LATHAM & WATKINS

Number 1293 February 16, 2012

Client Alert

Latham & Watkins
Environment, Land & Resources Department

Insurance Coverage for Climate Change Suits: Virginia Supreme Court Reconsidering 2011 *Steadfast v. AES Decision*

On February 27, 2012, the Virginia Supreme Court will hear oral argument on the petition for rehearing in *Steadfast Insurance Co. v. AES Corporation* (*Steadfast*). The Court's original decision in *Steadfast* ruled in favor of the insurer and declined coverage to AES Corporation (AES) under a comprehensive general liability (CGL) policy for certain alleged liabilities concerning greenhouse gas (GHG) emissions. The *Steadfast* opinion was the first state supreme court decision in the country to analyze insurance coverage in connection with climate change. The Virginia Supreme Court grants petitions for rehearing infrequently, and thus, its recent decision to rehear the *Steadfast* case may be significant for companies targeted in climate change litigation.

> "The *Steadfast* opinion was the first state supreme court decision in the country to analyze insurance coverage in connection with climate change."

Climate Change Litigation Underlying *Steadfast*

Policyholder AES is a Virginia-based power company that allegedly emitted GHGs in the course of its historical operations. In 2008, the City of Kivalina, Alaska, and the Native Village of Kivalina, Alaska (Kivalina plaintiffs) sued AES and other energy companies. According to the Kivalina plaintiffs, the company's GHG emissions caused global warming which, in turn, melted Arctic sea ice protecting the plaintiffs' coast from storms and thereby purportedly caused massive land erosion. *Native Vill. of Kivalina v. ExxonMobil Corp.* (*Kivalina*), 663 F. Supp. 2d 863, 868–69 (N.D. Cal. 2009). The plaintiffs seek damages accruing from the forced relocation of their village as a result of this erosion, including $400 million in relocation costs. *See id.* at 869.

The district court dismissed the case for lack of subject-matter jurisdiction. *Id.* at 882–83. The Kivalina plaintiffs appealed, and that case is currently pending before the US Court of Appeals for the Ninth Circuit.

Virginia Supreme Court's Initial Ruling

AES tendered its defense of the *Kivalina* lawsuit to Steadfast, one of its CGL insurers. AES's CGL policies obligated Steadfast to pay "those sums that [AES] becomes legally obligated to pay as damages because of 'bodily injury' or 'property damage'" "caused by an occurrence." The policies defined an "occurrence" as an "accident, including continuous or repeated exposure to substantially the same general harmful

condition." *See Steadfast*, 715 S.E.2d 28 (Va. Sept. 16, 2011). Steadfast initially agreed to provide a defense under a reservation of rights, but then sued its insured in state court, seeking a declaration that it had no duty to defend or indemnify AES in connection with the *Kivalina* lawsuit. The trial court held that the Kivalina plaintiffs' allegations of "negligence" were insufficient to allege an "occurrence" under the Steadfast policies and, thus, no coverage was available. AES ultimately appealed to the Virginia Supreme Court.

On September 16, 2011, the Court affirmed the trial court's decision. The Court held that intentional GHG emissions, even those with unintended results, did not constitute an "accident" (*i.e.*, an "occurrence") under the policies. The Court reasoned that "when the insured knows or should have known the consequences of his actions, there is no occurrence and therefore no coverage." *Steadfast*, 715 S.E.2d 28, 33-34. The Court thus adopted an objective view of an "occurrence" — viewing the issue from the perspective of a hypothetical, reasonable insured, rather than the subjective view of the particular insured. In other words, the fact that AES may have *subjectively* been unaware of the likelihood of this type of damage resulting from its GHG emissions, and thus negligent, was irrelevant to the Court's calculus. Senior Justice Koontz wrote a concurring opinion to "make clear and emphasize" that the majority's holding should be limited to the particular allegations of the *Kivalina* lawsuit and the definition of occurrence contained in the Steadfast policies. *Steadfast*, 715 S.E.2d at 34.

Policyholder's Petition for Rehearing Granted

Notably, however, the Court set aside its ruling on January 17, 2012, and granted policyholder AES's petition for rehearing in order to determine the appropriate standard governing whether damage was caused by an "occurrence." Although the Court initially concluded that the proper standard is whether the insured "knew or should have known" that its conduct would result in the alleged damage, AES stated in its petition that the applicable standard is whether an insured knew there was a "substantial probability" that its conduct would case the alleged harm. According to AES, by "omitting the words 'substantial probability' from the duty-to-defend test and relying solely on the words 'should have known,'" the Court "radically redefined 'accident' [or 'occurrence'] to exclude coverage in virtually all negligence cases." Pet. for Rehearing at 1. AES emphasizes that this "radical[]" restriction on coverage availability is exemplified by the instant case, where "the complaint alleges that the insured 'should have known' that an extraordinary series of events would follow from its acts and result in a harm that cannot plausibly be viewed as foreseeable, much less substantially certain." *Id.* at 1-2.

In support of its argument, AES quotes the principle recognized by the Eighth Circuit: "[T]o hold that an injury is not caused by accident because the injury is reasonably foreseeable would afford such minimal coverage as to be patently disproportionate to the premiums paid and would be inconsistent with the reasonable expectations of an insured purchasing the policy." *Id.* at 2 (alterations omitted). AES emphasizes that if "the term 'accident' as used in liability insurance policies excludes coverage for damage that should have been foreseen or expected by the insured, such insurance policies would be rendered all but meaningless." *Id.* (quotation omitted). Ultimately, AES stated that rehearing was essential to "correct a decision that w[ould] deprive AES of the coverage for which it bargained and render standard CGL policies 'all but meaningless.'" *See id.* at 3.

As the first case analyzing insurance coverage in connection with climate change litigation, the *Steadfast* decision will be a significant insurance opinion in 2012. Oral argument is scheduled in Richmond, Virginia in two weeks.

If you have any questions about this *Client Alert*, please contact one of the authors listed below or the Latham attorney with whom you normally consult:

Christine G. Rolph
+1.202.637.2200
christine.rolph@lw.com
Washington, D.C.

Cecilia O'Connell Miller
+1.619.236.1234
cecilia.miller@lw.com
San Diego

Elissa M. McClure
+1.619.236.1234
elissa.mcclure@lw.com
San Diego