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Fifth Circuit Says Insurers Do Not Have to Show Prejudice to Enforce Notice Provisions in Pollution Buyback Endorsements

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In two separate cases, the United States Court of Appeals for the Fifth Circuit, applying Texas law in one case and Louisiana law in the other, has held that insurers were not required to show prejudice before denying coverage for a pollution occurrence that the insured did not report within the 30 days required by the policies' pollution buyback endorsements. *Starr Indemnity & Liability Co. v. SGS Petroleum Service Corp.*, 719 F.3d 700 (5th Cir. June 18, 2013), and *In re Settoon Towing, L.L.C.*, 720 F.3d 268 (5th Cir. June 18, 2013).

In *SGS Petroleum*, an accidental release of a chemical occurred while one of the insured's employees was conducting operations at a plant in Texas. Although the insured learned of the release on the same day, it did not initially notify its excess insurer of the incident because the preliminary estimate for clean-up costs was within the limits of liability of its primary policy. The insured did not report the incident to the excess insurer until 59 days after learning about it. The excess insurer subsequently sought a declaratory judgment that it was not required to show prejudice before denying coverage because the insured did not report the incident within 30 days, as required by a pollution buyback endorsement contained in the policy. The trial court granted the insurer's motion for judgment on the pleadings, and the insured appealed.

The Fifth Circuit affirmed the trial court's decision on appeal, explaining that an insurance company does not always have to show prejudice to deny coverage for a failure to comply with a policy's notice provisions. The court reasoned that extending the notice period would expose the insurer to a broader risk than that expressly insured

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under the excess liability policy. In so doing, the court rejected the insured's argument that the modern trend in Texas case law was to require prejudice before enforcing a notice provision. The court found such cases distinguishable because they involved general notice requirements—not a specifically negotiated buyback provision—that were not "an essential part of the bargained-for exchange." Accordingly, the court held that the 30-day notice requirement, specifically bargained for when the pollution buyback endorsement was added to the policy, trumped the policy's general requirement that notice of an occurrence likely to cause liability be given "as soon as practicable."

The Fifth Circuit reached a similar conclusion in *Settoon Towing*. In that case, a towing company obtained a collision liability insurance policy with three layers of excess liability coverage. All three excess policies excluded coverage for pollution liability, but contained pollution buyback endorsements providing that the pollution exclusion would not apply if, among other things, the insured reported the occurrence giving rise to pollution liability within a specified amount of time. When one of the insured's vessels struck an oil well, causing oil to discharge into the water, the insured failed to notify the insurers within the time specified in the endorsements. As a result, the excess insurers sought a declaratory judgment that they were not liable because the insured did not satisfy the endorsements' notice requirements. The trial court held that the second- and third-layer excess insurers were not liable because the insured failed to comply with the notice provisions, but held that the first-layer excess insurer was liable because it had delayed delivery of the policy to the insured.

Agreeing with the trial court, the Fifth Circuit held that the pollution exclusions in the second- and third-layer excess policies barred coverage because the insured did not comply with the notice requirements of the pollution buyback endorsements. The court rejected the insured's argument that its non-compliance with the endorsements' notice provisions should not bar liability for three reasons: 1. the insurers were required to show that they were prejudiced by the delay; 2. in light of the policies' general notice provision requiring notice "as soon as reasonably practicable," delays beyond the specified notice period were permissible; and 3. the doctrine of impossibility excused the insured's failure to provide notice within the specified period. Rejecting the first argument, the court maintained that "both parties were sophisticated businesses," and that failure to comply with an "immediate notice" provision—which was an express condition precedent to coverage—precluded coverage regardless of whether the insurer was prejudiced by the delay. The court also rejected the insured's second and third arguments, explaining that the endorsements had primacy over the policies' other parts and that the doctrine of impossibility only applied to the failure to perform contractual obligations. Because the insured was not contractually obligated to satisfy conditions precedent, the court reasoned that the doctrine of impossibility was inapplicable.

Notwithstanding its rulings concerning the second- and third-layer excess policies, the court held that the first-layer excess insurer could not rely on the pollution exclusion contained in its policy because that insurer violated La. Rev. Stat. § 22:873(A), which requires insurers to deliver policies within a reasonable period of time after issuance. Because the first-layer excess insurer did not send the insured the excess policy until over two months after receiving the insured's premium payment (and after the insured notified the insurers of the incident), the court determined that the insured could not have known about the specific terms of the pollution

buyback endorsement. The court further explained that, under Louisiana law, "an insurer cannot take advantage of favorable policy terms where it delayed delivery of the policy after the insured pa[id] the premium."

A copy of the *SGS Petroleum* opinion is available here and a copy of the *Settoon Towing* opinion is available here.