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Climate Change Exposure In The Insurance Field

Law360, New York (June 29, 2010) -- Several types of climate change-related litigation are emerging or may soon emerge that could result in potential claims liability for an insurer:

(1) nuisance and other tort claims, as in Connecticut v. AEP, 582 F.3d 309 (2d Cir. 2009); Comer v. Murphy Oil USA Inc., No. 07-60756, 2010 WL 2136658 (5th Cir. May 28, 2010); and Kivalina v. ExxonMobil, 663 F. Supp. 2d 863 (N.D. Cal. Sept. 30, 2009) (on appeal);

(2) products liability claims alleging that products, such as cars and other products that emit greenhouse gases, are defective as designed;

(3) natural resource damage claims based on Comprehensive Environmental Response, Compensation and Liability Act or state law;

(4) regulatory enforcement actions related to GHG emissions — if GHG emissions limits are enacted;

(5) shareholder, U.S. Securities and Exchange Commission, or state actions related to misrepresentation, concealment or mismanagement of climate change-related risk; and

(6) a variety of claims against service providers arising out of efforts to fix the climate change problems, such as claims related to preparation of environmental impact statements and mitigation strategies pursuant to federal and state environmental policy acts; claims related to preparation of carbon footprints; disputes related to emerging carbon markets; greenwashing litigation related to allegedly green products; green building litigation; and failures of emerging technologies such as carbon capture sequestration and alternative energy.

Although some climate change-related claims may not ultimately be successful, they nonetheless could be costly for an insurer due to defense costs. These types of cases have the potential to affect many types of coverages. Depending on the nature of the claim, multiple types of coverage also could be triggered simultaneously. For example, a court could construe a commercial general liability pollution exclusion narrowly and conclude that GHGs are not pollutants barring coverage, while at the same time concluding that GHGs are pollutants for purposes of a coverage grant in an environmental liability policy. Some of the potential implications of climate change-related claims for each general policy type are as follows:

Implications for Property, Accident and Health

Episodic climatic events (e.g., hurricanes, winter storms, fires, etc.) will continue to result in first-party claims under personal and commercial property policies. If projections of climate change effects are accurate, then there will be increased frequency and severity of such claims. Insurers likely will continue to use their existing systems for predicting and monitoring severe weather events regardless of whether these events are caused by climate change. These should continue to be updated as the science evolves.

Implications for CGL

Customers hit with climate change-related tort lawsuits likely will look to CGL policies for coverage because CGL insurance generally provides broad coverage for defense and indemnity of claims for bodily injury, personal injury and property damage (potentially including natural resource damages). Insureds also may look to CGL coverage for advertising injury liability in the climate change context because builders and architects in the green building industry, as well as manufacturers of emitting products, may be subject to greenwashing claims if they misstate the green nature of their buildings and products.

CGL product liability policies also may be implicated by new climate change-related claims. Although no climate change-related products liability claims have been made thus far, it is possible that individuals could bring products liability claims against an insured, such as failure to warn or design defect claims related to products that emit GHGs. CGL is a particular source of exposure because there is potential liability on historic occurrence-based policies and the policies generally have defense in addition to policy limits. Even if climate change-related tort cases are not ultimately successful because of causation and other uphill battles, defense costs could be high.

CGL policies have pollution exclusions, known loss or loss in progress exclusions, expected or intended exclusions, contractual liability exclusions, and batch clauses that may be relevant in the climate change context, but these provisions will not entirely prevent exposures and will be heavily litigated in various jurisdictions.

In Steadfast v. AES, the first climate change coverage case, Steadfast litigated whether:

(1) GHG emissions can qualify as an occurrence,

(2) the known loss or loss in progress exclusion bars coverage, and

(3) the pollution exclusion bars coverage in the climate change-related tort suit, Kivalina.

The Virginia court granted summary judgment in favor of Steadfast because it held there was no occurrence. The court did not reach the pollution exclusion issue under Virginia law and the case is now on appeal. Interpretation of the pollution exclusion in the GHG context will be a hot topic in the future. Jurisdictions applying a traditional pollution doctrine may not consider a GHG to be a pollutant and others could rely on the U.S. Environmental Protection Agency or other governmental determinations about GHGs and find that a GHG is a pollutant. Accordingly, litigation regarding the applicability of these policy provisions in multiple jurisdictions likely will be costly.

Implications for Directors and Officers

In recent years, shareholder resolutions related to climate change have been on the rise, and investors have demanded increased disclosure of climate change-related risk. Voluntary disclosure programs abound. SEC has issued guidance on shareholder resolutions that impacts climate change-related resolutions, and has issued guidance specifically addressing climate change disclosure.

The National Association of Insurance Commissioners also has been active in the climate change disclosure area, although it reversed course this year on a mandatory climate risk disclosure survey for insurers. In this political climate, directors and officers eventually may face class actions and/or derivative actions by shareholders if a corporation, or its directors and officers, fail to disclose, misrepresent or mismanage climate change-related risk and such failures result in harm to a corporation, such as loss of revenues, market share, falling stock price, reputational damage, and/or missed business opportunities related to climate change issues.

Insureds facing claims related to concealment, misrepresentation or mismanagement of climate change-related risk likely will seek reimbursement of defense costs and indemnification under D&O policies. Most of these policies (except for some new Zurich Financial Services Ltd. and Liberty Mutual Insurance Co. products) do not specifically address whether climate change-related claims are covered. Some policies have pollution exclusions or pollution-related exclusions.

Courts will have to determine whether pollution exclusions apply to claims arising out of misrepresentation of or failure to identify climate change-related risks as opposed to claims arising more directly from climate change just as they have done in the asbestos context. See, e.g., Sealed Air Corp. v. Royal Indemnity Co., 961 A.2d 1195, 1201 (N.J. Super. Ct. App. Div. 2008). The particulars of any intentional/fraudulent acts exclusion, definition of loss, limits of liability provision related to interrelated wrongful acts, bodily injury and property damage exclusions also should be evaluated but likely will result in little, if any, reduction in exposure to insurers in this context.

Implications for Environmental Liability

Environmental liability insurance generally covers damages and cleanup costs arising out of "pollution events" at, on, under or migrating from locations covered in the policy and defense costs associated with such events. Thus, it is highly likely that insureds facing climate change-related claims will seek coverage under environmental policies. Whereas any conclusion that GHGs are pollutants for purposes of pollution exclusions could decrease exposure under CGL policies, a determination that GHGs are pollutants will increase insurer's exposure under environmental policies. Moreover, given recent political developments with EPA and Congress, it will likely become increasingly difficult for insurers to claim that GHGs are not pollutants. Thus, climate change will present a special risk in the environmental liability insurance field.

Insureds may try to seek coverage under environmental liability policies for tort claims arising out of episodic environmental events, other common law tort claims (such as AEP, Kivalina, and Comer) and statutory environmental claims, such as natural resource damages under CERCLA. In addition to tort lawsuits and CERCLA NRD actions, insureds may face statutory liability pursuant to the Clean Air Act or new GHG statutory schemes being contemplated by Congress. For example, insureds may attempt to seek costs of compliance through their environmental liability policies. Maintenance and improvement exclusions likely will prevent exposures for day-to-day operational costs, such as costs associated with Clean Air Act-related upgrades. The fact that most environmental policies are written on a claims-made as opposed to on an occurrence basis will temper some of this risk, because insureds will not be able to look to historic policies. Circumstance reporting of climate change events, however, may become more common place as insureds try to preserve their right to demand coverage for climate change events even under claims-made policies.

In evaluating coverage, the following provisions also should be considered: definition of natural resource damages; wrongful acts or deliberate noncompliance exclusion; injunctive relief exclusion; fines, penalties and punitive damages exclusion; and exclusions for pre-existing conditions and known pollution events. Limits of liability provisions for multiple claims arising out of the same pollution event, multiple insureds or claimants, multiple coverages, multiple policy periods and sublimits will not eliminate exposure but could bring the exposure within certain policy limits. Nevertheless, even if one of these provisions limited exposure, coverage battles over applicability of these provisions could be costly.

Implications for Professional/Errors and Omissions

Climate change-related claims could arise out of a wide variety of professional activities such as carbon footprinting, preparation of environmental impact statements and mitigation strategies, green building and greenwashing. As EPA, states and nonprofits demand disclosure of GHG emissions, professionals will be called on to account for or calculate GHG emissions for corporate clients for reports to EPA or other federal or state authorities. Regulated emitters will rely on professionals to help prepare reports pursuant to the EPA GHG Reporting Rule and in connection with preparation of environmental impact statements and mitigation strategies related to obtaining permits at the state and local level.

If professionals make mistakes in the course of doing such work, their customers may file claims against them. Professionals also could be subject to liability if there are problems arising from misrepresentations or mistakes made in connection with green building, installation of emissions reduction solutions and possibly handling of carbon credits. For example, if a professional fails to take the promised steps to mitigate GHGs in a “green building” project, causing a loss of LEED certification or loss of tax benefits, the client may have a suit against the professional. Finally, if a consultant assists a client in developing “green” products and the client is saddled with greenwashing claims, the client may, in turn, sue the consultant.

Professionals will seek coverage for these kinds of climate change-related claims. Exposure may be significant because professional liability policies often do not contain pollution exclusions and contractual liability and intentional/fraudulent acts exclusions will not significantly reduce exposure. Any exclusions for fines, penalties, taxes, and punitive, exemplary, and multiple damages and products liability may provide some reduction of exposure and thus should be considered. One limiting factor could be that the policies may have defense included within the policy limits. In light of the likely emerging claims and minimal impact of existing exclusions to control new exposures, it will be important to identify and monitor the evolving standard of care in this area.

This is just the tip of the iceberg for how the climate change debate will manifest itself as an insurance problem. Insurers should continue to monitor the climate change issue and evaluate how it will impact each line of business so that they can manage risks and maximize potential opportunities. Insureds who believe they may have potential climate change liability should evaluate their current insurance portfolios to ensure they have purchased adequate coverage for this emerging risk.

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