Insurance Law Blog

July 3, 2015

Dear Amy,

Chief Justice Hecht, joined by four Justices, recently issued the majority opinion in *McGinnes Industrial Maintenance Corp. v. The Phoenix Ins. Co.*, and held that the Environmental Protection Agency's "Potentially Responsible Party" letters and/or unilateral administrative orders constitute a "suit" within the meaning of a CGL policy. Justice Boyd authored a cutting dissent in which he provided a scathing review of the majority's reasoning and analyzed the question presented in light of contractual interpretation principles. The factual background of the case and the body of case law around the country on the issue are straightforward enough; however, the *McGinnes* opinions take the reader on an exciting and unexpected ride.

In the 1960s, McGinnes Industrial Waste Corporation dumped pulp and paper mill waste sludge into disposal pits near the San Jacinto River in Pasadena, Texas. Forty-odd years later, the EPA began investigating possible environmental contamination from the disposal pits. In 2008, the EPA sent McGinnes a general notice letter. The letter named McGinnes as the potentially responsible party for the contamination and kindly invited McGinnes to enter into negotiations for the cleanup and investigation costs. By 2009, McGinnes had not RSVP'd, and the EPA sent a special notice letter scrapping the niceties of negotiations and instead stating that it had determined McGinnes' responsibility for site cleanup and $378,863.61 in reimbursement costs.

During the relevant time period in the 1960s, McGinnes was insured under standard-form CGL policies issued by Phoenix Insurance Company and Travelers Indemnity Company. Each Policy provided that:

[T]he company shall have the right and duty to defend any suit against [an] insured seeking damages on account of such . . . property damage, . . . and may make such investigation and settlement of any claim or suit it deems expedient . . . .

Unlike modern policies, the policies at issue did not define the term "suit." After receiving the EPA's invitation to negotiate, McGinnes requested a defense from its insurers. They refused. After all, EPA letters and proceedings are not a "suit" in the traditional sense of the term. McGinnes filed a coverage lawsuit in federal court, and eventually the Fifth Circuit certified the following question to the Supreme Court of Texas:

Whether the EPA's RPR letters and/or unilateral administrative order, issued pursuant to CERCLA, constitute a "suit" within the meaning of the CGL policies, triggering the duty to defend.

The Court answered yes, the letters and administrative orders constituted a "suit" and, therefore, the insurers owed McGinnes a defense.

The bare majority based its ruling on three reasons. First, at the time the policies were written, in an era before there was an EPA or CERCLA, lawsuits enforced pollution laws. Under modern laws, EPA letters and proceedings, according to the majority, "in actuality, . . . are the suit itself." The Court, in a footnote, stated that it was not rewriting the contracts in so holding, but instead, they were interpreting the contracts as the parties intended. In support of its position, the Court identified parallels between the EPA proceedings and actual litigation:

The PRP notice letters serve as pleadings. The EPA obtains discovery through requests for information, indistinguishable from interrogatories under the rules of civil procedure. It engages in mediation through its invitations to settle. A unilateral administrative order resembles summary judgment. The fines and penalties for willful non-cooperation in the process are like sanctions in a court proceeding, only prescribed by statute. And part of the judicial function is ceded to the EPA by limiting a PRP's opportunity for review until the end of the process, and then limiting that review to an abuse of discretion by the EPA, based on its own record.

An EPA proceeding and a court trial may not be identical twins, but they are at least fraternal twins in Texas. The similarity between the two, even if not blatantly apparent, means an EPA proceeding is a suit.

Second, the Court started from the premise that "cleanup costs under CERCLA are 'damages' covered by the form CGL policies," (an issue the Supreme Court of Texas has never addressed) and reached the conclusion that an EPA proceeding is a covered suit for which an insurer owes a defense. The Court said:

To interpret the policies as covering the damages incurred as a result of pollution cleanup proceedings without giving the Insurers the right and duty to defend those proceedings creates perverse incentives and consequences for insurers and insureds alike.

Notably, the Court has held in the past that an insurer may have an indemnification obligation even if it does not owe a duty to defend without concern for perverse incentives. *See, e.g.*, *D.R.*

Horton-Texas, Ltd. v. Markel Int'l Ins. Co., Ltd., 300 S.W.3d 740, 744 (Tex. 2009) ("We hold that the duty to indemnify is not dependent on the duty to defend and that an insurer may have a duty to indemnify its insured even if the duty to defend never arises.").

Finally, the majority was persuaded that it should join the thirteen of sixteen state high courts to have considered the same issue (including interpreting policies without "suit" defined) and held that EPA proceedings are suits. The Court concluded that "insureds in Texas should not be deprived the coverage insureds have in thirteen other states." The Court admitted it could not achieve uniformity (after all, three courts have already gone the other way); however, they felt it was "prudent to strive for uniformity as much as possible." Of course, the Court historically has had no problem ignoring the weight of non-binding authority in favor of their jurisprudential rules of contract interpretation, even if that resulted in a departure from the results in the majority of other jurisdictions. *See, e.g.*, *Gilbert Texas Constr., L.P. v. Underwriters at Lloyd's London*, 327 S.W.3d 118, 129 n.8 (Tex. 2010). That one hurt a bit. Putting the pain of *Gilbert* aside, it's now fourteen out of seventeen courts, for those of you keeping score, and EPA proceedings are suits in Texas.

Needless to say, the dissent did not see eye-to-eye with the Court's opinion and reasoning. The dissent started out simply enough: "If you do not like your insurance policy, the Supreme Court of Texas can now change it for you. Never mind all those times the Court has said 'we may neither rewrite the parties' contract nor add to its language.'" Things took off from there:

Today the Court demonstrates that it can and will rewrite your insurance policy if it wants to. . . . Why would the Court do this, in spite of everything we've always said about construing insurance policies? Because it seems like a good thing to do here (and on top of that, everyone else is doing it). My law professors (and my momma) taught me better. I respectfully dissent.

The dissenters would have adhered to the plain meaning analysis that the Supreme Court of Texas always has espoused, so the dissenters would have held that "EPA letters and orders do not fall within the common, ordinary meaning of the term 'suit,' and the policies' context does not in any way indicate the contrary."

In short, the Court held that an EPA letter or proceeding is a "suit." The dissent, on the other hand, hopes "that today's decision will soon be seen as a fluke, an oversight, and a rare misstep by a Court that has otherwise been steadfastly committed to enforcing contracts as written, to refraining from rewriting parties' agreements, and to determining the parties' intent by relying on the ordinary meanings of the terms the parties choose."

Commentary

McGinnes is a win for policyholders—but one that could be a double-edged sword. The application of the holding may be limited to a narrow set of cases that will come up only periodically. After all, modern CGL policies are different than the one interpreted by the Court. In particular, modern CGL policies specifically define the term "suit" as "a civil proceeding,"

including “arbitration proceedings” and “other alternative dispute resolution proceedings.” In addition, modern policies have broader pollution exclusions that exclude coverage for any “[r]equest, demand, order or statutory or regulatory requirements or claims or ‘suits’ by or on behalf of a governmental authority.” On the other hand, the reasoning behind the majority opinion likely will be fertile ground for creative arguments in contract interpretation cases. For example, what about demands under statutory right to repair laws? Only time will tell.

However, one very recent example of this is the decision in *Altman Contractors, Inc. v. Crum & Forster Specialty Ins. Co.*, 13-80831-CIV, 2015 WL 3539755 (S.D. Fla. June 4, 2015). The court had to determine whether the notice provision in Florida’s “notice and repair” statute triggered the duty to defend. The policy defined the term suit as a “civil proceeding” including “arbitration proceedings” and “other alternative dispute resolution proceedings.” The court looked to *Black’s Law Dictionary* for the definition of “civil proceeding”— “A judicial hearing, session, or lawsuit in which the purpose is to decide or delineate private rights and remedies, as in a dispute between litigants in a matter relating to torts, contracts, property, or family law.” Based in large part on that definition, the court held that the statutory mechanism was neither a “proceeding” nor “an alternative dispute resolution proceeding.”

The apprehension that comes with an opinion like this is that the Court is presumably free, after this opinion, to interpret what the insurer intended as opposed to what is actually written in the policy. In any event, this opinion came as a bit of a surprise (a pleasant one) because Justice Boyd’s analysis of contract interpretation in the dissenting opinion rings true of how Texas courts traditionally approached insurance policies. But, for now, “Yeah policyholders!” As always, stay tuned . . . **We’ve Got You Covered.**

In the meantime, Happy Fourth of July!!

Sincerely,

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