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B.C. COURT OF APPEAL APPLIES POLLUTION EXCLUSION CLAUSE IN CGL POLICY

Richards Buell Sutton Insurance Newsletter

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In *Precision Plating Ltd. v. Axa Pacific Insurance Co.*, 2015 BCCA 277, the B.C. Court of Appeal considered the applicability of a pollution exclusion clause contained in a commercial general liability (“CGL”) policy in the context of overflowing chemical vats consequent of a strata complex fire.

THE FACTS

The insured was in the business of electroplating and operates its business out of leased strata premises. The insured maintained and used vats filled with toxic chemical solutions that could contaminate and pollute the surrounding property if not properly stored.

On April 12, 2011, a fire at the insured’s premises activated the building’s sprinkler system and water from the sprinkler system caused the chemical vats to overflow. Diluted chemical solutions ran onto and contaminated the surrounding property used by neighbouring businesses. Following the fire, four of the surrounding business owners commenced actions against the insured for property damage caused by contamination.

The CGL policy contained the following exclusion:

4. This insurance does not apply to:

(b) (i) Bodily Injury, Personal Injury or Property Damage caused by, contributed to by or arising out of the actual, alleged or threatened discharge, emission, dispersal, seepage, leakage, migration, release or escape at any time of Pollutants:

(1) at or from any premises, site or location owned, rented or occupied at any time by an Insured;

...

“Pollutants” means any solid, liquid, gaseous or thermal irritant or contaminant, including but not limited to smoke, odour, vapor, soot, fumes, airborne or waterborne particles, acids, alkalis, chemicals,



sewage, micro-organisms and waste. Waste includes (but is not limited to) materials to be recycled, reconditioned or reclaimed.

The insurer refused to defend the insured in the actions on the basis that the claims therein were, in substance, pollution claims and thus excluded from coverage. The insured sought a declaration of coverage.

At trial, the insurer conceded that fire damage would be covered, despite the fact that smoke, soot and chemicals were included in the definition of pollution. The trial judge took issue with the insurer's "elastic approach" to interpreting the pollution exclusion clause, as a literal interpretation of that clause would bar coverage for third party claims arising out of many of the usual consequences of fire and the third party claims as pleaded were at least in part for damage caused by fire. The trial judge found the exclusion clause was ambiguous, as a reasonable CGL policy holder would expect that the policy insured the very risk that occurred in this case, and concluded that the exclusion should not be applied "where to do so would nullify coverage provided by the policy and would be contrary to the reasonable expectations of the parties."

On appeal, the insurer contended the trial judge had erred in finding the pollution exclusion ambiguous. The insurer further argued that the trial judge erred in finding that the cause of the damage was fire and that the application of the pollution exclusion clause to the facts of the case would render the policy coverage nugatory and defeat the reasonable expectations of its insured.

The insured countered that it purchased liability insurance to cover it for liability caused by fire, and it had a fire on its premises, which caused damage including the overflow of the vats which contaminated the neighbouring business owners' properties. The insured argued that the policy was ambiguous and any ambiguity should be resolved in its favor.

THE RULING

Initially the court was challenged by the standard of appellate review of insurance policy decisions rendered by lower courts. Rulings in 2014 and 2015 from the Supreme Court of Canada and the Alberta Court of Appeal were considered on the standard of appellate review. Based on the wide precedential value of court rulings on insurance policy interpretation questions the court determined the standard of review was correctness of the ruling below rather than a palpable and overriding error of the ruling below.

The court went on to find the trial judge had erred in framing his analysis as a question of the cause of the damage, rather than the cause of the liability; it is not the "true cause" of the damage that is relevant, but the true cause of the liability. The court's decision states as follows (at para. 41):

"...The judge seemed to construe the policy as covering the peril of fire, rather than liability for



damages. What the judge needed to determine in this case was whether the pleadings alleged the escape of pollutants as the source of liability, which would then be a cause of the potential ‘loss’ for the insured...”

The court also considered the “concurrent cause” language contained in the exclusion. It found that the words “caused by, contributed to by or arising out of” ousted coverage when liability for the release of pollutants was a concurrent cause of the loss, as it was pleaded in this case to be along with fire.

The court also considered the trial judge’s conclusion that the exclusion was ambiguous. It ruled that the trial judge erred by conflating the reasonable expectations of the parties with a contextual analysis of the definition of “Pollutant”. The court found that a strict or literal interpretation of the policy would exclude coverage and that, in the contextual circumstances, the insured could not reasonably expect that it would be indemnified for escape of chemicals from its vats.

Finally, the court analyzed the pleadings of the third party business owners and found that all four actions alleged liability based on the release of pollutants – the very risk to which the exclusion clause was intended to apply. As a result of its conclusion that there was no possibility the insurer would be obligated to indemnify it did not have a duty to defend.

PRACTICAL CONSIDERATIONS FOR INSURERS

The B.C. Court of Appeal’s decision in *Precision Plating* confirms many established principles of insurance policy interpretation in the context of a pollution exclusion clause in a CGL policy.

Perhaps the most salient feature of *Precision Plating* is the court’s consideration of the standard of appellate review of insurance contracts. Insurers considering the appeal of a lower court’s adverse ruling on a question of policy interpretation should take comfort in the knowledge that predictability and certainty are among the courts’ primary objectives in interpreting insurance policy language.

In construing coverage under a CGL policy, remember the analysis should focus on the source of potential liability, and not the source of potential damage.

Where concurrent causes of loss are alleged, do not underestimate the power of language such as “caused by”, “resulting from” and “arising out of” to remove any ambiguity from the meaning of an exclusion clause.