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Editor's Note: In this issue, Bruce Campbell and Brian Sniffen of Miller Nash LLP analyze the Oregon Supreme Court's decision in *ZRZ Realty v. Beneficial Fire and Cas. Ins.*, addressing whether certain marine insurance policies provide coverage for sediment remediation.

We have reproduced the entire article below. Any opinions expressed in this article are those of the authors alone. For those who prefer to view this article in PDF format, a copy will be posted on the Section's website: http://www.osbenviro.homestead.com/.

E-Outlook Editor
Patrick Rowe
prowe@sussmanshank.com

The Oregon Supreme Court Sets Precedent for Burden of Proof and Allows for Insurance Coverage of Contaminated-Sediment Cleanup

By: Bruce L. Campbell and Brian T. Sniffen
Miller Nash LLP

The Oregon Supreme Court recently issued a significant decision, handed down on October 14, 2010, allowing for insurance coverage of contaminated-sediment cleanup under certain marine policies. The decision, *ZRZ Realty v. Beneficial Fire and Cas. Ins.*, 349 Or 117, 241 P3d 710 (2010), benefits insureds that are involved in contaminated-sediment sites, such as the Portland Harbor Superfund Site.

Specifically, the Oregon Supreme Court held that:

1. an insurer, under an implied-fortuity policy, has the burden of proving that environmental damages resulting from the operation of the insured's business were expected or intended by the insured;
2. an insured, under an express-fortuity policy, has the burden of proving that environmental damages resulting from the insured's business were neither expected nor intended by the insured, if the "expected or intended" language is contained in the policy's grant of coverage; and
3. the following language requires an insurer to provide indemnity for damages to riverbed sediment adjacent to an insured's property:

"'damage to any harbour, dock (graving or otherwise), slipway, way, gridiron, pontoon, pier, quay, jetty, stage, buoy, telegraph cable or other fixed or moveable thing whatsoever.'" *ZRZ Realty*, 349 Or at 139.

Background

Portland-based Zidell Marine Corporation and other Zidell Companies ("Zidell") dismantled decommissioned navy and merchant marine ships for the United States government after World War II. Zidell conducted its dismantling operation at its property adjacent to the Willamette River, on the South Waterfront in Portland, Oregon.

As part of its operations, Zidell purchased several types of insurance policies, including bumbershoot policies, commercial general liability ("CGL") policies, and ship-dismantling or protection and indemnity ("P&I") policies. These policies were issued from 1956 to 1983. Some of the policies at issue, the so-called implied-fortuity policies, contain an implied requirement that any loss under the policy be neither expected nor intended. That is, these implied-fortuity policies did not state in express terms that a covered loss must be unintended or unexpected. In contrast, other policies purchased by Zidell, the so-called express-fortuity policies, explicitly stated that any covered loss be unexpected or unintended by the insured.

In addition, Zidell had a series of P&I policies that provided it with insurance coverage for "damage to any harbour, dock (graving or otherwise), slipway, way, gridiron, pontoon, pier, quay, jetty, stage, buoy, telegraph cable or other fixed or moveable thing whatsoever." This language will be referred to hereafter as the "Damage to Harbor clause."

In approximately 1994, when the riverbed adjacent to Zidell's property was found to be contaminated, Zidell agreed to a voluntary cleanup of the sediment and sought to recover the costs it incurred (and would continue to incur) in the cleanup from its insurers. After the insurers refused to indemnify Zidell for the costs Zidell incurred (and would continue to incur), Zidell sued its insurance carriers. Many insurers settled with Zidell before going to trial. The insurers that remained in the litigation argued that Zidell had the burden of proving that the contamination was neither intended nor expected by Zidell and that the Damage to Harbor clause did not provide coverage for damages caused to the riverbed.

The Trial Court

Zidell first brought suit against its insurers in 1997, and prevailed at trial against its insurers in 2003. Among other things, the trial court held that:

1. the insurers had a duty to defend in response to the potentially-responsible-party letter Zidell received from the Oregon Department of Environmental Quality;
2. the insurers were liable for cleanup costs and future indemnity costs;
3. the insurers had the burden of proving that the environmental contamination was expected or intended under all the policies at issue; and
4. the insurers were required to pay Zidell's attorney fees, which at the time exceeded $1.5 million.

After losing at the trial court level, the insurers appealed.

The Court of Appeals

At the court of appeals, the insurers attacked the trial court's decision on many grounds. This article addresses only the burden-of-proof issue and the Damage to Harbor clause issue, however, because only those two issues were eventually decided by the Oregon Supreme Court.

On the burden-of-proof issue, the court of appeals separately addressed the express- and implied-fortuity policies. With regard to the express-fortuity policies, the court of appeals held that insureds such as Zidell have the burden of proving that any loss was within that coverage. The court of appeals therefore concluded that the trial court erred in putting the burden of proof on the insurers with respect to the express-fortuity policies. For the implied-fortuity policies, the court of appeals held that insurers bear the burden of proving that a loss was expected or intended by the insured. In affirming the trial court's decision in this regard, the court of appeals wrote: "[W]here the insured is able to demonstrate that the loss would otherwise fall within the plain language of the policy, the insurer can prevail only by demonstrating that a policy provision or exclusion is implied by operation of law." 222 Or App 453, 475, 194 P3d 167 (2008).

Although the court of appeals affirmed the trial court's burden-of-proof rulings insofar as they concerned the implied-fortuity policies, the court reversed the trial court's judgment in its entirety and remanded the case to the trial court for a new trial on all CGL policies.

On the issue whether the P&I policies provided coverage for the riverbed sediment, the court of appeals reversed the trial court. The court found that the Damage to Harbor clause, in the "context in which that phrase appears," 222 Or App at 489, did not refer to natural objects such as river sediment. Rather, the court interpreted the Damage to Harbor clause to "most likely refer[] to something that has been built or constructed." 222 Or App at 490.

The Oregon Supreme Court

The Oregon Supreme Court affirmed the court of appeals' decision with regard to the burden-of-proof issue, but reversed the court of appeals' decision regarding riverbed sediment coverage. The court began with the premise that insureds bear the burden of proving that a loss is within the scope of coverage, while insurers typically bear the burden of showing that an otherwise-covered loss falls within an exclusion of coverage. Starting with that premise, the court held that, with regard to express-fortuity policies, the parties agreed to "structure their agreement to provide limited coverage." *ZRZ Realty*, 349 Or at 129. That is, the "unintended and unexpected" language acted as a limit on coverage, not an exclusion. In such cases, the "burden [is] on the insured to prove that the event that triggered the loss came within the scope of that coverage." *Id.* In contrast, the court held that insurers carry the burden of proof regarding implied-fortuity policies because "implied fortuity policies function[] as an exclusion." *Id.* at 133.

The court, however, held that the trial court erred in reversing the trial court's judgment on all policies. Because the express-fortuity and implied-fortuity policies are separate and distinct, the supreme court reversed the court of appeals and reinstated the trial court's judgment

in favor of Zidell on the implied-fortuity policies. The supreme court also reinstated the trial court's judgment and supplemental judgment awarding attorney fees to Zidell.

Regarding riverbed sediment coverage under the P&I policies, the Oregon Supreme Court found that the interpretations of the Damage to Harbor clause proposed by both Zidell and the insurers were plausible. Further, examination of the remainder of the policies did not resolve which side's interpretation was correct. The court, citing *Hoffman Construction Co. v. Fred S. James & Co.*, 313 Or 464, 470, 836 P2d 703 (1992), stated that in such circumstances, the phrase in question should be construed against the drafter. The Oregon Supreme Court therefore held that the Damage to Harbor clause should be construed in Zidell's favor to include coverage of sediment contamination.

Application Beyond This Case

Many entities involved with complex contaminated-sediment sites will benefit from this decision because they likely have insurance policies similar to those at issue in this case. For example, the Portland Harbor Site involves other parties that, like Zidell, dismantled United States vessels after World War II, had various marine activities involving repairs or other operations involving vessels, and purchased insurance policies containing various forms of Damage to Harbor clauses. As a result, the Oregon Supreme Court's decision should result in many more carriers' funding site remedial activities.

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If you would like to contribute or have comments, please contact the E-Outlook Editor, Patrick Rowe, at prowe@sussmanshank.com or (503) 243-1651.