

The CGL Pollution Exclusion

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Arguably one of the least understood and most litigated portions of the commercial general liability (CGL) policy, the "pollution exclusion," has vexed policyholders and insurers alike for over 20 years. Why such confusion and controversy? What exactly does the October 2001 edition of the Insurance Services Office, Inc. (ISO), CGL policy exclude as pollution? What pollution coverage is left? This article will offer some answers to those questions and attempt to provide some straightforward explanations as to how the "pollution exclusion" applies.

A Historical Perspective

The late 1970s and early 1980s saw two major environmental laws enacted that dramatically changed the way our society and the law viewed environmental contamination. Responsibility that had never before existed was now being imposed on business and industry with passage of the Resource Conservation and Recovery Act (RCRA) and the Comprehensive Environmental Response, Compensation and Liability Act (CERCLA).

The former regulated and tracked the life cycle of hazardous waste, the latter forced just about anyone involved to clean up or pay for the cleanup of such wastes. Liability was not only joint and several, it applied *without regard to fault*. While there is just a bit more to these laws than stated, there was one clear affect—pollution that had been tolerated for many years was not only to be stopped, it was to be cleaned up *right now!*

Federal and state environmental authorities began sending out letters to businesses and organizations as a gentle, friendly reminder of their legal obligations to clean up the mess. If your name appeared on an RCRA manifest, you automatically qualified—no purchase was necessary. But wait, there is more—cost was no object!

The Comprehensive General Liability Policy—Sudden and Accidental

Occasionally, a member of this large but select group handed in a claim to their general liability insurance company, seeking defense of these government orders and payment of remediation costs being imposed. Many insurers looked at the claim, at the policy wording, looked at the claim again, looked at the price tag and said "*no coverage*." Their legal position: "This pollution stuff has been going on for almost 100 years—and you want us to defend you and pay for all of this! Forget it!"

As large sums were involved, litigation quickly followed. One of the many legal arguments insurers put forth was that the CGL policy excluded pollution—unless the pollution was sudden and accidental. Although many of the claims were the result of years of accumulated contamination, initially many courts found CGL coverage still applied as "sudden and accidental" was ambiguous and really meant "unexpected or unintended." Insurers were ordered by courts to pay hundreds of millions in remediation costs.

Despite the fact some state insurance regulators produced explanatory memos previously filed by insurance bureaus essentially stating that the phrase "sudden and accidental" was intended only to reinforce the phrase "unexpected and unintended," insurers were incredulous. Feeling like the Red Sox in a World Series, they needed to *really* exclude pollution from the CGL and do it as soon as possible. The alternative was to not offer liability coverage at all—contributing to the liability crisis of the mid- and late 1980s.

The So-Called Absolute Pollution Exclusion

Rushed to the market as an endorsement to the 1973 nonsimplified comprehensive general liability policy in early 1985, the "absolute pollution exclusion" showed that insurers meant business.

Whether pollutants were released quickly or gradually was now immaterial. Fearing judicial activism that would find a way to negate *any pollution exclusion*, ISO filed an extraordinarily broad exclusion for pollution.

ISO Comments and Publications

Minutes of an October 25, 1984, ISO Underwriting/Legal Review Committee provide some insight into the mindset of ISO when drafting this new "absolute pollution exclusion."

The Committee agreed that the proposed language for this exclusion accomplishes a 'total pollution' exclusion (except for 'products') in the CGL policy. However, such an exclusion precludes some bona fide fortuitous loss which should be insurable under a CGL policy.

Incorporated into the basic simplified commercial general liability policy in 1986, ISO offered the following explanation of the new pollution exclusion in their Commercial Lines Manual, Division Six—General Liability, 1985 (page 4).

Old versus New Pollution Exclusion
<p>Pollution Liability—The new pollution exclusion differs from the old exclusion in the following ways:</p> <ol style="list-style-type: none">1. There is no distinction between sudden/accidental and gradual events.2. All pollution coverage for bodily injury/property damage is excluded under most circumstances, including the following situations:<ol style="list-style-type: none">a. The emission originates on the insured's premises.b. The emission originates from a waste disposal or treatment site.c. The pollutants are handled or treated as waste.d. The emission comes from a site where operations are being performed by the named insured or a subcontractor, and the pollutants are brought onto the site in connection with the work being done, or if the work involves containment or treatment of pollutants.3. Cleanup costs and similar costs are specifically excluded. <p>Pollution arising from Products/Completed Operations hazard is covered under the new policy.</p>

The above is still a useful guide for reference regarding the *general* scope of the CGL pollution exclusion. Consideration needs to be given, however, to several subsequent changes to the exclusion that further refine its scope and will be discussed later in this article.

From Ancient History to Present Day

Even a superficial understanding of today's CGL pollution exclusion requires some insight into the exclusion's historical development. Thus, the preceding history lesson is vital.

Several changes have been made to the CGL pollution over the past 18 years—first to "strengthen the exclusion" and then to add exceptions to the exclusion to provide what some might argue is coverage for "bona fide fortuitous loss which should be insurable under a CGL policy."

2001 CGL Pollution Exclusion—The First Paragraph (f. (1))

The first section of the pollution exclusion (f. (1)) does not exclude *pollution*—it excludes bodily injury or property damage arising out of the release of a pollutant. While this at first may appear to be semantics, the practical results of this become evident in view of a few notorious insurer claim denials.

For example, insurers have denied claims and asserted in litigation that the CGL pollution exclusion eliminated coverage for:

- Fumes from flooring material being applied by a contractor that damaged food products stored on site.
- Carbon dioxide released by a leak in a vent stack of a boiler that resulted in injury to others.
- Cooking equipment that releases fumes, causing patrons' illness.
- Sulfuric acid splashes on a claimant when the bottle breaks.
- Smoke from a hostile fire that resulted in property damage.

But consider the following. Isn't the CGL pollution exclusion intended to apply to *traditional* environmental damage—such as industrial pollution of the atmosphere, water, ground, or groundwater? Where did this come from? This just doesn't make sense!

"Pollution." Actually, it does make sense. When read literally, the pollution exclusion says nothing about environmental damage or industrial polluters.

In fact, not only is the term "pollution" not defined, it does not appear anywhere within the 695-word exclusion. *Whether the policyholder has caused pollution is irrelevant to the strict application of this exclusion.* While some courts have looked beyond such a strict interpretation and have allowed coverage when no environmental damage occurred, court interpretation is decidedly mixed on this issue.

"Pollutants." What is very relevant and is defined (in the CGL's definition section) is the term "pollutant," the understanding of which is central to the pollution exclusion. "Pollutant" is a very expansive term that includes just about any type of irritant or contaminant, whether it is a solid, liquid, gas, or by heat (thermal). The definition specifically mentions, but is not limited to smoke, vapor, soot, fumes, acids, alkalis, chemicals, and waste.

Substances that would normally be expected to be considered "pollutants," and which have been found by courts to be "pollutants," include ammonia, asbestos, benzene, carbon dioxide, carbon monoxide, chemical fumes, DDT, gasoline, heating oil, insecticide, lead paint, PCB, and TCE.

Some substances, not normally considered "pollutants," have been found by courts in some circumstances to be "pollutants," including dust, foundry sand, manure, salt water, sewage, and skunk spray.

The First Paragraph (f.(1))—The Essence

The crux of the first part (f.(1)) of the 2001 CGL pollution exclusion is quite simple—there is no coverage, subject to the exceptions noted below, for any injury or damage arising out of a "pollutant." What is considered a "contaminant or irritant" is often an open question. Following are some noted exceptions.

"Your Premises." Exclusion f.(1)(a) applies to releases or emissions of "pollutants" at or from any premises owned, occupied, rented, or loaned to any insured at any time. Express exceptions to this portion of the exclusion are:

(i) **Building Heating Equipment Exception.** Bodily injury is sustained within a building caused by fumes, smoke, vapor or soot from equipment used to heat the building is covered. The exception does not appear to apply to equipment used for air conditioning or ventilation and is thus a very limited exception. If pollutants are dispersed by the ventilation system, resulting injuries or illness are probably not covered.

(ii) **Owner as Additional Insured Exception.** Bodily injury or property damage away from the named insured's premises is covered if the named insured is a contractor and applies even if the site's owner is listed as an additional insured. Absent this exception, a contractor would not have coverage under their own CGL policy for operations away from the contractor's premises solely because the owner is listed as an additional insured on contractor's CGL policy.

(iii) **Hostile Fire Exception.** Coverage applies to bodily injury, or property damage arising from heat, smoke or fumes from a "hostile fire." A "hostile fire" is a fire which becomes uncontrollable or breaks out from where it is intended to be. For instance, if a chemical plant catches fire, releasing toxic fumes into the neighborhood, resulting bodily injury is covered.

"Waste." Exclusions f.(1)(b) and (c) apply to waste, which includes but is not limited to materials to be recycled, reconditioned, or reclaimed. This portion of the exclusion has no exceptions—waste is excluded regardless of where or how it causes injury or damage.

"Away From Your Premises." Exclusion f.(1)(d) applies the pollution exclusion to the *locations of others* where any insured (or any of the insured's contractors or subcontractors) are performing (present tense) operations *if the pollutants are brought to the premises* by the insured or their contractors or subcontractors *in connection with the operations*. Express exceptions to this *off-premises* portion of the exclusions are:

(i) **Mobile Equipment Exception.** Coverage applies to releases from the insured's mobile equipment *if the pollutants are for the normal operation* of the mobile equipment, such as diesel fuel, motor oil, or hydraulic fluid *if they escape from a vehicle part designed to hold such pollutants*. This exception does not apply if the release is intentional, such as oiling down a road prior to paving. As an example of how this exception might apply, consider a contractor who hits a large boulder with a bulldozer and rips open the diesel fuel tank. Coverage applies to damage caused by the diesel fuel to a newly poured foundation (if poured by another contractor).

(ii) **Operations Within Building Exception.** If an insured contractor (or subcontractors of the insured) is performing operations, releases of fumes, gases, or vapors from materials brought into the building in connection with the operations are covered *if the bodily injury or property damage is sustained within the building*. Say, for example, a flooring contractor brings varnish in to finish a floor of an office building. The flooring contractor will have coverage if fumes from the varnish make an upstairs tenant ill.

(iii) **Hostile Fire Exception.** The "hostile fire" exception also applies away from the premises—if bodily injury or property damage arises from heat, smoke or fumes from a hostile fire *away from an insured's premises*, coverage applies.

Away From Your Premises—Environmental Contractors. Exclusion f.(1)(e) eliminates coverage if any insured or an insured's contractors or subcontractors are involved in performing environmental operations, such as testing, clean up, treating, or responding to pollutants. There are no exceptions to this portion of the exclusion.

Products and Completed Operations. Bodily injury or property damage arising out of an insured's products or completed operations is not expressly eliminated by the pollution exclusion. Therefore, coverage applies by implied exception, to the extent other portions of the exclusion do not apply. For instance, if an insured's product is considered waste, coverage would be excluded, despite the implied exception for products.

2001 CGL Pollution Exclusion—The Second Paragraph (f.(2))

As the second paragraph of the Pollution Exclusion, f.(2), is an independent clause that stands alone, all of the previously noted express and implied exceptions to paragraph f. (1) are limited by f.(2).

From the beginning (in this case, 1985), f.(2) has removed coverage for “cleanup and similar costs.” A revision to f.(2) in 1988 strengthened this portion of the exclusion to eliminate coverage for “any loss, cost or expense arising out of any ... request, demand or order that any insured ... *clean up*, remove, contain, treat, detoxify ... or in any way respond to ... pollutants.” Further, also expressly excluded are claims or suits “by a governmental authority for damages because of testing for, monitoring, cleaning up, removing ... or in any way responding to ... the effects of pollutants.” There is no coverage for the clean up of pollutants—implied or express exceptions notwithstanding.

An Illustration. A manufacturer of valves sells its product to a chemical distributor. Unfortunately, one of the valves purchased and put to use by the chemical distributor malfunctions, releasing toxic chemicals into the soil and groundwater. A court finds the valve was defective and orders the manufacturer to pay \$500,000 of remediation costs as required by the state environmental authority.

The manufacturer looks to their CGL insurer to pay for such costs, relying on the implied “products” exception. Their insurer denies coverage for the cleanup, citing the plain meaning of the wording of paragraph f.(2) of the pollution exclusion. The insurer does, however, offer to pay for the chemical distributor’s loss of use (property damage) and any resulting bodily injury. Neither has resulted from this release.

The valve manufacturer brings suit against the insurer and attempts to introduce into the litigation a half dozen ISO publications that contain statements such as “under our new [pollution] exclusion, coverage is provided in the basic policy for products and completed operations.” Unfortunately, the court rules the ISO publications cannot be admitted as evidence. The publications are not part of the policy and act only to *contradict the plain meaning of the policy exclusion*; the cost of cleanup or remediation is flatly and totally excluded, regardless of the nature or location of the release of pollutants.

A Riddle. How can pollution coverage be provided in the CGL (by the limited exceptions) and yet completely exclude any and all cleanup costs? More to the point—how can ISO’s representations of pollution coverage be reconciled with a total exclusion for any pollutant cleanup? This is all the more puzzling when considering that the basic ISO Business Auto Coverage grants full cleanup coverage (in limited circumstances only) within the definition of “Covered Pollution Cost and Expense.”

A Partial Solution. First introduced in the July 1998 edition of the CGL, and included in the 2001 ISO CGL policy, is a paragraph added to f.(2). According to accompanying ISO Circular, “Coverage is also clarified with respect to certain third-party property damage claims with respect to cleanup by indicating paragraph (2) of the exclusion does not nullify coverage not excluded by paragraph (1) of the exclusion.”

The paragraph being added, however, is not quite as broadly worded as the Circular would indicate. In reference to f.(2), the 1998 and 2001 ISO CGL pollution exclusion states:

However, this paragraph does not apply to liability for damages because of “property damage” that the insured would have in the absence of such request, demand, order or statutory or regulatory requirement, or such claim or “suit” by or on behalf of a governmental authority.

Cleanup coverage exists in the CGL (triggered by an exception to the exclusion, such as products) if the costs are property damage *and* the obligation for remediation of the property exists *outside* of any statute, regulation, or government order to remediate.

A Troubling Situation. As a practical matter, due to the expansive nature of environmental laws and regulations, a vast majority of liability for cleanup costs will be imposed on an insured *because* of such laws or regulations. This puts insurers in the awkward position of determining whether or not the insured—who may be clearly liable due to statute or regulation—*would be* liable if the

statute or regulation *didn't exist*. This "guessing game" determination of coverage leaves a policyholder in limbo, without any genuine promise of coverage.

Conclusion

The basic 2001 ISO CGL policy provides very little pollution coverage, particularly in the area of cleanup or remediation—perhaps the most important aspect of pollution coverage. A policyholder with any significant pollution risk, even in the area of an exception to the exclusion, such as products and completed operations, does not have adequate coverage under the basic ISO 2001 edition of the commercial general liability policy. Risk managers, brokers, and agents would do well to either extensively amend the CGL or obtain separate pollution coverage for any of their policyholders who have more than minimal or incidental pollution exposures.

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