II. DISCUSSION

A. The Only Decision Addressing the OECAA Found it Constitutional

The PCI Letter does not dispute that the federal district court for the District of Oregon in *Century Indem. Co. v. The Marine Group LLC*, 848 F Supp 2d 1238 (D Or 2012) examined the existing terms of the Oregon Environmental Cleanup Assistance Act ("OECAA"), ORS 465.475 *et seq.*, and found it passed constitutional muster. Nor does the PCI Letter make any distinction between the kind of regulation of environmental claims under the existing OECAA (enacted first in 1999) and that proposed by SB 814 because, in fact, there is none. Rather the PCI Letter would conclude that SB 814 (and by extension the OECAA) is unconstitutional because *Century Indemnity* was an "as applied" challenge as opposed to a ruling on "the facial constitutionality of the OECAA." This is a remarkable and unprecedented conclusion.

Except in the area of First Amendment rights, a party challenging a statute as facially unconstitutional "must establish that the statute is unconstitutional in all its applications." *State v. Hirsch*, 338 Or. 622, 627, 114 P3d 1104 (2005); *State v. Christian*, 249 Or. App. 1, 3, 274 P3d 262 (2012) ("[G]enerally a facial challenge to a law will fail if the law can constitutionally be applied in any imaginable situation."). For example, then-Justice De Muniz authored an opinion stressing that "[a] statute is not facially unconstitutional unless the statute is incapable of constitutional application in any circumstance." *Jensen v. Whitlow*, 334 Or 412, 421, 51 P3d 599 (2002). Similarly, the very fact that the *Century Indemnity* court upheld the OECAA in the context before it means that the OECAA is *not* facially unconstitutional.

The PCI letter essentially concludes that SB 814 and the OECAA cannot possibly be applied constitutionally because they would impair every possible insurance contract no matter what the policy language. However, the question under Article I, section 21 of the Oregon Constitution is in fact whether legislation "impair[ed] an obligation of contract." When a private contract is at issue, this question that cannot be answered in a facial challenge *because it is necessary to review the actual terms of the contract to determine whether it is impaired.* As shown below, the PCI Letter is fundamentally flawed because its skips the obvious but necessary first step of examining the terms of particular insurance contracts to determine if these terms are "impaired." This was a step not omitted by the *Century Indemnity* court and shows why *Century Indemnity* rather than the PCI Letter is the correct analysis.

B. The Contracts Clause Analysis in the Heavily Regulated Area of Private Insurance Contract

The PCI Letter's analysis of the Oregon Contracts Cause relies entirely on cases involving *public contracts*, cases in which "one of the *parties* to the contract (the state)... now is attempting to rely on a change in circumstances to permit it to alter its contractual obligations." *Strunk v. PERB*, 338 Or 145, 207, 108 P3d 1058 (2005) (emphasis in original); *see also id.* ("[W]e emphasize that we are not dealing here with legislation that impairs private contracts"); *State v. Petersen*, 308 Or 632, 643, 784 P2d 1076 (1989) (stressing "a distinction between private and

governmental contracts.") The PCI letter does not address the fact that SB 814 regulates private contracts in the already heavily regulated insurance industry. Indeed, the PCI Letter omits to mention that when the state is not allegedly attempting to escape its own contractual obligations, that "[t]he prohibitions against impairing the obligation of contracts in both the state and federal constitutions are not absolute." *Kilrpatrick v. Snow Mountain Pine Co.*, 105 Or App 240, 243, 805 P2d 137 (1991). And even in the case of public contracts, a Contracts Clause violation exists only when there is a substantial impairment of a contractual interest. *Hughes v. State,* 314 Or 1, 20, 838 P2d 1018 (1992).

SB 814 merely adds to the existing comprehensive regulation of the insurance industry. *See e.g.,* ORS chs 731-35, 737, 742-44, 748, 750; *Lovejoy v. City of Portland*, 95 Or 459, 479, 188 P 207 (1920) ("The purpose of [the Oregon Insurance Code] is to provide for the entire state a uniform and complete system of regulation and supervision of the insurance business.") The failure to address the existing comprehensive regulation of the insurance industry is a critical omission in the PCI Letter. *See Campanelli v. Allstate Life Ins. Co.*, 322 F.3d 1086, 1098-99 (9th Cir. 2003) (no Contracts Clause violation "[g]iven the highly regulated nature of the California insurance industry"); *Energy Reserves Group, Inc. v. Kansas City Power & Light Cor.*, 459 US 400, 416 (1983) (extensive government regulation of gas industry weighs against finding impairment of contract by new gas price regulation). For example, in *Weyerhaeuser Co. v. Ellison*, 208 Or App 612, 145 P3d 309 (2006), the court found that a change in workers compensation benefits was not a Contracts Clause violation. *See also Marquam Inv. Corp. v. Beers*, 47 Or App 711, 615 P2d 1064 (1980) (Residential Landlord and Tenant Act's affect on leases not a Contracts Clause violation.)

Moreover, as the Ninth Circuit explained in a sister case to *Strunk* and also involving PERS reform, the first question in the Contract Clause analysis is "whether there was a contractual agreement *regarding the specific... terms allegedly at issue.*" *Robertson v. Kulongoski*, 466 F3d 1114, 1117 (9th Cir 2006) (emphasis in original). Because PCI Letter skips this essential step and simply assumes that there are such terms that would be impaired by SB 814 it offers no reliable guidance.

C. The Effect of Section 2 Relating to Assignments Depends on the Policy Language

The flaw in the PCI Letter of not addressing specifically policy language shows in full force regarding Section 2 of SB 814, regulating assignments. Section 2 of SB 814 relates to assignment of existing insurance *claims*, not insurance policies. Consistent with *Portland School District No. 1J v. Great American Insurance Company*, 241 Or App. 161, 249 P3d 148 (2011), which recognized Oregon law allows assignment of insurance claims where there is a judgment, Section 2 makes clear that environmental insurance claims are also subject to assignment. The PCI Letter, however, relies on *Holloway v. Republic Indemnity Company*, 341 Or 642, 147 P3d 329 (2006), in which the court in the context of a sexual harassment claim interpreted specific policy language (in part, "[y]our rights or duties under this policy may not be transferred without our written consent"). 341 Or at 644 (brackets in original). The Oregon Supreme Court found

that, in the context of the particular policy at issue, it was able to construe the intent of the parties in that particular clause to mean that it prohibited the assignment of the insured's rights or duties without regard to whether they arose pre-loss or post-loss.

However, the historical insurance policies at issue in environmental insurance claims often have different policy language that would not prohibit assignment of claims as opposed to "an interest in the policy." Again, in Oregon to determine whether Section 2 "impairs" any contract, it obviously is necessary to examine the actual policy language. The PCI Letter erroneously assumes that all insurance policies have the identical language to that in *Holloway.* They do not.

In any event, Section 4(8) of SB 814 says that "the rules of construction set forth in this section and sections 2 and 7 of this 2013 Act do not apply if the application of the rule results in an interpretation contrary to the intent of the parties to the general liability insurance policy." For those insurance policies which have the *Holloway* language (including the historical policies that cover environmental claims), based on the current Oregon court interpretation of that language, Section 4(8) makes clear that SB 814 would be inapplicable and so would not impair any contract.

D. No Policy Language Addresses Contribution Between Insurance Carriers (Section 4(2)(d))

The same flaw applies to the PCI's Letter analysis of Section 4(2)(d) relating to non-cumulation clauses. The PCI letter simply assumes without citing policy language that the insurance policies subject to SB 814 have policy language that controls an insurance company's right to contribution against another insurance company. However, there is no such language nor could there be because *contribution between insurance companies is not based on contract.* Indeed, there is no contractual privity between co-insurers of the same insured. Rather, contribution rights between insurance companies are a judge-made doctrine based on equitable principles to which a Contract Clause analysis is necessary inapplicable. *See Cascade Corp. v. Am. Home Assur. Co.,* 206 Or App 1, 12-14, 135 P3d 450 (2006)(discussing Oregon's common law contribution scheme before the enactment of the OECAA). The OECAA replaced the common law contribution scheme in the case of environmental claims with a statutory one and sets forth the factors to be evaluating in determining contribution rights. ORS 465.480(4). SB 814 would simply make further adjustments to the existing statutory scheme.

E. SB 814's Interpretation of the Owned Property Exclusion is Not Contrary to the *Schnitzer* Case (Section 4(2)(e))

The point of the PCI's letter regarding Section 4(2)(e) is somewhat confused. The PCI Letter states that Section 4(2)(e) would impair "the previously bargained for obligation of an insurer to pay only for environmental contamination on an insured's own property," citing *Schnitzer. Investment Corp. v. Certain Underwriters,* 341 Or 128, 137 P3d 1282 (2006) for this proposition. However, the *Schnitzer* holding was exactly the opposite. *Schnitzer* held that when

only the insured's property is affected by environmental contamination, there are no "damages" due to the "property" damage. 341 Or at 133-135. Existing Oregon law is clear that environmental damage to the property of third parties, including the State's interest in the groundwater, is covered property damage. *Lane Electric Coop. v. Federated Rural Electric,* 114 Or App 156, 161, 834 P2d 502 (1992).

Even aside from the PCI Letter's apparent confusion about Oregon law, it ignores the actual language of Section 4(2)(e). The first sentence of the section merely restates that environmental contamination is property damage, which has long been decided by Oregon courts. The second sentence clarifies an issue that has not been decided by the Oregon courts. Specifically, it establishes Oregon law to be applied to costs incurred to respond to damage to third party property—like the contamination of surface water belonging to the State—when part of those costs are work that has to be done on the insured's own property to cut off the source of contamination to that third party property. This is an issue that *Schnitzer* did not address. Specifically, the *Schnitzer* Court said "this case does not require us to decide whether we would follow the *dictum* in *Wyoming Sawmills,*" a construction case where the insured's own property had to be removed and replaced in order to repair the damage to property of a third party. 341 Or at 138. To fill the gap in case law called out by the *Schnitzer* case, Section (4)(2)(e) of SB 814 provides that everything the insured does to remedy third party property, including actions it has to implement on its own property, are covered. The PCI Letter fails to explain how filling in a gap in the case law not addressed by specific policy language impairs anyone's contract. There is one particular by which SB 814 changes Oregon law, rather than just filling a gap in case law. The words "threatens to" in the sixth line of section 4(2)(e) will make Oregon law consistent with the majority rule in other states, which says that, even if a remedy to third party property is not yet required, the actions done on the insured's own property to cut off the pathway to that third party property are covered. Again, because this is not an issue addressed by any policy language, it cannot be an unconstitutional impairment of contract. And, as the PCI Letter itself admits, it is fully within the purview of the legislature to make such a clarification.

F. No Policy Language Addresses the Independent Counsel Issue (Section 7)

The PCI Letter concludes without citing any policy language that the right to independent counsel recognized by Section 7 of SB 814 "retroactively impairs a previously bargained for obligation to of an insurer to appoint and control the defense of the insured under a reservation of rights." The reason the PCI Letter cites no policy language may be that there is none on point, which the author of the letter would have discovered if standard policy language had been consulted before jumping to the conclusions stated in the letter. Standard policy language merely states that an insurer shall have "a right and a duty to defend" a potentially covered claim. It does not specify whether this defense is to be conducted by independent as opposed to insurance company-affiliated counsel. Indeed, standard policy language does not even allow an insurance company to reserve its rights. Rather, the concept of a reservation of rights is a judge created doctrine that allows an insurance company to agree to defend without giving up its

coverage defenses. *See e.g., United Pacific Ins. Co. v. Pacific Northwest Research Foundation*, 39 Or App 873, 877-78, 593 P2d 1278 (1979). The right to independent counsel has been created in other states by case law or statute in the recognition that insurer-affiliated lawyers can have a conflict of interest between their loyalty to the insurance company that is the source of their business (and sometimes even their employer) and their duties to the insured that, in Oregon for example, is their primary client. *See* Cal Civ Code § 2860 (creating right to independent counsel by statute); *San Diego Fed. Credit Union v. Cumis Ins. Soc'y, Inc.*, 162 Cal App 3d 358, 208 Cal Rptr. 494 (1984) (common law right to independent counsel.) In any event, Section 7 cannot possibly impair a contract when it is not contrary to any insurance policy language.

G. SB 814 Merely Adds to Existing Unfair Claims Practices Regulation (Section 6)

The PCI Letter's half-hearted examination of Section 6 merely concludes that it is "very possible" this section, which lists specific unfair environmental claims practices, impairs contracts because "it is unclear from the text how this section would be applied to claims settlement practices under existing policies." However, the *entire reason that unfair claims settlement practices laws—existing and proposed—are necessary is that the policies do not specify how claims are to be adjusted.* If, for example, the policies provided deadlines for insurance companies to respond to communications from insureds and pay defense costs and provided for (or precluded) interest on late payments, Section 6 would be unnecessary. However, the policies do not say anything about these issues. Rather Oregon existing unfair claims settlement practice statute, ORS 746.230, and the SB 814's proposed regulation of environmental claims adjusting is necessary to protect Oregon's insureds with regard to matters *not* addressed by policy language. Because there is no policy language to the contrary, there can be no violation of the Contracts Clause.

H. The Savings Clause is Applicable and Effective (Section 4(8)).

The reasoning on the PCI Letter regarding Section 8 is somewhat opaque, but it seems to express a concern that the savings clause in Section 4(8), which states that "the rules of construction set forth in this section and sections 2 and 7 of this 2013 Act do not apply if the application of the rule results in an interpretation contrary to the intent of the parties" is problematic because Sections 2 and 7 allegedly are not rules of construction. As discussed above, however, Section 2 plainly is a rule of construction relating to policy language that "requires the consent of an insurance company before rights under an insurance policy may be assigned." Section 2(1). Section 2 makes clear that unless the policy has language as in *Holloway* or is otherwise to the contrary, these "rights" include only the policies themselves and not matured claims.

We agree that there would not typically be a contract construction issue regarding Section 7 because the historical policies that cover environmental claims policies typically do not address one way or the other the availability of independent counsel or choice of counsel. However, in the event that there is a manuscript policy that does address the issue, Section 7 would be a rule

of construction. More importantly, in the case where there is no such policy language, the savings clause is beside the point because there is nothing to save and no constitutional issue.

III. CONCLUSION

The broad brush conclusions in the PCI Letter that SB 814 (and by extension the OECAA as it has existed since 1999) violate the Oregon Contracts Clause do not withstand scrutiny when carefully considered in light of what SB 814 actually does, the policy language in question and the governing law. The author of the PCI Letter admits that "my time to review SB 814 has been limited" and apparently did not include time to review relevant policy language to see whether SB 814 could actually "impair" any contract right, which is probably the source of the erroneous conclusions in the document.

Finally, we must comment on the PCI Letter's conclusion, with absolutely no supporting reasoning or evidence, that provisions of SB 814 "lack a significant and legitimate public purpose." Even a superficial review of the legislative record would show this to be erroneous. As was well established in testimony before the Senate Committee, and as documented in the 1999 and 2003 bills that created OECAA, investigation and cleanup of sites such as the Portland Harbor Superfund site has been delayed and hindered by insurance companies' failure to pay their bills in a timely way and to pay all of the costs that are due. The public purpose in facilitating the cleanup of Oregon's environment and preserving the jobs thousands of Oregonians working in and around Portland Harbor would certainly seem to be a significant and legitimate public purpose. Moreover, the interest in ensuring that environmental insurance claims are properly administered by insurance companies operating in the State of Oregon is itself a very significant and legitimate public purpose of the Oregon legislature.