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Representative Paul Holvey, Chair
House Committee on Consumer Protection
and Government Efficiency
Oregon State Capitol
99 Court St NE, Room 453
Salem OR 97301

Re: Opposition to SB 814

Dear Chair Holvey and Members of the Committee:

Please accept this letter on behalf of the Property Casualty Insurers Association of America and the American Insurance Association in opposition to Senate Bill 814. PCIAA and AIA share the concerns that litigation over insurance coverage for environmental claims can be expensive and time-consuming and can present complicated fact and complex legal issues. However, PCIAA and AIA believe that the provisions of Senate Bill 814 will not resolve these concerns, and urge you not to pass Senate Bill 814.

There are many reasons why Senate Bill 814 is problematic. This letter focuses on three problems posed by the Act. These are: (1) Section 2, invalidating consent-to-assignment provisions in insurance contracts in environmental claims; (2) Section 7, creating an automatic independent counsel requirement even in the absence of any adversity of interest between the insurer and policyholder; and (3) certain constitutional infirmities of the Act, particularly in light of the retroactive effect of the proposed legislation.

A discussion of these provisions will illustrate why enactment of Senate Bill 814 would be short-sighted and would not advance the goals of environmental cleanup or a stable insurance system.

Invalidation of Consent to Assignment Clauses

Section 2 of Senate Bill 814 overrides the effect of consent-to-assignment clauses in environmental claims seeking coverage for losses or damages that commenced prior to the assignment. Unless the assignment explicitly states that it extinguishes a cause of action against the insurer, the Act provides that it may not do so. The provision broadly supersedes the law and the contract terms without limitation in voluntary assignments, assignments made in settlement of an environmental claim against the policyholder, assignments made as a matter of

law, and assignments made in the course of a corporate insured reorganization, merger, acquisition or liquidation. Overriding express anti-assignment clauses and extending coverage to strangers to the contract would have significant, undesirable consequences for insurers, policyholders, and the insurance mechanism.

For instance, overriding the express terms of non-assignment clauses prevents insurers from being able to determine precisely what risks they will cover. Insurers engage in careful risk calculations in determining whether to provide coverage to a prospective policyholder and, if so, the extent and cost of coverage to be issued. These calculations are crucial. The insurer must be able to control the identity of its policyholders so that it can carefully calculate what level of liability it faces. When the identity of the policyholder changes, regardless of when the event giving rise to liability occurs, the insurer's risks are altered. For example, ignoring non-assignment clauses changes the defense obligations an insurer assumes – and can artificially create obligations to defend a stranger to the contract as well as the actual policyholder. Providing defense obligations to strangers is exactly the type of risk that the non-assignment clause is intended to avoid. As a California court explained in Quemetco, Inc. v. Pacific Automobile Insurance Co., 24 Cal. App. 4th 494, 503 (1994), "[t]he purpose of consent provisions is to prevent an increase of risk and hazard of loss by a change of ownership without the knowledge of the insurer."

If a policy can be transferred absent a valid consent, there is no certainty as to the numbers of strangers an insurer will be forced to defend, making the insurer's costs inevitably higher than that originally contemplated. See, e.g., Quemetco, 24 Cal. App. 4th at 503 (recognizing that reading the clause out of existence would result in an "increased risk [to the insurer] of having to defend two corporations"). Further, invalidating a consent-to-assignment clause causes serious risks where, for instance, the policyholder remains a going concern and is claiming policy benefits simultaneously with another entity who allegedly acquired insurance rights by assignment. The policyholder owns the policies at issue and has the right to obtain benefits under the policies. Enabling another company to gain coverage rights will both increase the insurers' assumed risks -- and diminish the coverage available to the true policyholder.

It is important to recognize that the non-assignment clause not only protects insurers; the clause also protects policyholders. It is therefore short-sighted to

allow the override of a non-assignment clause, as Senate Bill 814 does in Section 2. If coverage is extended to another entity, it will draw upon the indemnity limits for which the policyholder paid premiums. Policyholders should not have to compete with strangers to the contract for the coverage that the policyholder purchased. See, e.g., Quemetco, 24 Cal. App. 4th at 503 ("To hold that the policies were assignable without [the insurers'] consent would leave [the policyholder] without any insurance to cover any potential liability assessed against it.").

The public's interest in receiving affordable insurance coverage also would be undermined by granting coverage despite a policy's non-assignment clause. Mandating coverage in the manner proposed by Senate Bill 814 leaves "ordinary insureds to bear the expense of increased premiums necessitated by the erroneous expansion of their insurers' potential liabilities." Garvey v. State Farm Fire & Cas. Co., 48 Cal. 3d 395, 408 (1989); N. River Ins. Co. v. Cy Thompson Transp. Agency Inc., 840 F.2d 139, 142 (1st Cir. 1988) (coverage is tailored to risks defined in the insurance policy).

Independent Counsel Provisions

The "tripartite" relationship refers to the relationship among the three parties when a lawyer is hired by an insurer to defend a suit against its policyholder. Within the tripartite relationship, defense counsel routinely act pursuant to the insurer's instructions in defending the insured, protecting the interests of both parties in an effective and cost-efficient manner. The insurer has the ability to protect its interest in potential indemnity exposure and the policyholder is afforded the often superior experience of the insurer in selection, oversight and monitoring of its counsel and defense.

Senate Bill 814 unnecessarily curtails the terms of insurance contracts which set out the insurer's right to control the defense and settlement of suits against the insured or to designate counsel to defend the policyholder. For example, general liability policies often expressly grant the insurer with the unqualified right to "defend any suit against the insured" seeking damages on account of bodily injury or property damage to which the policy applies, and to "make such investigation and settlement of any claim or suit as it deems expedient..." Senate Bill 814 would substantially change the tripartite relationship, taking an extreme position that "independent" counsel must be provided to a policyholder in an

environmental claim whenever the insurer defends under a reservation of rights or if the insured has potential liability in excess of the limits of its insurance. This is out of step with the majority view on the tripartite relationship and existing Oregon law. Existing Oregon law recognizes the insurer's ability to control the defense of its policyholder. See Ferguson v. Birmingham Fire Ins., 254 Or. 496, 509, 460 P.2d 342, 348 (1969).

Many other states reject the *per se* independent counsel requirement imposed in Section 7 of Senate Bill 814, often in well-considered opinions and settled case law. E.g., Public Service Mutual Insurance Co. v. Goldfarb, 425 N.E.2d 810 (N.Y. 1981); Lusk v. Imperial Casualty and Indemnity Co., 603 N.E.2d 420, 423 (Ohio Ct. App. 1992), Nisson v. American Home Assurance Co., 917 P.2d 488, 489-90 (Okla. Ct. App. 1996); Pennbank v. St. Paul Fire and Marine Insurance Co., 669 F. Supp. 122, 126-27 (W.D. Pa. 1987); St. Paul Fire & Marine Ins. Co. v. Roach Bros Co., 639 F. Supp. 134, 139 (E.D. Pa. 1986).

California provides by statute that a conflict of interest "may" exist, "when an insurer reserves its rights on a given issue and the outcome of that coverage issue can be controlled by counsel first retained by the insurer for the defense of the claim . . . ." Cal. Civ. Code §2860(b) (West 1996). The California statute also explicitly provides that a conflict of interest does not exist as to claims for damages in excess of the insurance policy limits, taking the opposite approach to Senate Bill 814. Here, Senate Bill 814 would create an independent counsel requirement whenever there is a claim for damages in excess of the applicable policy limits. Because environmental cleanups are often costly and because a responsible party can often be held jointly and severally liable for the entire cost, hazardous waste related actions frequently involve the potential for an excess verdict. The weight of authority nationwide holds that the potential of excess liability above the indemnity limits of a defending primary insurer will not—standing alone—create a conflict requiring independent counsel. Imposing it in the settings contemplated by Senate Bill 814 could reach the vast majority of cases involving environmental claims, depriving the insurer of the right to control the defense and protect its interests in potential indemnity exposure, and ultimately increasing the costs of environmental insurance coverage in Oregon.

Senate Bill 814 would essentially force imposition of independent counsel for virtually all environmental claims. The issuance of a reservation of rights as to indemnity coverage is characteristic of most environmental coverage cases today.

This is true because of the widespread use of pollution exclusions, the coverage issues relating to the nature of relief sought in cleanup cases, the potential for environmental harm that is expected or intended because it results from routine business practices, and a host of other coverage issues that arise in the environmental setting (for example, late notice, voluntary payments, and so forth). Both existing Oregon law and the majority view nationwide reject a *per se* rule automatically requiring independent counsel whenever there is any reservation of rights. Oregon should not adopt this extreme view.

PCIAA and AIA urge you to honor the bargain made in the insurance contract under which the insurer assumes responsibility for a risk in exchange for control over the litigation against its insured. This arrangement should not be abandoned solely because there may be excess liability or a reservation of rights, as Senate Bill 814 provides in Section 7. These provisions would override the insurance policy terms in virtually all environmental cases where an attorney is retained by an insurer to defend a suit against its policyholder.

Constitutionality and Retroactivity

Overall, the bill inserts a series of unbargained-for terms into commercial general liability insurance policies issued to certain policyholders, dramatically expands coverage afforded to those policyholders, applies retroactively as well as prospectively, and appears to be geared specifically to dictate how Oregon courts should rule in selected pending cases. In doing so, the bill violates the Oregon and United States Constitutions. Article I, Section 21 of the Oregon Constitution provides that "No . . . law impairing the obligation of contracts shall ever be passed . . ." The United States Constitution similarly provides that "[n]o State shall … pass any … Law impairing the Obligation of Contracts." See U.S. Const. art. I, § 10.

Senate Bill 814 substantially impairs the obligation of contracts and, specifically, liability insurance policies by inserting into them material terms that broaden coverage beyond what insurers and policyholders alike understood when they entered into the contracts. Moreover, the bill expressly applies not only to insurance policies issued after the Act's passage, but to policies issued at any time in the past whose provisions are at issue in pending disputes, or may be challenged in future claims. Section 8 of the bill provides that, with very limited exceptions, the Act applies "to all environmental claims, whether arising before,

on or after the effective date of this 2013 Act. " The Act adversely affects the public interest by disrupting the efficient functioning of the insurance market and muddling the judiciary's traditional, well-recognized role as the neutral arbiter of private contract terms.

Legislation that attempts to make material alterations in the character, terms or legal effect of existing contracts is clearly void. Senate Bill 814 significantly alters the scope of the coverage that insurers underwrote and priced, by, for instance, both invalidating terms requiring an insurer's consent to assignment of rights under a general liability policy in the context of environmental claims and dictating that no effect is to be given to clauses providing for a reduction of covered loss to account for amounts covered under prior insurance. As these examples illustrate, it alters the fundamental character of the insurance contract.

The changes that the Act imposes on insurance contracts are important. To function properly, insurance is dependent upon the faithful application of plain language chosen by the contracting parties to define and limit the scope of the risks assumed. Here, the provisions of Senate Bill 814 upset that balance. The impairment of contract effected by Senate Bill 814, moreover, is particularly acute because of its expressly retroactive reach. It intrudes not only upon the terms of policies that insurers and policyholders will enter into going forward, but also on the terms of insurance contracts entered into in decades past.

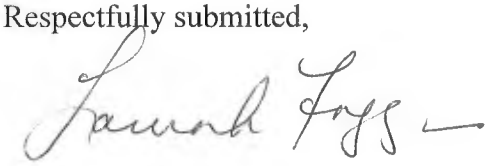
The courts have not hesitated to bar the application of laws that impair insurance-related contracts retroactively and thereby thwart the contracting parties' expectations at the time of contracting. Moreover, public policy is not served by altering contract terms in order to expand coverage in favor of those insureds who seek to evade paying the costs occasioned by their environmental misdeeds, and manage to convince the legislature that they are entitled to a coverage windfall.

Conclusion

In this letter, PCIAA and AIA have highlighted just three of the many sections of Senate Bill 814 that are highly troublesome. The Act will not serve to promote the fair and efficient resolution of environmental insurance claims. Indeed, Senate Bill 814 unfortunately may create incentives for companies facing environmental liability to evade their responsibilities and look to insurers as deep

pockets, to the detriment of the insurance system and the Oregon marketplace for environmental coverage.

Respectfully submitted,



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