

MTBE: COVERAGE FOR THE PETROLEUM INDUSTRY'S "SPREADING" PROBLEM

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Most petroleum products are exempted from the reach of Superfund liability. See 42 U.S.C. § 9601(14) (exempting petroleum from the CERCLA/Superfund definition of "hazardous substance"). The law is set up this way for two basis reasons. First, petroleum is a naturally-occurring substance. It would be ludicrous to have to treat the La Brea tar pits as a Superfund site. Second, petroleum hydrocarbon products occupy a unique position in the global social and economic order.

What happens, however, when the government requires that you mix petroleum with something else? The mixture may hurt people or property. But if government requirements result in legal actions relating to substances exempted from Superfund liability, can your insurance company deny coverage based on a so-called absolute or total polluter's exclusion?

Methyl tertiary butyl ether (MTBE), a substance almost exclusively used as a fuel additive in gasoline, is one of a group of chemicals commonly known as "oxygenates"—they raise the oxygen content and burning efficiency of petroleum hydrocarbons. MTBE has been used in domestic gasoline at low levels since 1979 to replace lead as an octane enhancer. Since 1992, MTBE has been used at higher concentrations in some gasoline to fulfill the oxygenate requirements set by Congress in the 1990 Clean Air Act Amendments. MTBE

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is currently added to about 87% of the gasoline that is marketed, sold, and used in the United States.

MTBE's expanded use has caused increasing problems related to environmental liabilities for damage or injury. The principal source of MTBE contamination is leaking underground fuel storage tanks (commonly known as "USTs"). When MTBE spills or leaks into the ground, its chemical properties cause it to travel faster and further than other components of gasoline. The ultimate health impacts of exposure to MTBE have not fully been determined. It is a known animal carcinogen, however, and has been identified as a possible human carcinogen.

Legal actions involving MTBE contamination are on the rise. Throughout the United States, litigation has included MTBE claims based on negligence, conspiracy, property damage, and product liability. In April 2002, for example, after an 11-month trial brought by a California public utility against MTBE producers, oil refineries, and gasoline retailers, a jury found that gasoline containing MTBE was a defective product and that Lyondall Chemical Co., a manufacturer of MTBE, and Shell Oil Co., a refiner, acted maliciously by withholding information about MTBE's potential hazards. As a result, in August 2002 Shell agreed to pay \$28 million as part of an out-of-court settlement, bringing the total settlement in that action to over \$69 million. As evidence of the increasing notoriety of MTBE and as a possible harbinger of what is to come, a number of plaintiff personal injury law firms now include information relating to MTBE on their Web sites.

As MTBE-based claims increase, disputes concerning insurance coverage for those claims will also most assuredly increase. This article provides a framework for helping to determine how your insurance policies cover MTBE-related claims.

ANALYSIS

A. Cleanup for MTBE Contamination Should Trigger Insurance Coverage Under the Insuring Agreement

The plain meaning of the insuring agreement of the standard-form comprehensive general liability insurance policy indicates that the defense and indemnity obligations of the insurance company are triggered by third-party liability claims alleging property damage. MTBE contamination caused by a spill or storage tank leak routinely gives rise to such claims.

First, the large majority of jurisdictions that have addressed the issue of the "legal obligation to pay" hold that amounts paid to address government mandates in administrative enforcement actions are amounts that the policyholder "is legally obligated to pay as damages." Thus, costs to investigate and remediate MTBE contamination in response to a government directive

should be construed "as damages" that a policyholder is legally obligated to pay. Second, environmental contamination arising from gasoline containing MTBE is "property damage" and courts uniformly hold so. Such damage generally is to the property of a third-party because most states designate groundwater as a resource held in trust for all people so actual or potential threats to groundwater from MTBE are considered damage to the property of another. Third, "property damage" takes place or "triggers" coverage as long as the gasoline spill or leak was released into the environment at least in part during the policy period at issue.

B. Various Exclusions Relied Upon by the Insurance Industry

To deny insurance coverage for MTBE-related environmental damages, the insurance industry has (with varying degrees of success) relied upon the following exclusions/defenses to coverage: (1) the "expected or intended"/no "occurrence" defense; and (2) various forms of so-called polluter's exclusions.

1. "Expected or Intended" Defense

Based upon the typical "occurrence" definition, insurance companies routinely argue that coverage for "environmental" liabilities is barred because the policyholder "expected or intended" the property damage. There is a split of authority on the standard of proof applicable to this defense. Most courts hold that the relevant standard is a subjective one, i.e., the policyholder or, more often, company management must actually expect or intend the specific property damage and the resulting harm for coverage to be avoided. Some courts, however, hold that the relevant standard is an objective one, i.e., irrespective of the policyholder's actual knowledge or intent, coverage is barred only if the policyholder reasonably should have expected that property damage would take place. Whatever standard may be applied, as long as the MTBE contamination was not intended, expected, or reasonably should have been expected, the "expected or intended" defense should not preclude coverage for MTBE-related events and, accordingly, insurance companies have had marginal success with this defense.

2. The Various So-Called Polluter's Exclusions

a. The Qualified Exclusion—1970–1985

From the early 1970s through approximately 1985, most general liability insurance policies contained a qualified polluter's exclusion that purported to exclude coverage for "releases" and "discharges" of "pollutants" unless they were "sudden and accidental." The primary dispute over this "clarification" on coverage centers on whether the word "sudden" means "unexpected," or

always includes a temporal element requiring that a covered claim arise out of an event that is "abrupt, immediate, or of short duration." Some courts have held that the uncertainty alone creates an ambiguity favoring policyholders. Other courts have looked to contemporaneous statements to insurance regulators at the time the purported exclusion was introduced by the insurance industry. Irrespective of the interpretation or legal theory, an unintentional spill resulting in MTBE contamination should not be excluded under the "sudden and accidental" pollution exclusion. If a court reads a temporal component into the exception, however, then damage occurring over an extended period of time, such as a slow leak from an UST, may not be covered even if the pollution is unexpected and unintended.

Based on the insurance industry's representations to regulators that this exclusion would only bar intentional pollution, a number of courts throughout the country have rejected the insurance industry's attempts to escape environmental liabilities. The most comprehensive analysis of the history of the insurance industry's efforts to secure regulatory approval for the "sudden and accidental" pollution exclusion as a mere "clarification" (not a "restriction" that would have required premium adjustment) is set forth in the New Jersey Supreme Court's decision in *Morton International, Inc. v. General Accident Insurance Co.* The *Morton* court, applying a theory known as "regulatory estoppel," held that the standard form "sudden and accidental" polluter's exclusion does not bar insurance coverage except when the policyholder intentionally discharges a known pollutant. Accordingly, for a variety of reasons, many state courts have rejected exclusion of coverage for environmental liability pursuant to the "sudden and accidental" polluter's exclusion.

Another area of contention concerns whether the particular injury-producing agent is a "pollutant." Although there are no decisions resolving application of the so-called "sudden and accidental" polluter's exclusion to MTBE contamination, an argument could be made that because MTBE is a useful, environmentally friendly product, it is not a "pollutant," "irritant," or "contaminant" and, therefore, is not excluded under the "sudden and accidental" polluters exclusion. Such an argument has been accepted by some courts for gasoline itself as well as for lead paint, which is merely paint plus a paint additive—lead. If these useful products are not "pollutants," the useful gasoline additive MTBE should likewise not be deemed a "pollutant."

b. The So-Called "Total" or "Absolute" Exclusions 1985–Present

From approximately 1985 forward, the insurance industry will also rely upon the so-called "absolute" or the more recent "total" pollution exclusions to exclude coverage for MTBE contamination. These exclusions removed the "sudden and accidental" language. The main areas of litigation involve: (1) the

term "pollutant," which is the same as discussed previously; and (2) whether there has been an "actual, alleged or threatened discharge, dispersal, seepage, migration, release or escape" of the purported "pollutant."

As litigation surrounding the scope of environmental coverage mushroomed in the 1980s, the insurance industry, through the Insurance Services Office (ISO), an insurance industry trade organization that drafts and revises standard-form liability insurance policies and endorsements, drafted other pollution exclusions: first, the "absolute" pollution exclusion and then the "total" pollution exclusion. ISO specifically crafted these exclusions to exclude liability for CERCLA-directed cleanup of damage to the natural environment. Courts generally have recognized that many of the key terms in the so-called absolute pollution exclusion—"release," "disposal," and "escape"—are environmental terms of art; indeed, many are key defining terms for the imposition of liability under CERCLA. *See, e.g.,* 42 U.S.C. § 9607(a).

When these newer exclusions were introduced, the insurance industry made clear that they were designed to address environmental issues arising out of federal environmental laws, i.e., regular, long-term industrial pollution. For instance, at a 1985 hearing before the Texas State Board of Insurance, representatives of the insurance industry stated that the so-called absolute exclusion was not intended to bar coverage in all instances. These representatives discussed several examples of passive pollution that were not intended to be barred from coverage, including leaking USTs. In fact, the Liberty Mutual Insurance Company representative stated specifically that the manufacturer of leaking USTs should not lose coverage for "pollution":

You can read today's CGL [Comprehensive General Liability] policy and say that if you insure a tank manufacturer whose tank is put in the ground and leaks, that leak is a pollution loss. And the pollution exclusion if you read it literally would deny coverage for that. I don't know anybody that's reading the policy that way.

Moreover, as discussed above, to the extent MTBE is a useful, governmentally-required additive to petroleum products expressly exempted from the ambit of environmental law under CERCLA/Superfund, it does not fit within the definition of pollutant. Whether this distinction is accepted by a court, the mere fact that reasonable people disagree can be used as evidence of an ambiguity in favor of the policyholder.

Thus, policyholders should be able to hold the insurance industry and Congress to their words: pollution exclusions should not apply in the normal circumstances that would give rise to "releases" or "dispersals" of MTBE into the environment, in part because MTBE is a required additive to a ubiquitous product that is not a hazardous substance as the term is defined under federal and state law.

CONCLUSION

While coverage for MTBE-related liabilities will not come easily, policyholders should be heartened by the fact that strong evidence and arguments exist to support a claim for MTBE coverage. You are entitled to the coverage you pay for, especially when an insurance company engages in revisionist underwriting after the fact. MTBE, as a government-mandated product, should be encompassed within that coverage.