The Vital Role of Insurance in Redeveloping New Jersey

by Stuart Lieberman and Shari Blecher

Historically, we have thought of insurance as something that responds to disasters. Where there is a fire, we think about insurance for rebuilding. When there is a car accident, we think of insurance for providing repairs and for paying medical bills. If we are very ill, we think of insurance in terms of providing payments to medical providers, and in certain instances payments to sustain us through a prolonged disability.

An overlooked but significant role of insurance is in environmental cleanups. Since much of New Jersey's redevelopment requires some level of environmental remediation, those interested in redeveloping New Jersey cities and, to some extent, preserving what remains of New Jersey's green lands, must not ignore the vital role insurance plays.

Essentially, there are two distinct functions satisfied by insurance policies in the context of New Jersey's redevelopment. First, there is the function of paying for necessary environmental cleanups before redevelopment can proceed. Second, there are environmental insurance policies, a special breed of coverage in existence for approximately 10 years, which allow complex environmental transactions to go forward.

Initially, let us consider the role of environmental insurance claims as part of the environmental remediation process that is so often a prerequisite before redevelopment can be considered in this state. Surprisingly, many real estate professionals still do not fully appreciate how important it is to ask a client this simple question: "Do you have your old insurance policies?" Indeed, sophisticated real estate transactions often involve identification of insurance policies that were maintained by the seller, and even predecessors to the seller.

Many of the environmental and other regulatory programs in effect in this state promote the redevelopment of our cities and provide incentives for development to occur in urban areas. Of course, many of these urban projects require some level of environmental cleanup.

Environmental cleanups can range from simple, isolated cleanups of barely contaminated soil to more complex soil and groundwater remediations. Many sites that need to be redeveloped have old tanks on them, which generally fall into two categories: those that store petroleum, and those that store something other than petroleum.

Historically, petroleum tanks either were used to supply heating furnaces or to fuel vehicles operated by the on-site businesses. In either case, old tanks leaked petroleum products. Petroleum cleanups are the most frequent cleanups encountered in New Jersey redevelopment projects.

Besides petroleum, underground tanks may contain volatile organic substances such as industrial degreasers, and waste products. These tanks are often the focus of mandatory cleanups that must occur before redevelopment can proceed.

Heavy metals, consisting of lead and other metals that were used as part of industrial processes, are also frequently uncovered on redeveloped properties. Lead can also be found where there have been gasoline leaks, since fuel oil contained lead until recently.

Whatever has been identified on site requiring an environmental cleanup, there is always a possibility the property owners' and operator's liability policies will respond to the

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cleanup obligations. Again, the very first question to pose, but often *never* asked, is: "Where are your insurance policies?"

Insurance policies in existence before 1986 may respond to these claims. There are a myriad of *caveats*, the scope of which extend well beyond the focus of this article. In the most general sense, insurance policies that predate 1986 apply to third-party claims. The most common kind of third-party claim that triggers the obligation to defend and indemnify in the context of an environmental incident relates to contaminated groundwater. In New Jersey, groundwater is considered to be property owned by a third party.

Once again, even though commentators have been discussing the necessity of comprehensive general liability policies as a significant source of revenue needed to fund these overwhelmingly expensive cleanups, the word has still not gotten out. Environmental consultant after environmental consultant act today as if the concept is completely foreign when advised of this option.

It is absolutely essential that, to the extent they are professionally able, attorneys in redevelopment projects insist policyholders do everything they can to locate pertinent insurance policies. Yes, there is gold in those policies.

Under New Jersey law, the burden is on the policyholder to prove by a preponderance of the evidence that there is coverage. Of course, the very best evidence of coverage is the policies themselves. Frequently, the policyholder confesses there is no policy. Sometimes that ends the discussion. Ending the discussion at this point is a terrible mistake.

While insurance policies undoubtedly represent the best evidence of coverage, by no means are they the only proof of coverage.

- What else can a lawyer use in prosecuting a claim against insurance carriers for coverage?
- How about check stubs evidencing payments to carriers?
- How about correspondence from insurance carriers rejecting certain claims that were paid years ago?
- How about sworn statements from former bookkeepers or insurance agents regarding the personal knowledge those persons possess about the identity of the companies that provided coverage and the terms of those policies?

The consequence of not having properly prosecuted a good claim for environmental coverage extends beyond harm to the policyholder. Indeed, everyone involved in a redevelopment that requires insurance funding to pay for a necessary environmental cleanup stands to lose. It is not an overstatement to suggest that the redevelopment of all New Jersey cities requires active participation by the insurance community. Thus, it is fair to opine that our statewide redevelopment initiative requires a vigorous prosecution of valid insurance claims by knowledgeable practitioners who are aware of the potential pitfalls and are capable of presenting the necessary proofs.

New Jersey has a good faith and fair dealing regulation that applies to all licensed insurance carriers. It requires, among other things, that there be unequivocal and prompt responses to presented claims. In the landmark case of *Princeton Gamma-Tech, Inc. v. Hartford Ins. Co.*,[1] it became abundantly clear that the old avoidance routine followed by many insurers is no longer tolerable.

Under New Jersey's insurance regulations, carriers have an obligation to provide a prompt response with reasons and justification. Anything short of that exposes a carrier to not only a breach of contract claim, but also the possibility of a claim for bad faith and punitive damages.

Various kinds of insurance policies can be called upon to address claims as part of the redevelopment process. First, there are the primary insurance policies. Primary insurance is the first line of coverage that every policyholder

possesses. It responds to a claim for defense and indemnification after some deductible is satisfied by the policyholder. It will respond to a claim up to the policy limits.

The next level of defense provided by insurance is called excess insurance. Usually this means coverage that applies after the primary insurance has been satisfied. Sometimes it is triggered in instances where the primary policy does not provide coverage.

The insurance carriers have a duty to both defend and indemnify a policyholder. How does one defend in the case of an environmental cleanup relating to a redevelopment? Defense costs may include the costs of defending a party in a site remediation lawsuit filed to bring about a redevelopment. They may also include costs associated with defending against claims brought by the Department of Environmental Protection.

Defense costs are defined in individual policies, and it is incumbent upon a claimant to prove the costs incurred are defense costs within the meaning of the policy. Where there are numerous insurance companies that have an obligation to provide coverage, one carrier has a right to file a contribution action against another carrier to demand the defense obligation be shared.[2]

While excess carriers generally do not have an obligation to pay the defense costs, there are occasions when they must pay. One occasion exists when an excess policy provides coverage for defense obligations in instances in which no primary policy responds. Therefore, do not overlook excess policies that might be available to respond to the duty to defend as well.

New Jersey adheres to the continuous trigger theory, as explained in *Owens-Illinois, Inc. v. United Ins. Co.*[3] In *Owens*, the New Jersey Supreme Court ruled that multiple insurers must respond based on years of their risk and their policy limits. The Court suggested that policies will be triggered from the discharge date through the date the contamination is discovered or ultimately addressed.

Thus, in the context of environmental insurance claims, there is a need to find every policy and determine the date an environmental discharge occurred. Often, expert testimony is required by a forensic hydrogeologist capable of providing an expert opinion on the first date of discharge. Unfortunately, few hydrogeologists are capable of offering a sustainable opinion regarding the date of discharge. Choosing the best witnesses is critical.

A myriad of cases have addressed the question of how far back one can go in triggering insurance policies. In *Quincy Mut. Fire Ins. Co. v. Borough of Bellmawr*[4] the Court held that a policyholder may go back to the first date the hazardous waste was discharged. In so holding, the Court rejected the argument that the contamination was discharged into a landfill on one date but the actual damage did not occur for a significant period thereafter, when the contamination migrated from the landfill into the groundwater. The Supreme Court found the injury commenced when the waste was deposited, and not when it reached the landfill. The Court's rationale was supported by public policy, not exclusively policy language construction.

Should it be necessary to file a lawsuit against an insurance carrier to obtain coverage for a redevelopment project to proceed, practitioners need to ensure the claim is filed in time, and does not run contrary to the entire controversy doctrine. The question of whether the entire controversy doctrine may bar an insurance claim was addressed recently in *Hobart Bros. Co. v. National Union Fire Ins. Co.*[5] The Appellate Division reversed a trial court's ruling that a claim against an insurance carrier had been precluded by application of the entire controversy doctrine. The court ruled that as a general matter, litigants must present all aspects of a controversy in one proceeding. It described the doctrine as intended to bar a party from voluntarily electing to hold back a related component of a controversy in one case by precluding it from being subsequently raised in another.

Notwithstanding this general rule, the court held that in the final analysis "the entire controversy doctrine is...an equitable one,"[6] and opined that its application must ultimately be left to judicial discretion based on factual circumstances. The court provided a list of factors to be considered in determining whether a coverage claim should be barred by operation of this doctrine. Included in the analysis is a question of the extent that rights have been permanently surrendered by the delay, whether some kind of reallocation can cure any inequity caused by the delay, whether there is some ulterior motive associated with the delay, and whether the act of delaying the claim against the carrier was reasonable.

Policyholders should also take comfort from the 2003 decision in *Spaulding Composites Co., Inc. v. Aetna Cas. and Sur. Co.*[7] At issue in that case was whether the well-accepted continuous trigger theory could be defeated by a non-cumulation clause the carriers asserted required a much more limited result.

While the Appellate Division concurred with the insurance company defendants, the Supreme Court reversed, reaffirming the vitality of the continuous trigger theory. The Court held that there must be an allocation of liability pro-rated based on considerations relating to policy limits and policy terms. Again, the Court ruled that public policy requires this result even if it might be construed as inconsistent with a technical reading of the policy language. The Court held that the public

policy favors maximizing, in a fair and just manner, insurance coverage proceeds for New Jersey environmental claims.

Thus, it is clear that insurance consultants, property owners, property purchasers, and master redevelopers must be sure to ask at the outset of any transaction this fundamental question: "Where are all of the applicable insurance policies, going back as far as possible?" Too often that question is not asked, or when asked is not adequately answered. Ignoring this issue is a potentially costly mistake that may cause irreparable injury to a redevelopment project.

Another kind of insurance policy (often called an environmental insurance policy), approximately a decade old and more refined and better understood, is now available. Because environmental insurance policies are provided by only a handful of national carriers, case law relating to these policies is sparse. Of course, the carriers have been rather quiet about the claims experience relating to them. Since the tragedies associated with September 11, 2001, these policies are becoming more difficult to obtain.

The most well known of these policies is called a property transfer policy. These insurance policies may protect any party to a transaction involving real estate that may have environmental problems. The buyer, the seller and the lenders may all be insured through a property transfer policy. Within this broad category are sub-categories designed to meet specific types of property transfers. For example, there are policies geared toward shopping centers and policies designed for office buildings, while others work well for residential re-uses.

Property transfer policies can provide a heightened level of assurance that an environmental discovery will not destroy a project, and offer the extra level of protection necessary to ensure an environmental risk can be addressed. Property transfer policies are now routine. Lenders often insist on them as a condition to loans. Lenders do not want a situation where a borrower becomes insolvent as a result of an environmental liability and cannot complete the project. Lenders never want to foreclose on half-completed projects.

An environmental insurance policy called a professional errors and omission policy may protect directors and officers of manufacturing operations from liability associated with discharges on industrial properties. Since many management decisions may have significant environmental consequences, these policies have become increasingly important.

Another kind of environmental policy that may be important in redevelopment is called a contractor's pollution liability policy. These policies are designed to protect contractors who actually perform site remediation. They cover claims caused by a contractor's actions, where it is alleged that the contractor either caused contamination or exacerbated an existing condition. Many site cleanups include claims that existing problems were worsened as a result of on-site activities. Contractor policies can be pivotal in those situations, and keep many a contractor financially secure.

Frequently, environmental insurance policies are negotiated. It is incumbent upon environmental attorneys to negotiate language that maximizes coverage with the fewest exceptions. A policy that is inexpensive but effectively covers nothing at all has very little value.

Furthermore, they are claims-made policies, meaning these environmental insurance policies only cover claims made during the policy term. Through amendments to a policy, this claim presentation period can be somewhat extended, but they still remain claims-made policies. Consequently, claims made outside the policy term will not be honored.

Clearly, the role of insurance has not been fully explored by real estate and environmental practitioners, who are, overall, the first line of defense. Professionals who participate in redevelopment in New Jersey and encounter environmental contamination need to evaluate whether previously issued insurance policies may be responsive to a claim.

Practically speaking, the effective redevelopment of New Jersey's urban core requires a thorough understanding of the manner in which both older and contemporary insurance policies may react to these claims. Premiums should legitimately be called upon to react to an event that honestly triggers the duty to defend and indemnify. A failure to appreciate this resource may result in an unfortunate failure to fully redevelop. In the final analysis, there is no excuse for this unfortunate result to materialize.

Endnotes

1. Superior Court of New Jersey, Law Division, Docket No. SOM-L-1289-91 (1992).
2. *See Cosmopolitan Mut. Ins. Co. v. Continental Cas. Co.*, 28 N.J. 554 (1959).
3. 138 N.J. 437 (1994).
4. 172 N.J. 409 (2002).
5. 354 N.J. Super. 229 (App. Div. 2002).
6. *Id.* at 241.
7. 176 N.J. 25 (2003).

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