

## MAJOR VICTORY FOR POLICY HOLDERS

*California Supreme Court Reaffirms Insurance Companies' Expansive Duties to Provide a Legal Defense of Environmental Claims.*

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by Mark D. Harrison, Esq.

When environmental contamination is at issue, many insurance companies beat a hasty retreat, leaving policy holders on their own to defend against costly litigation. Two recent landmark California Supreme Court decisions, however, have strongly reaffirmed policy holders' rights to receive a legal defense, paid for by their insurance companies, against environmental lawsuits. These California Supreme Court decisions represent an important victory for policy holders across the state.

### THE ISSUE

The rapid growth of environmental regulation and litigation has had profound effects in the area of liability insurance. Insurance companies have become keenly aware of the substantial risks and costs associated with environmental contamination. Older liability policies had no specific provisions excluding environmental damages from coverage. Currently, insurance companies attempt to absolve themselves of all responsibilities for environmental claims with so-called "absolute pollution exclusion" clauses. Needless to say, insurance companies and policy holders have rarely agreed on the proper interpretation of liability policies, even with pollution exclusion clauses, in the context of an environmental claim.

Insurance companies have two primary duties under the terms of a typical liability policy. The first duty is known as the "duty to defend" which requires the insurance companies to pay all costs of legal defense. The second duty is the "duty to indemnify." The duty to indemnify "requires insurance companies, in addition to paying for the cost of defense, also to pay any settlement or judgment assessed against the insured, up to the limits of the policy."

When policy holders receive a claim (by way of law suit or otherwise) they notify their insurers and request a legal defense of the claim. Initial insurance disputes, therefore, are invariably concerned with the insurance companies' duty to defend. For the insured, obtaining a defense is no trivial matter. Environmental litigation is expensive and complex. Few insureds have sufficient resources to independently fund litigation of this type. The expense associated with environmental litigation is also the reason insurance companies seek to limit their defense obligations.

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The dispute regarding the duty to defend boils down to two key questions: 1) What must policy holders establish in order to trigger the duty to defend? and 2) Which insurance companies owe defense duties when the damages in question occurred over a series of years covered by different insurance policies?

Enter the California Supreme Court. In two recent decisions, which landed on the insurance industry with the force of small atomic explosions, the Court reaffirmed in the broadest possible terms the rights of policy holders to be fully and fairly defended against environmental claims.

**MONTROSE CHEMICAL CORPORATION V. SUPERIOR COURT  
(MONTROSE I)**

On November 22, 1993, the Court issued its opinion in *Montrose Chemical Corporation v Superior Court*, 6. Cal. 4th 287 (1993). The Court held that in order to trigger the duty to defend policy holders must only show a possibility of coverage under the insurance contract. The Court specifically rejected the insurance companies' arguments that policy holders should be required to make a greater showing before the defense duty is triggered.

From 1947 to 1982 Montrose manufactured DDT at a facility in the Los Angeles area. In 1990 the United States sued Montrose. The suit alleged that Montrose's operation of this facility caused environmental contamination and damaged land, water and wildlife in the Los Angeles Harbor. Montrose was also sued by the Los Angeles County Sanitation District for the same alleged damages.

Montrose had purchased liability insurance from various carriers from 1960 to 1986. Montrose gave notice of these lawsuits to its insurance companies and requested that they provide a defense. Each carrier denied its duty to defend. Montrose went to court to obtain a determination that it was entitled to a defense of the lawsuits.

Montrose argued that the duty to defend is triggered whenever the claim may fall within policy coverage. The insurance companies argued that the correct test should be more restrictive, requiring Montrose to show a "reasonable potential for coverage."

In a strongly worded opinion, the Court rejected the insurance companies' arguments. The Court began by noting that "imposition of an immediate duty to defend is necessary to afford the insured what it is entitled to: the full protection of a defense on its behalf. The Court explained the practical meaning of this principle as follows:

[T]he insured need only show that the underlying claim may fall within policy coverage; the insurer must prove that it cannot. Facts merely tending to show that the claim is not covered, or may not be covered, but are insufficient to eliminate the possibility that resultant damages ... will fall within the scope of coverage, therefore add no weight to the scales.

The holding of *Montrose I*, therefore, prevents insurance companies from arguing that mere uncertainty as to whether a claim may eventually be covered somehow absolves them from their defense obligations. The question left unanswered by *Montrose I* was which insurers owe

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such defense duties where the damage may have occurred over many successive years and policy periods (for example, see page of hazardous substances). On July 13th, 1995 the Court provided the answer.

**MONTROSE CHEMICAL CORPORATION V. ADMIRAL INSURANCE COMPANY  
(MONTROSE II)**

In *Montrose Chemical Corporation v. Admiral Insurance Company*, 95 Daily Journal D.A.R. 8783 (July 13, 1995) the Court held that the potential for coverage, and the duty to defend, arises under all policies in effect during periods of continuous or progressive damage. Because the potential of coverage arises under such policies, so does the duty to defend of all the insurance companies.

The facts of Montrose II concern the same Los Angeles area chemical facility. Between 1960 and 1986 seven different carriers, including Admiral Insurance Company, furnished liability policies to Montrose. Montrose tendered the defense of various lawsuits to its insurance carriers. Admiral refused to provide a defense primarily on the basis that the damage (the alleged contamination by hazardous substances) did not occur within Admiral's policy periods. Admiral took the position that coverage is triggered when the damage is first discovered. Admiral argued that because the contamination was first discovered before the start of Admiral's policies no possibility of coverage existed and no duty to defend arose. Montrose, on the other hand, argued that damages that are continuous or progressively deteriorating throughout successive policy periods are covered by all policies in effect during those periods (a theory known as the "continuous injury trigger.")

The Court rejected Admiral's contentions in their entirety. The Court established the continuous injury trigger as the rule in California:

We therefore conclude that the continuous injury trigger of coverage should be applied to the underlying ... claims of continuous or progressively deteriorating damage or injury alleged to have occurred during Admiral's policy periods. Where, as here, successive ... policy periods are implicated, [damage] which is continuous or progressively deteriorating throughout several policy periods is potentially covered by all policies in effect during those periods.

The holding in Montrose II, therefore, closes a significant escape hatch that insurance companies have used to limit their defense obligations. Under Montrose II, policy holders should be entitled to a defense from each of the insurance companies that provided coverage during the periods that the contamination was released and was progressively migrating through soils and groundwater.

**CONCLUSION**

Montrose I and Montrose II clear the way for policy holders to obtain what they are entitled to under their insurance policies: a full and immediate legal defense. Although each individual case depends on its own specific facts, policy holders who have had their claims denied should

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immediately determine whether such denial was proper in light of these significant California Supreme Court decisions.

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