? Into the interior of a building? One would argue that this was not an industrial "operation" since it was precisely the cessation of operations which caused the loss.

E. Vandalism. Vandalism is sometimes a named peril, sometimes not. Vandalism may lead to pollution. Louisville and Jefferson County Metro. Sewer Dist. v. Travelers Ins. Co., 753 F.2d 533 (6th Cir. 1985). (Sewage, dumped down a manhole, damaged a waste treatment

facility. The insurer denied coverage, but the insured prevailed.) Thus, it may be important to ask: what is the definition of vandalism in this policy? The definition of the term "vandalism" often includes the term "willful," but it does not always include the term "malicious." Moreover, the physical loss caused by vandalism need not be intended or even expected. Id. at 536-37.

F. Incivility. Riots, riots attendant upon strikes, and physical losses resulting from civil commotion are frequently (but not always) named perils. These might well cause pollution losses. However, insurrection, rebellion, revolution, and usurpation are almost always excluded. Obviously, they too may cause pollution losses. It is usually easy to tell the difference between a riot and a rebellion, but (over the long haul) not always.

XI. What exclusions apply to a particular case? This is really part of the second crucial question, since it ultimately concerns whether the insuring agreement is satisfied. Steuber & Lindberg, First-Party Property Policies in an Environmental Claims Context -- A Look at the Exclusions, 2 Envtl. Claims J. 141 (1989-90). Keep in mind that policy exclusions are not always the exclusion of perils; resultant conditions may also be excluded; and theoretically so could causal mechanisms or sequences.

A. Pragmatics. An exclusion-question can be asked in either of two ways:

1. What exclusions apply to the proximate causes for the loss?
2. What proximate cause is there which is not excluded?

At least two formulations are really the same questions. But the emphasis (pragmatics) is different, so that your mind is focused differently, pending on which formulation is used. Which formulation a lawyer should use will depend upon the issue before him. In either case, he must study the exclusions in the applicable policy. They vary substantially both as to the categories of exclusion set forth in the policy and in terms of the wording of individual exclusions. Nevertheless, there are some fairly common exclusions.

B. Pollutants Exclusion. Some property policies expressly exclude the release, discharge, or dispersal of pollutants.

1. There is little (so far) in the way of judicial construction of the term "pollutant." One would expect the courts to rely on non-legal dictionaries and the proposition that a pollutant is anything which causes pollution.
 2. One would expect guidance in interpreting the Pollutant Exclusion and the property policy from the Absolute Pollution Exclusion in the recent liability policies. Comments, Pollution Exclusion Clauses: The Agony, the Ecstasy, and the Irony for Insurance Companies, 17 N. Ky. L. Rev. 443 (1990).
 3. The new Absolute Exclusion defines the term "pollutants" as follows: "Pollutants means any solid, liquid, gaseous or thermal irritant or contaminant, including smoke, vapor, soot, fumes, acids, alkalis, chemicals and waste. Waste includes materials to be recycled, reconditioned or reclaimed." One wonders if the contra-insurer ambiguity rule will ever come up in connection with the meaning of the term "waste." See II.A.
 4. At least in some policies, there is an exception to the exclusion. The ISO 1984 HO-3 excepts from the exclusion the following: "If the dispersal of a pollutant causes water damage not otherwise excluded from a plumbing, heating, or air conditioning or automatic fire protective sprinkler system or household appliance, we will cover loss caused by the water including the cost of tearing out or repairing any part of the building necessary to repair the system or appliance. We do not cover loss to the system or appliance to which this water escaped."
- C. Contamination. Obviously, this is an extremely important exclusion from the point of view of pollution coverage. Some policies have it; some do it.
1. It has been litigated several times on the micro-pollution level. Raybestos-Manhattan, Inc. v. Industrial Risk Insurers, 433 A.2d 906 (Pa. Super. 1981) (fuel oil negligently mixed with heptane in an underground tank inflicted damage to work in progress).
 2. It has also been litigated in the industrial context outside of pollution, strictly so-called.
 - a. Many property policies exclude contamination. "Contamination occurs when a condition of impairment impurity results from mixture or contact with a foreign substance." Auten v.

Employers Nat'l Ins. Co., 722 S.W.2d 468 (Tex. App.--Dallas 1986), writ denied, 749 S.W.2d 497 (Tex. 1988). The Supreme Court of Texas granted a writ of error in this case and for a time considered reversing the decision of the Court of Appeals. Eventually, however, the Supreme Court decided that the writ had been improvidently granted, vacated its earlier order, and summarily denied the writ.

- b. Other significant contamination cases include American Casualty Co. v. Myrick, 304 F.2d 179 (5th Cir. 1962), Insurance Co. of St. Louis v. McConnel Constr. Co., 428 S.W.2d 659 (Tex. 1968) (contrasting contamination with corrosion in a muriatic acids spill case), and Mc Quade v. Nationwide Mut. Fire Ins. Co., 587 F. Supp. 67 (D. Mass. 1984). See Hi-G, Inc. v. St. Paul Fire Marine Ins. Co., 283 F. Supp. 211 (D. Mass. 1967), aff'd., 391 F.2d 924 (1st Cir. 1968) (an indoor industrial accident involving oil vapors). See also American Produce & Vegetable Co. v. Phoenix Assurance Co., 408 S.W.2d 954 (Tex. Civ. App.--Dallas 1966, no writ) (ammonia leakage not within the explosion exception to the contamination exclusion). See Brodkin v. State Fire & Casualty Co., 217 Cal. App. 3d 210, 265 Cal. Rptr. 710 (1990) (contamination, deterioration, and antecedent defect exclusions considered here).
 - c. In some policies, the exclusion is not a contamination exclusion, but a contaminants exclusion. For example, ISO's HO-3 (1984) excludes any "release, discharge or dispersal of contaminants or pollutants."
 - d. Sometimes, insureds have tempted to claim that contamination, a property condition rather than a cause of property damage, is covered if the cause of the contamination is a peril insured against. Auten, 749 S.W.2d 497 (Tex. 1988) (resolved against insured).
2. Contamination exclusions may not eliminate coverage where the contaminants are released by fire. Marshall Produce v. St. Paul Fire & Marine Ins. Co., 256 Minn. 404, 98 N.W.2d 280, 289-91 (1959). Indeed, some policies specifically state that exclusions do not cover the direct results of fire.

D. Corrosion. Some policies exclude corrosion, while some do not. Arkwright-Boston Mfr. Mut. Ins. Co. v. Wausau Paper Mills Co., 818 F.2d 591 (7th Cir. 1987).

1. Obviously, pollution can cause corrosion.
2. When contamination is excluded, and corrosion is not, arguments will arise as to whether a loss is a corrosion loss or a contamination loss. Myrick, 304 F.2d 179 (contamination connotes impurity resulting from a mixing of substances, whereas corrosion involves disintegration, oxidization (i.e. rust) or the decay of metals).
3. Sometimes, property policies exclude corrosion itself. In Texas, this exclusion has led to a dispute which is either celebrated or notorious depending on your point of view. In National Fire Ins. Co. v. Valero Energy Corp., 777 S.W.2d 501 (Tex. App.--Corpus Christi 1989, writ denied), a commercial-industrial insured recovered \$10 million in actual damages and \$15 million in exemplary-bad faith damages in a case which arose out of corrosion. The policy excluded corrosion, unless it resulted from a named peril. Corrosion in this case resulted from faulty design and construction. Those activities were also an excluded peril, but there was an exception to the exclusion. Physical loss consequent upon faulty design, etc., was not within the exclusion. The court held that the faulty design resulted in corrosion, which was a physical loss, and therefore that the corrosion resulted from a named peril and was hence not excluded.

The problem in Valero was the interaction between two exclusionary clauses. One could easily imagine this exact same situation arising in a pollution context. The lesson here is to watch out for exceptions to exclusions.

E. Ordinance Exclusion. Most policies exclude coverage for, in the words of one policy, "enforcement of any local or state ordinance or law regulating the construction," repair or demolition of buildings or structures, or in the language of another policy, the "enforcement of any ordinance or law: (1) regulating the construction, use, or repair of any property; or (2) requiring the tearing down of any property, including the cost for removing its debris." (These two formulations are somewhat different, since the second one includes use while the first one does not and because the first one refers to the demolition of buildings or structures, whereas the second one refers to the tearing down of any property.)

1. Under the case law of many jurisdictions, the ordinance exclusion is severely restricted. For example, if a building is partially destroyed by a covered peril and is ordered torn down, then the building is a constructive total loss, and the ordinance exclusion does not apply. Maryland Casualty Co. v. Frank, 452 P.2d 919 (Nev. 1969) ("The loss was caused by the fire, and the condemnation order was merely an unchallenged recognition of the loss." Id. at 920.); Midwood Sanatorium v. Fireman's Fund Ins. Co., 261 N.Y. 381, 185 N.E.2d 674 (1933). See Stahlberg v. Travelers Indem. Co., 568 S.W.2d 79 (Mo. App. 1978) ("The general rule is that if repair or reconstruction of a building damaged by fire is prohibited by municipal ordinances acting under proper authority of law, recovery may be had by the insured as for a total loss." Id. at 84. Stahlberg cites many cases on this matter.).
 2. Increased repair costs (a/k/a "betterment") mandated by ordinance are not covered, however. The doctrine of constructive total loss does not apply. Bradford v. Home Ins. Co., 384 A.2d 52 (Me. 1978). See Breshears v. Indiana Lumbermens Mut. Ins. Co., 256 Cal. App. 2d 245, 63 Cal. Rptr. 879 (1967).
- F. Deterioration. Many homeowners' policies exclude deterioration. The theory is that if deterioration were included, then the insurance contract would be a maintenance agreement. Murray v. State Farm Fire & Casualty Co., 219 Cal. App. 3d 58, 268 Cal. Rptr. 33 (1990). In Murray, electrolysis caused a copper pipe to leak. The leakage resulted in settlement damage. The court upheld the insurer's denial of liability under the deterioration exclusion, saying that the term "deterioration" excluded not only normal and predictable deterioration, but all types, included unexpected--albeit gradual--deterioration. The court rejected the view that there was an ensuing loss.
- G. Ensuing Loss. There are exceptions to exclusions, as already stated. One common exception involves ensuing losses. When this phrase, or its cognates, creates an exception to an exclusion, the insurer agrees to pay for the excluded losses, although it will not indemnify for that which is itself excluded. Employers Casualty Co. v. Holm, 393 S.W.2d 363 (Tex. Civ. App.--Houston 1965, no writ).
1. Obviously, there is much room for controversy over that which is excluded and that which is ensuing (and hence not excluded). Exclusions for which

there are ensuing loss exceptions are not exclusions as to perils insured against, but exclusions as to the kind of physical loss insured against. Frequently, however, the distinction is not apparent from the face of the policy.

- H. Other Exclusions. There are many other exclusions in virtually every property policy. An exclusion for power failure is common; such an event might lead to pollution. It is not unusual to exclude losses resulting from seeping water. That, too, might lead to pollution. In any case, the exclusions, their wording, and their relationship to named perils (if any) is an extremely important part of the lawyer's coverage evaluation.
- I. Interaction Among Exclusions. It is extremely important to look not only at each individual exclusion, but at how they interrelate. An exception to one exclusion may trigger another or may nullify another.
1. If the face of the opinion tells the real story, it cost National Fire \$10 million to learn this lesson. See National Fire Ins. Co. v. Valero Energy Corp., 777 S.W.2d 501, 505-06 (Tex. Civ. App.--Corpus Christ 1989, writ denied.)
 2. The fact that exclusions constitute a system creates possibilities for inspired lawyering. In a radiation contamination case, attorneys for the insured argued that the presence of a narrow nuclear exclusion, which arguably did not defeat coverage, rendered the more general contamination exclusion, which arguably did defeat coverage, inapplicable. That particularly elegant argument failed. Falcon Prods., Inc. v. Insurance Co. of Pa., 615 F. Supp. 37 (E.D. Mo. 1985).
- J. Exclusions & Public Policy. An intermediate appellate court in New Jersey has found it necessary to hold that a judiciary may not nullify contract exclusions on the grounds of public policy. Summit Assocs. v. Liberty Mut. Fire Ins. Co., 229 N.J. Super. 56, 550 A.2d 1235 (1988). The lower court had nullified the "owned property" exclusion in a liability policy because of the very strong New Jersey public policy regarding environmental cleanup. The appellate court flatly reversed the trial court. Some contract provisions are nullities as the result of public policy. An agreement to commit a murder, for example, is not enforceable in any way. Of course, in that case, a statute is violated. There are public policies which abrogate contracts where no statute is involved. For example, some persons lack the capacity to contract as a matter of law, even though no statute is involved. This is a manifestation of a public policy to

protect the infirm. The New Jersey Appellate Court may be saying any one of three things. First, it may be saying that you cannot abrogate contracts, in part, on the basis of public policy. Second, it may be saying that environmental public policy is not the sort of public policy which can be utilized to nullify contracts. Or third, it may be complaining about the retroactivity of the lower court's decision. It is unquestionably, the lower court's decision was lacking in subtlety.

XII. What types of losses are insured? This is the third crucial question which every lawyer analyzing a property policy for pollution coverage must ask. In general, there are two types of losses brought within the insuring agreements of property policies.

A. Physical Losses. Property policies generally insure against physical loss. The wording of the insuring agreement varies. Sometimes insurance is simply against "direct loss"; sometimes it is for "physical loss"; sometimes it is for "direct physical loss"; and sometimes it is for "physical loss or damage";

1. Where the word "damage" occurs along with the word "loss", the courts will look to the definition of "property damage" in CGL policies for guidance. This is especially true when the policy is a package policy, containing both property and liability elements.

a. Some lawyers believe that the term "property damage" should be avoided in pollution/property insurance litigation, whenever possible. They are concerned that the phrase "property damage" will be somehow imported from the liability policies.

b. Courts may look to the definition of property damage in any case; indeed, they are likely to do it in pollution coverage disputes, since the existence of property damage has been hotly contested in pollution-related liability coverage disputes.

2. In general, entities which are burned, broken, split asunder, and so forth, have sustained the requisite loss. Contrariwise, if an insured merely suspects that an entity may have suffered, say, internal fissures, and as a result that there has been a drop in the market value of the object, damage has not thereby been established. Glen Falls Ins. Co. v. Covert, 526 S.W.2d 222, (Tex. Civ. App.--Beaumont 1975, reh'g denied). Moreover,

mere loss of use is not a covered loss. Similarly, a denial of access to a building, without some actual physical damage, is not covered Cleland Simpson Co. v. Firemans Ins. Co., 392 P.2d 67, 140 A.2d 41 (1958). And, of course, title defects are not normally recoverable. Nevers v. Aetna Ins. Co., 14 Wash. App. 906, 546 P.2d 1240 (1976); Fruehauf Corp. v. Royal Exch. Assurance, 704 F.2d 1168 (9th Cir. 1983).

3. On the other hand, losses due to conversion are compensable under the policy, even if the physical objects insured are not smashed up. Great Northern Ins. Co. v. Dayco Corp., 637 F. Supp. 765 (S.D.N.Y. 1986); Buckeye Cellulose Corp. v. Atlantic Mut. Ins. Co., 643 F. Supp. 1030 (S.D.N.Y. 1986). (In Dayco, the conversion arose out of a complex and intentional swindle perpetrated on Dayco by an international trading consultant, with the (mostly) inadvertent assistance of corrupt Dayco employees. In Buckeye Cellulose, there was no coverage. The court acknowledged that conversion losses were usually covered in all risk policies, but found that the particular policy at issue provided neither coverage for conversion nor coverage for the kind of property at issue. The court's decision turned on some rather complicated interactions between insurance policy and the use of letters of credit in international trade.) The point in discussing these commercial conversion cases in a pollution outline is quite simple, although the cases themselves are not. First, the concept of physical loss is not always clear. Some imagination may be required. Second, sometimes insurance coverage decisions turn on precise terms contained in a policy.
4. More importantly, if a building becomes uninhabitable as the result of seeping odor, there may be a physical loss. Western Fire Ins. Co. v. First Presbyterian Church, 437 P.2d 52 (Colo. 1968). In that case, gas seeped into a church basement, and the town fire department shut the church down. The Colorado Supreme Court claimed that the action of the fire department could not be viewed in splendid isolation, but must be thought of in its proper context, which was as a consequential result of the accumulation of gasoline entering a church, which so infiltrated and saturated the building as to make it uninhabitable and made further use of the building highly dangerous. The Court classified this as a direct physical loss. (Some lawyers regard Western

Fire as the most important pollution-property insurance case.)

5. The requirement that the physical loss be "direct" has been considered from time to time. Fred Meyer, Inc. v. Central Mut. Ins. Co., 235 F. Supp. 540 (D. Or. 1964). See also North River Ins. Co. v. Clark, 80 F.2d 202 (9th Cir. 1935). The directness requirement is something like a proximate causation of requirement. It is unclear whether the presence of asbestos in buildings constitutes direct physical loss. See Paris at M-6. Prompt notice requirements are usually subject to a requirement that the delay substantially materially prejudiced the property insurer. Compagnie des Bauxites de Guinne v. Insurance Co. of N. Am., 724 F.2d 369 (3d Cir. 1983); Brakeman v. Potamoc Ins. Co., 472 Pa. 66, 371 A.2d 193 (1977); Colonial Gas Energy Systems v. Unigard Mut. Ins. Co., 441 F. Supp. 765 (N.D. Cal. 1977). See Blaine Richards & Co. v. Marine Indem. Ins. Co., 635 F.2d 1051, 1056 (2d Cir. 1980). See also Grzadzielewski v. Walsh County Mut. Ins. Co., 297 N.W.2d 780, 784-85 n.2 (N.D. 1980).
 6. Similarly, when a repeated flooding of a river isolated a dwelling so as to make it unusable, there was a direct physical loss under flood insurance. Gibson v. Secretary of U.S. Dept. of Housing, 479 F.2d 3 (M.D. Pa. 1978). Gibson sharply distinguished a dwelling (in effect, a homeowner's) case from a commercial case, and acknowledged that a loss of use doctrine might be applicable in a commercial case.
 7. Sometimes, policies do not insure against all types of physical loss. Sometimes, various types of physical loss are also excluded. Frequently, this is done by exclusions which are grouped together with clauses excluding perils from the list of those insured against. This elision is usually not a source of meaningful confusion. Nevertheless, the two matters are conceptually distinct. For example, contamination is perhaps better viewed as a condition of property, rather than a peril which might cause damage. Perhaps corrosion should be viewed the same way.
- B. Debris Removal. Most property policies agree to pay for the removal of some debris. Here is typical language: "This policy covers expense incurred in the removal of debris of the property covered hereunder [buildings and certain personalty] which may be occasioned by loss, by a peril insured against. The total amount recoverable

under this policy shall not exceed the limit of liability stipulated for each item." Another typical "Debris Removal" clause is as follows: "We will pay your expense to remove debris of Covered Property caused by or resulting from a Covered Cause of Loss."

1. This clause appears to mean, and the main insurance industry believes, that there is no agreement to pay for the removal of debris, unless three conditions are met:
 - a. there is debris;
 - b. the debris is the remains of covered property; and
 - c. that which (proximately) caused the covered property to become debris is a peril insured against (and not excluded).

2. The key case construing the debris removal clause is Lexington Ins. Co. v. Ryder System, Inc., 142 Ga. App. 36, 234 S.E.2d 839 (1977). Some lawyers regard this case as right up there with Western Fire when it comes to important pollution-property insurance cases. In Ryder, oil leaked out of an underground storage tank. The insurer paid for the oil, but refused coverage for the cost of removing the oil from the ground. The insurer suggested that the escaped oil was not debris.
 - a. The court declined the gambit and found coverage. The Ryder court did not justify its holding but courts would look to dictionaries, common linguistic custom, and trade usages. Query: Is "debris" ambiguous?
 - b. The debris removal clause at issue in Lexington provided coverage for "the cost of demolition and removal of debris formerly an insured part of the property and no longer suitable for the purpose for which it was intended." The insurer put a good deal of emphasis on the word "and" and refused coverage because no demolition was required. The court held that demolition and removal were not separate acts. In effect, the court observed that the insurer provided coverage for the single activity, demolition-and-debris-removal. The court pointed out that the insurer would have paid for removing the ashes of a completely burned building, even though there was no demolition.

- c. The logic of the court's demolition argument is not completely clear. At one point it appears to suggest that the term "demolition" is ambiguous and will be construed in favor of the insured. It also appears as though the court is implicitly relying on the doctrine of reasonable expectations. See Compass Ins. Co. v. Cravens, Dargan & Co., 748 P.2d 724 (Wyo. 1988).
 - d. For a thoughtful critique of the doctrine of reasonable expectations, see K. Abraham, Risk 101-33 for an application of his critique to the environmental area, see Abraham, Limits 960-61 ("judge-made insurance also destabilizes the insuring function" and constitutes a "mandatory retroactive price decrease").
3. Knoll includes a systematic and lengthy discussion of debris-removal coverage at 252-262. Also there is an interesting speech-outline concerning leaking underground storage tanks. Butler, First Party Coverage Continued/With An Emphasis On Leaking Underground Storage Tanks, in Insurance Coverage For Environmental Claims H-1 (Defensive Research Institute, 817C, Chicago, IL, Nov. 17-18, 1988).

XIII. Are there substantive conditions subsequent which might defeat coverage?

- A. Property policies frequently suspend coverage during any period of time when the insured increases the risk. (Some policies list this as an exclusion, but it is really something like a condition subsequent for avoiding coverage.) Once court classifies it as a promissory warranty. National Union Fire Ins. Co. v. Richards, 290 S.W. 912 (Tex. Civ. App.--Waco 1927, no writ).
- B. The problem of increase of risk (or increase of hazard) has been considered a number of times.
 - 1. Property insurers insure against risks inherent in the business of the insured at the time the policy was issued. Hence, the insurer is deemed to know the nature and extent of the risks it insured against, including the normal and customary hazards inherent in the insured's business. If an insurer does not intend to insure against the risk which is "necessarily incident" to the business of its policyholder, it must exclude that risk expressly. Triple-X Chemical Labs. Inc. v. Great Am. Ins. Co., 54 Ill. App. 3d 676, 370 N.E.2d 70 (1977).

2. On the other hand, if the insured substantially changes its business, so that new "material and substantial" hazards are introduced, then it will be unjust for the insured to be bound. Smith v. Peninsula Ins. Co., 181 So.2d 212, 217 (Fla. App. 1966, reh'g denied).
 3. Transient, temporary increases do not suspend coverage. Orient Ins. Co. v. Cox, 218 Ark. 804, 238 S.W.2d 757 (1951).
 4. "The negligence of misjudgment of the insured" which increased the risk and "caused the loss . . . is insufficient to," void coverage. Plaza Equities Corp. v. Aetna Casualty & Sur. Co., 372 F. Supp. 1325 (S.D.N.Y. 1974). (In this case, an insured mounted a statue over a skylight, and it crashed through the skylight. The importance of this case is that an insured can deliberately perform an act he negligently fails to realize will increase the risk, and he hasn't increased the risk for the purposes of property insurance law. This principle has obvious applications in the contest of pollution.)
 5. According to some courts, if the hazard is increased without the insured's knowledge, or in a way which is outside his control, then he has not increased the risk, and coverage is not avoided or suspended. Richards, 290 S.W. 912. (The insured rented a dwelling to others. They, in turn, rented rooms to still others, thereby converting a dwelling to a boarding house and thereby increasing the risk. The insured did not know what his tenants were doing, and so the increase in the risk was outside his knowledge and control. In Richards, the insured's lack of knowledge was arguably negligent, but more significantly preventing the activities of his tenants was within his control. He could have forbade contractually or made it his business to know what his tenants were doing. The term "control" is a weasel-word, and since it works a forfeiture, it will be construed strictly against the insurer.)
- C. Whether there has been an increase in the hazard is a jury issue.

XIV. Was the loss fortuitous?

- A. Definition. Property insurance policies insure only fortuitous losses. Losses which are certain to happen, or which are intentional, are not the sort of thing for

which insurance is available. The certainty of loss "is generally, though not invariably, considered from the point of view of the person (usually the insured) whose interest is the basis of an insurance claim." R. Keeton & A. Widiss, Insurance Law § 5.3(a), at 475 (1988). See Employers Casualty Co. v. Holm, 393 S.W.2d 363 (Tex. Civ. App.--Houston 1965, no writ). See also Essex House v. St. Paul Fire & Marine Ins. Co., 404 F. Supp. 978 (S.D. Ohio 1975).

- B. Intended & Expected. Fortuity in property policies is frequently subject to dispute. If a pollution claim becomes a significant source of controversy under property insurance policies, fortuity will be hotly disputed. Courts will probably look for guidance to the "intended or expected" cases under liability policies.
- C. Fortuity & Pollution. A number of pollution incidents, particularly waste disposal, turn out to be intentional, even deliberate acts and courses of conduct. In general, the principle of fortuity bars insurance for intentional actions. But things are different when the act is intentional, but the consequence unintended and not reasonably foreseeable. Obviously, the principle of fortuity will pervade pollution/property insurance disputes.

XV. What about the moral hazard?

- A. Insurers will also, doubtless, argue that courts should take a jaundiced view of coverage for pollution losses on the grounds that such coverage would increase the moral hazard.
 - 1. In general, the moral hazard is the increased probability that a socially unacceptable event will occur, simply as the result of the existence of insurance coverage. K. Abraham, Risk at 14-15 and 35-36; Abraham, Limits at 946-47 and 952. See S. Shavell, Economic Analysis Of Accident Law 194-95 (1987). For English usage, which is somewhat different, see E. Ivamy, General Principles Of Insurance Law 134-36 (5th Ed. 1986).
 - 2. There is clearly a public policy against pollution, and some argue that governmentally-mandated pollution cleanup expenses should not be passed on to insurers, because of legislative intent that polluters should pay and because the existence of insurance will decrease statutory incentives to refrain from polluting. See Boeing v. Aetna, 113 Wash. 2d 869, 784 P.2d 507 (1990) (C. J., dissenting). Similar arguments can be made from the area of property insurance. For a spirited

critique of the insurance industries point of view, see Anderson & Luppi, Government Officials Are Calming the Environmental Insurance Coverage Frenzy, 4 Mealey's Litigation Reports: Insurance (April 24, 1990). The author's firm regularly represents policyholders in insurance coverage disputes, and he argues vigorously (perhaps hysterically in spots) that the insurance industry view of the intended and expected proviso, the meaning of the phrase "property damage," the meaning of the phrase "as damages," and the meaning of the pollution exclusion are all self-serving, without historical foundation, erroneous, and contrary to public policy. Anderson interestingly points out that the government regularly files *amicus* briefs on behalf of policyholders. Public policy may favor the insurance industry, but government policy does not. (Is that a paradox, or what?)

- B. These arguments are more background arguments, rather than direct attacks of the existence on coverage. The existence, or nonexistence of coverage will depend upon the wording of the policy. Considerations such as public policy on pollution and problems associated with a moral hazard may affect the attitudes and inclinations of the judges, thereby indirectly affecting how the language is construed.

XVI. When did the loss occur? This is the fourth crucial question the lawyer must ask.

- A. If a policy of insurance is a contract transferring risk for a specified duration of time, the loss must occur within the duration of the policy, or there is no contractual transfer of risk.
- B. Hence, another way to put the fourth crucial question is this. At what point does the potential or contingent liability of the insured to indemnify the insured for a covered loss become converted into a contractual obligation to indemnify? This is usually called the question of "trigger."
 - 1. Questions of trigger have not, as such, been prominent issues in a property insurance litigation. Issues of notice and limitation had a much higher profile.
 - 2. Appearances are somewhat deceiving, however. Notice intervals and limitation intervals are frequently tied to some sort of coverage trigger. As a result, issues of notice and issues of limitation are sub rosa trigger issues.

3. Moreover, questions of trigger are explicitly important when there are successive carriers. See Hook, Multiple Policy Period Losses and Liability Under First-Party Policies, 21 Torts & Ins. L.J. 393 (1986).
- C. So, when does a loss take place? Does it take place when the last event physically necessary to cause insured injury occurs? Is it when injury itself occurs (whether observed or not)? Does it occur when the injury is first observed? Or does it occur when the injury first could have been observed by a reasonably observant (but not omniscient) person?
- D. Many property policies prescribe that the insurer shall be notified of a loss within a specified period of time after the "inception of the loss." This phrase is utilized mostly to regulate notice and determine when a suit must be brought. Nevertheless, it might be used to determine trigger as well. The trigger question would then become: When is the inception of a loss?
1. Conceptually, and therefore necessarily, the term "inception" refers to the beginning. Hence, if the inception of a loss constitutes the trigger, then insurance is triggered at the beginning of that loss. (Notice, on this view, the trigger would not be the inception of the proximate causal chain leading to the loss. It would be the inception of the loss itself.)
 2. The Inception of Loss rule would make a good deal of sense as a trigger rule for ordinary losses, but it is not clear how well the rule would work for losses which begin as invisible losses and then creep--progressively--towards observable catastrophes. (In effect, this raises the semantic--or perhaps philosophical--question: When does decay become a loss?)
- E. Not all policies utilized "inception" language. Some state that they will cover loss or damage "commencing during the policy." This type of "Policy Period" clause raises trigger problems with a vengeance.
1. On the other hand, such a "Policy Period" clause is probably better than one which simply states that "This policy applies only to loss to property during the policy period." Some property policies contain this language.
 2. Other property policies state that they will cover losses which occur during the policy period. These policies are closely analogous to CGL policies,

although, in the CGL policy, the occurrence is not the loss, but the cause of the injury giving rise to the liability claim.

- F. To the extent that the rule of law for trigger has been formulated for property policies, it has been formulated for the successive insurer situation. "[T]he general rule is that the date of manifestation determines which carrier must provide indemnity for a loss suffered by its insured." Home Ins. Co. v. Landmark Ins. Co., 205 Cal. App. 3d 1388, 253 Cal. Rptr. 277 (1988) (appeal pending) (masonry problems in a building of a continuing nature). What does this rule mean?
1. Trivially, it means that the insurer's potential liability becomes contractual rather than potential only at the time and on the date of manifestation. Id. at 280.
 - a. But what is manifestation?
 - b. Obviously, it is not the date that the last-necessary-cause occurred. Nor is it the date the injury takes place.
 - c. It is the date that the injury is manifested. But what date is that?
 - d. Is it the actual date of observation, or is it the date upon which observation could have been made under reasonable circumstances?
 2. Obviously, the Manifestation Rule of Home Ins. is different, in theory, than the Inception Rule. This theoretical difference has only occasionally made a practical difference, since most losses are manifested from their inception. It is not true in the context of pollution.
- G. The significance of Home v. Landmark is unclear. First, it was narrowly restricted to the facts stipulated in the case. Second, it is presently before the California Supreme Court on appeal.
- H. However, the very significant pollution/property insurance case of Western Fire, 437 P.2d 52, also makes manifestation the trigger of coverage.
- I. Physical damage to property caused by pollution will place the Manifestation Rule, the Inception Rule, the Commencement Rule, and the Occurred During Rule under substantial strain. Quite naturally, insureds will seek

some sort of discovery rule, so that manifestation--and even commencement or inception--are deferred until the insured knew what it was up against.

XVII. By what date must the insured be notified? This is the fifth crucial question. The lawyer analyzing a pollution property insurance problem must ask.

- A. Virtually all policies require notification as soon as possible.
- B. Most property insurance policies mandate the submission of a proof of loss in accordance with some schedule.
- C. Many property policies require notice within a fixed interval--one year, two years, three years--after the inception of the loss. (Of course, a notice can fail to be prompt, even though it is within the fixed interval. The purpose of the fixed interval is to eliminate a long tail.)
- D. Traditionally, the absolute timetable within which notice must be given is not subject to a discovery rule. Avis v. Hartford Fire Ins. Co., 195 S.E.2d 545 (N.C. 1973); Sager Glove Corp. v. Aetna Ins. Co., 317 F.2d 439 (7th Cir. 1963), cert. denied, 375 U.S. 921 (1963) (under-discovered vandalism); Marshburn v. Associated Indem. Corp., 84 N.C. App. 365, 353 S.E.2d 123 (1987); Harris v. Hanover Fire Ins. Co., 425 F.2d 1168 (5th Cir. 1970) (part of a loss undiscovered).
- E. The no-discovery-rule-for-fixed-notice-clauses is under some stress. Prudential-LMI Commercial Ins. v. Superior Court, 211 Cal. App. 3d 1131, 260 Cal. Rptr. 85 (1989). This case was cited by the same court which decided Home v. Landmark. The Court of Appeals decision in Prudential-LMI has been vacated by order of the California Supreme Court. It is therefore bereft of precedential value until the appeal is decided.
 - 1. Prudential-LMI involved progressive soil subsidence damage. The issue was "whether an insured is required to comply with an internal policy notice of claims provision and one-year suit limitations when the claimed loss could not reasonably have been discovered within the policy period." The court held that "for purposes of assessing the timeliness of the filing of a claim and action thereon, a delayed discovery rule must be applied such that the time at which the insured is required to take action to enforce his or her rights begins to run at the point at which a reasonable person would be found to be in possession of facts placing

him or her on notice of a possible defect in the property." Id. at 86.

2. Obviously, the holding in Prudential-LMI is at substantial variance with the established rule of many jurisdictions. Perhaps, it is consistent with earlier California law. See Zurn Engineers v. Eagle Star Ins. Co., 61 Cal. App. 3d 493, 132 Cal. Rptr. 206 (1976).
3. The reasoning employed by the Prudential-LMI court is abstruse.
 - a. The court relies upon asbestos trigger cases which arose in conjunction with personal injury. These insurance policies are conceptually quite different.
 - b. The court also stated that "[a]s a matter of policy, we seek to interpret the claims requirement and one-year suit limitation period in such a manner as to avoid forfeiture of claims on procedural grounds, in order to allow coverage issues for potentially meritorious claims to be litigated on the merits." Prudential-LMI, 260 Cal. Rptr. at 93.
 - (1) Obviously, it is appropriate to interpret language so as to avoid a forfeiture. It is not appropriate to read new terms into a policy, in order to circumvent contractually prescribed results.
 - (2) This is especially inappropriate where the notice provision is mandated or authorized by state statute.

XVIII. By what date must suit be filed? This is the sixth crucial question which the lawyer must ask.

- A. Virtually all property policies contain some contractual provision regarding limitation. General State Authority v. Planet Ins. Co., 464 Pa. 162, 346 A.2d 265 (1975).
- B. It is extremely important to examine each individual provision to determine how long the period is and what triggers it. See Florsheim v. Travelers Indem. Co., 75 Ill. App. 3d 298, 393 N.E.2d 1223 (1979).
- C. The issue of a discovery exception to a limitation on suit provision is just beginning to be explored. Naghten v. Maryland Casualty Co., 47 Ill. App. 2d 74, 197 N.E.2d 489 (1964) (This case involved a progressive loss which

him or her on notice of a possible defect in the property." Id. at 86.

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was discovered in plenty of time. In dicta, the court implied it might come to a different conclusion if discovery were really an issue. Id. at 490-91.). Nevertheless, most courts treat the limitation provision as absolute.

XIX. What about bad faith?

- A. Property insurers are getting hit for big exemplary damages in bad faith cases. Valero may be the largest in this state, but it is by no means it is the only one.
- B. A property insurance lawyer examining a policy for coverage should not ask whether it would be bad faith to deny claim. He should recommend the claim be denied only if it should be denied, not if it wouldn't be bad faith to deny the claim.
- C. It should also be remembered that wrongful denial is not the only legal foundation for bad faith. Judah v. State Farm Fire & Casualty Co., 217 Cal. App. 3d 1181, 266 Cal. Rptr. 455 (1990) (appellate petition for review granted, 26 Cal. Rptr. 541, 789 P.2d 341).

XX. What is in the interest of justice? It should be remembered by everyone, that the legal system is for doing justice, and that lawyers, above all, should have a passion for it. R. Solomon, A Passion for Justice (1990).