

ENVIRONMENTAL LAW DEVELOPMENTS: HOPE AND AMBIGUITY IN ACHIEVING THE OPTIMUM ENVIRONMENT

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INTRODUCTION

The body of law that governs environmental regulation and litigation in Indiana expanded and evolved during the survey period. Indiana appellate decisions lead the nation in supporting insurance coverage for environmental claims, and a new decision further advances that law. Lawsuits against Indiana utilities by the federal government alleging violations of the Clean Air Act (“CAA”) potentially involve expenditures in the hundreds of millions of dollars. The intensity of litigation involving such massive financial exposure and the complexity of the CAA and its regulations have spawned important decisions in this area. Other significant environmental issues litigated in Indiana’s appellate courts during the survey period include development activities in isolated wetlands, citizen standing to challenge an agency action on environmental permits, proof of personal injury arising from exposure to chemicals in the environment, and significant expansion of a city’s right to use its power to seek damages and abatement of a public nuisance. The legal developments summarized below have far-reaching effects on the lives and livelihoods of Indiana citizens.

I. RECENT DEVELOPMENTS IN INDIANA ENVIRONMENTAL INSURANCE LAW—FUNDS FOR ENVIRONMENTAL CLEANUPS

On January 16, 2004, the Indiana Court of Appeals issued a decision, *PSI Energy, Inc. v. Home Insurance Co.*, that adds to a body of appellate law that makes Indiana one of the most favorable states in the nation for policyholders to obtain insurance coverage for environmental claims.¹ This law gives Indiana a unique and important tool to meet the enormous costs which have been imposed by the revolution in environmental regulation.

A. *The Sea Change in Environmental Regulation*

Indiana’s industrial history has left a legacy of significant environmental cleanup needs. Whether it is a corner gas station, a failed recycling facility, a municipal landfill, or a major factory, the reassessment of the nation’s environmental requirements over the past thirty or more years has required a vast social investment. Even routine small scale cleanups run into hundreds of thousands of dollars. A major remediation project at a large factory easily can

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1. 801 N.E.2d 705 (Ind. Ct. App. 2004).

cost tens of millions of dollars.

Regardless of whether change is mandated by the Comprehensive Environmental Response Compensation and Liability Act of 1980 ("CERCLA"),² the "Superfund" statute, the Resource Conservation and Recovery Act ("RCRA"), the hazardous waste regulatory statute, or any of the myriad of other government remediation statutes, or by common law or statutory remedies,³ all of this cleanup costs money. In the main, it costs money which no one anticipated having to spend. The liability for this unprecedented wave of cleanups is retroactive and strict, and it is imposed for practices which were perfectly legal when undertaken.

Consider, for example, a typical Superfund cleanup at a landfill. The landfill was fully licensed and inspected by state and local agencies. It land disposed a vast array of materials, including many, such as solvents, which, based upon our present understanding of the impact and operation of the chemicals in the environment, we no longer land dispose. Under CERCLA present and past owners and operators of the landfills and generators and transporters of the wastes to the landfill must pay the cleanup costs.⁴

Over the last forty years of the twentieth century, our environmental sensibilities have changed. From *Silent Spring* to Love Canal, to the Superfund and RCRA statutes, we witnessed a dramatic shift from subjective qualitative to "objective," largely quantitative regulation of the environment. While nuisance statutory and case law and anti-pollution statutes⁵ were enacted prior to this time, they were focused on acute, tangible instances of pollution which were detectable by ordinary sight, smell, or other senses. The notion that such work was the business of full-time state regulatory agencies, much less a federal agency, is a novel development of the years since 1970.⁶

In part, this shift was the result of scientific progress, not only in the understanding of the environmental effects of compounds, but also in our capacity to measure the presence of substances in the environment in increasingly smaller quantities. This allowed objective quantitative analysis without which

2. 42 U.S.C. § 9601-9675 (2003).

3. *E.g.*, Indiana's relatively new Environmental Legal Action Statute, IND. CODE § 13-30-9-2 (2003) (allowing a "person [to] bring an environmental legal action against a person who caused or contributed to a release of a hazardous substance . . . into the . . . soil or groundwater to recover reasonable costs of a removal or remedial action involving the hazardous substance").

4. 42 U.S.C. § 9607.

5. *See, e.g.*, IND. CODE § 32-30-6-6 (Indiana's nuisance statute first passed in 1881, which allows a citizen to bring an action for anything which is "injurious to health, indecent, offensive to the senses, or an obstruction to the free use of property"). Another example is Indiana's first Stream Pollution Control Act, IND. CODE § 13-18-3-1, which is intended to prevent any conduct which would injure "fish life or any beneficial animal or vegetable life."

6. Not surprisingly, this corresponds to the first wide-spread inclusion of environmental law courses in law school curriculum. One of the co-authors of this Article took the first environmental law course taught at Harvard Law School in 1978, offered only via mimeographed materials, because no acceptable text books on the subject were available.

broad-scale regulation is impossible. Without data reports neither contamination nor cleanup levels can be confirmed. This new possibility enhanced a heightened public and political appetite to acquire more environmental protection in measurable quantities.

Environmental protection, like national defense, is frequently cited as the classic paradigm of a public good. That is, everyone wants it, but the market choices of individuals and industry do not necessarily produce an optimum quantity. This is because an individual can freely enjoy a clean environment if someone else pays to maintain it. Individuals have little incentive to pay for marginal environmental improvements, and if no one has such incentives, we all may end up with less than what we want. Hence, a leading role for government developed to achieve, in some rough measure, the right amount of environmental protection, at least the optimum clean environment. This new role with new objective standards has produced a liability revolution.

But public goods still have costs. Somewhere, someone has to produce the resources to address the measure of what is clean enough. In the main, we have selected an individual attribution model, a model which seeks to attach the new costs to the original sources of what we lately have chosen to call unacceptable contamination.

This has been an imperfect attribution because it stretches back to attach present-day costs to conduct that occurred thirty to sixty or more years ago which typically was perfectly “legal” and not generally understood to be likely to result in significant damage or liability in the future. In a very real sense, this is both unfair and inefficient. The decision-makers, the companies, and the shareholders are only rarely the same entities as those when the choices were made. The impact of this falls upon not those who “benefited” from what has now resulted in cleanup costs, but upon those a generation or more removed from those choices.

For many insurance policyholders, this disproportionate unexpected imposition of costs is more than a theoretical problem. These costs can ruin a business, or sap all the value from a property. Fortunately, in Indiana, insurance purchased to protect against this type of cleanup liability and any other unexpected liability is available to help. To understand the intellectual foundation of this law, it is first necessary to grasp the unique nature of liability insurance policies.

B. The Nature of the Insurance Policy

It is common to find statements in judicial opinions, even in Indiana, along the lines of insurance policies are contracts and are subject to all the ordinary rules of contract interpretation.⁷ This is not really accurate. Insurance, especially in its modern pre-printed form, is not best described as a contract.

Insurance is a *product*—it is risk protection. It is not an individualized agreement, arrived at by free and open arm’s length negotiations over crucial details such as those which might characterize a “real” contract. The insurance

7. See, e.g., *Westfield Cos. v. Knapp*, 804 N.E.2d 1270, 1274 (Ind. Ct. App. 2004).

product is printed up in full, or nearly full, and final form. Generally, nothing more than the quantity purchased and the price paid are even discussed, much less negotiated. Even major insurers and their major corporate clients often do not obtain a clear understanding of what coverage is agreed upon (or *not* agreed upon) until the point of claim. Very often, the underwriting and claims wings of an insurer do not see the coverage in the same way. A partner of mine relates a story of an experienced policy underwriter justifying an ambiguous draft policy as follows: "We draft them this way so that we can say later that the policy means whatever we want it to mean." The lawyer present objected that this was not a sound way to design a policy. The story illustrates, however, how far from a classic contract insurance policies stray. Insurance companies do not even retain copies of these "contracts" for any significant length of time. On the policyholder side, the goal is usually an aggregate sum of the "best coverage we can get" or the "typical" or "usual" or "standard" coverage. There is no real closure or meeting of the minds.

The way in which insurance policies come into being also reflects their non-contractual nature. Normally, the person or entity desiring to protect itself from risk looks for insurance coverages. Usually with the assistance of a licensed insurance agent or broker, the prospective insured identifies the coverages desired and sets out to find them. Typically, there is an application, which frequently is filled out by the agent or broker. The application is then sent to one or more insurance companies (or "carriers"), which underwrite the application for the policy. During this underwriting process, the insurance company's underwriters evaluate the potential risk that the application appears to represent, determine if they will accept the risk, and, if so, with the help of the company's actuarial department, determine the price (or "premium"). The price (at least for liability coverage and for most other forms) is formula-driven. That is, the potential policyholder's amount of sales, total compensation, or number of employees will determine the premium price, based on a pre-set rate schedule for a specific category of business (e.g., manufacturers, offices, etc.), rather than on an individual assessment of operations. If the carrier accepts the risk, commonly the agent or broker is informed and will report back to the applicant that the agent or broker has "placed" the insurance with an insurance company or combination of companies for a proposed total premium. If the proposed policyholder approves of the price, the insurance deal is made, and the insurance company is bound to the risk.

After all of this, someone in the administration department of the insurance company pulls together an appropriate policy for the insured and mails it to the policyholder. At no point does the policyholder sign a contract. At most, the policyholder's signature is on the application. The policyholder's form of acceptance is payment of the premium. Indeed, the only signatures by the insurance carrier are pre-printed signatures of the president and the secretary of the insurance company. The policy may or may not be counter-signed with an original signature of the insurance broker or agent. Note that typically no lawyers have been involved in this process at all to this point.

There is nothing in law or common usage that makes the insurance coverage effective only upon the execution of a written contract. In many cases, the

insurance policy does not arrive until months or maybe years after the inception of the insurance coverage and sometimes does not arrive at all. Because of the way in which insurance is entered into and the fact that the policy may arrive much later, if ever, a rule has developed in Indiana, which provides that where there has been a parol acceptance of an insurance risk, “the contract in parol continues until the policy is delivered, when it is superseded by the policy.”⁸ The parties have probably never agreed to be bound in parol until the policy arrives in the mail; the policy just arrives in the mail.

There are other features of insurance policies that make them quite different from other types of contracts:

1. Policy forms are written by the insurance industry. Although they are not required to be followed, sample policy forms are prepared and filed with state insurance departments for approval and made available to all insurance companies through the Insurance Services Office, Inc. (“ISO”), headquartered in New York City. The ISO consults with a small number of selected insurance companies to draft these policy forms.

2. The insurance industry decides itself and without consultation with the market that certain coverages will be eliminated or modified.

3. The McCarran-Ferguson Act⁹ provides a specific antitrust exemption for this process on the basis that insurance companies’ coverages must be uniform in order to allow for coherent risk rating evaluations.

4. Extremely rarely is language contained in a policy actually negotiated between parties. The rare exception to this is called a “manuscripted” policy or endorsement.

5. As stated above, there is no requirement that the policyholder execute the policy.

C. Another Distinguishing Characteristic—Policy Interpretation Rules

Courts sometimes say they use the same rules of contract interpretation for insurance policies that they have for other types of contracts.¹⁰ However, while acknowledging that insurance policies are in certain respects like other contracts, the courts also have recognized that these policies are forms drafted by the insurance industry, and the courts have developed numerous specific rules governing their construction. The Indiana Supreme Court recently affirmed that such form policies and exclusions are strictly construed against insurers for just that reason: “This strict construal against the insurer is driven by the fact that the insurer drafts the policy and foists its terms upon the customer. ‘The insurance companies write the policies: we buy their forms or we do not buy insurance.’”¹¹

One major difference between the interpretation of general contracts and

8. *W. Assurance Co. v. McAlpin*, 55 N.E. 119, 122 (Ind. App. 1899).

9. 15 U.S.C.A. § 1011-1013 (2003).

10. *E.g.*, *Stockberger v. Meridian Mut. Ins. Co.*, 395 N.E.2d 1272, 1277 (Ind. App. 1979); *Am. States Ins. Co. v. Aetna Life & Cas. Co.*, 379 N.E.2d 510, 516 (Ind. App. 1978).

11. *Am. States Ins. Co. v. Kiger*, 662 N.E.2d 945, 947 (Ind. 1996) (quoting *Am. Econ. Ins. Co. v. Liggett*, 426 N.E.2d 134, 142 (Ind. Ct. App. 1981)).

insurance contracts in Indiana is the absence of an “implied covenant of good faith” in general contracts in this state side by side with the imposition of an “implied covenant of good faith” on insurers. The law of general contract interpretation in Indiana is very traditional. While many states, including our neighbors, have adopted numerous rules concerning various implied covenants with respect to general contracts, including covenants of “good faith” and “fair dealing,” the courts of Indiana have consistently and emphatically refused to do so in the absence of an ambiguous contract.¹²

On the other hand, under Indiana law, an insurance company has a “special relationship” with its insureds that in many respects is fiduciary in nature and requires the insurer to deal with its policyholders in “good faith.”¹³ A breach of the obligation of good faith by the insurer may give rise to a tort action for compensatory damages or an action for punitive damages.¹⁴ Factors that help determine whether an insurance company has acted in good faith with respect to policy interpretation include whether the insurer has taken inconsistent positions with respect to the same policy language, whether the insurer has a factual basis for its coverage position, whether the insurer has any legal support for its position, and the nature and extent of any investigation conducted prior to arriving at the coverage position.

Despite the occasional nod to the supposed contractual nature of an insurance policy, the cases actually show, on the whole, that an insurance policy is very different from an ordinary contract. For example “[a]n insurance policy should be so construed as to effectuate indemnification . . . rather than to defeat it.”¹⁵ “This is particularly true where a policy provision excludes coverage.”¹⁶ An exclusionary clause must “clearly and unmistakably” bring the excluded condition within its scope to be effective.¹⁷

Terms in an insurance contract may not be construed in a manner which is “repugnant to the purposes of the policy as a whole.”¹⁸ Policy terms are interpreted from the perspective of an ordinary policyholder of average intelligence.¹⁹ Terms are given a consistent meaning throughout an insurance

12. See *Rothe v. Revco D.S., Inc.*, 976 F. Supp. 784, 794-95 (S.D. Ind. 1997); *First Fed. Sav. Bank v. Key Mkts., Inc.*, 559 N.E.2d 600, 604 (Ind. 1990).

13. *Erie Ins. Co. v. Hickman*, 622 N.E.2d 515, 518-19 (Ind. 1993).

14. *Id.*

15. *Masonic Accident Ins. Co. v. Jackson*, 164 N.E. 628, 631 (Ind. 1929); see also *Tate v. Secura*, 587 N.E.2d 665, 668 (Ind. 1992); *Eli Lilly & Co. v. Home Ins. Co.*, 482 N.E.2d 467, 470 (Ind. 1985).

16. *Travelers Indem. Co. v. Summit Corp. of Am.*, 715 N.E.2d 926, 936 (Ind. Ct. App. 1999).

17. *Masonic*, 164 N.E. at 631 (coverage “will not be destroyed by language of exception, unless such exception shall be clear and free from reasonable doubt”); *Ashbury v. Ind. Union Mut. Ins. Co.*, 441 N.E.2d 232, 242 (Ind. Ct. App. 1982); *Huntington Mut. Ins. Co. v. Walker*, 392 N.E.2d 1182, 1185 (Ind. App. 1979).

18. *Prop. Owners Ins. Co. v. Hack*, 559 N.E.2d 396, 402 (Ind. Ct. App. 1990) (citing *J.B. Kramer Grocery Co., Inc. v. Glens Falls Ins. Co.*, 497 F.2d 709, 712 (8th Cir. 1974)).

19. *Ashbury*, 441 N.E.2d at 237.

policy.²⁰

Ambiguity—which results in a construction in favor of coverage—can and will be found according to the following standard: “[A]n insurance policy is ambiguous if reasonable persons may honestly differ as to the meaning of the policy language.”²¹ Words that have been accorded different meanings by different courts are ambiguous as a matter of law.²² If there is *any* ambiguity in a policy term, it *must* be interpreted in favor of the insured and in favor of coverage, especially in an exclusion from coverage. The Indiana Supreme Court in *American States Insurance Co. v. Kiger* expressly affirmed this point: “Where there is ambiguity, insurance policies are to be construed strictly against the insurer. This is particularly true where a policy excludes coverage.”²³

The policyholder need not prove that its suggested interpretation of a policy term is the *only* reasonable interpretation. If *any* reasonable construction of a term supports coverage, that construction governs as a matter of law.²⁴ “Where any reasonable construction can be placed on a policy that will prevent the defeat of the insured’s indemnification for a loss covered by general language, that construction will be given.”²⁵ To prevail in a denial of coverage, therefore, the insurer must demonstrate that its construction of insurance policy terms is the *only* plausible or reasonable reading of the policy language.

A policyholder’s expectations of coverage must be honored. Some jurisdictions label this approach as the “reasonable expectations doctrine.”²⁶ The Indiana Supreme Court has specifically endorsed adherence to the policyholder’s reasonable expectations of coverage: “In the instant case, based on the relevant policy language, Lilly could have reasonably formed an expectation that it was purchasing insurance coverage for all future liability arising from the manufacturing and selling of DES.”²⁷ These reasonable expectations are particularly important where policy language is ambiguous.²⁸

20. *Taracorp., Inc. v. NL Indus., Inc.*, 73 F.3d 738, 744 (7th Cir. 1996); *Thompson v. Amoco Oil Co.*, 903 F.2d 1118, 1121 (7th Cir. 1990).

21. *Eli Lilly & Co. v. Home Ins. Co.*, 482 N.E.2d 467, 470 (Ind. 1985).

22. *See Summit*, 715 N.E.2d at 936; *Hartford Accident & Indem. Co. v. Dana Corp.*, 690 N.E.2d 285, 295 (Ind. Ct. App. 1997); *Ind. Ins. Co. v. O.K. Transport, Inc.*, 587 N.E.2d 129, 132 (Ind. Ct. App. 1992); *Ind. Dep’t of Revenue v. RCA Corp.*, 310 N.E.2d 96, 99 (Ind. App. 1974), *rev’d on other grounds*, 520 N.E.2d 457 (Ind. Ct. App. 1988).

23. 662 N.E.2d 945, 947 (Ind. 1996); *see also* *Governmental Interins. Exch. v. City of Angola*, 8 F. Supp. 2d 1120, 1125 (N.D. Ind. 1998); *Lilly*, 482 N.E.2d at 470-71; *Summit*, 715 N.E.2d at 936.

24. *Lilly*, 482 N.E.2d at 471; *see also* *Am. Econ. Ins. Co. v. Liggett*, 426 N.E.2d 134, 144 (Ind. Ct. App. 1981).

25. *Liggett*, 426 N.E.2d at 144 (citation omitted).

26. Certain jurisdictions differ substantially from Indiana by explicitly rejecting adherence to the policyholder’s reasonable expectations of coverage. Examples of these jurisdictions include Colorado, Florida and Pennsylvania.

27. *Lilly*, 482 N.E.2d at 470.

28. *See Summit*, 715 N.E.2d at 936; *Great Lakes Chem. Corp. v. Int’l Surplus Lines Ins. Co.*,

The common thread among most of the rules in Indiana is that coverage will be effectuated whenever that is reasonably possible. These rules sensibly arise from the actual nature of the insurance policy. There is no real meeting of the minds when a policy is purchased; instead, a risk protection product is acquired. As in typical modern products liability law, risks arising from defects—ambiguity—in the product are properly assigned to the manufacturer, in this case the insurance company. The insurer is in the best position to avoid the risk through clarification of policy terms, and the risk of loss is most efficiently and fairly placed there. That is why these special rules of policy construction have developed and make sense.

D. Indiana's Courts Respond to Environmental Liability Claims

This law has had significant application as to environmental liability claims, which have presented an unanticipated loss not clearly addressed by the form policies. Insurance coverage law is a state-by-state determination. As in so many areas of the common law, Indiana jurisprudence on insurance coverage for environmental liability claims has developed through step by step analysis of specific issues. Numerous trial court decisions²⁹ preceded and followed these appellate landmarks.

But the first Indiana Supreme Court decision to address coverage for these claims was a major one that drew national attention. In *American States Insurance Co. v. Kiger*,³⁰ the Indiana Supreme Court, on direct appeal from the Hendricks Circuit Court to address an issue of “great public importance,” held that both forms of the pollution exclusion found in comprehensive general liability (“CGL”) policies from 1970 to the present were ambiguous. Therefore, these exclusions were construed in favor of coverage.

The early “standard” form (1970-1985) exclusion purports to bar coverage for any damage caused by discharge of contaminants, pollutants, or chemicals unless that release was “sudden and accidental.” Insurers insisted “sudden” required a strictly temporal construction, meaning “all at once” and, thus, excluding gradual contamination, the predominant kind of contamination. The policyholder contended that “sudden,” which was not defined in the policy, at least as plausibly means “unexpected.”

The supreme court traced the history of the exclusion, noting that the insurance industry claimed its addition was a “mere clarification” that no coverage was provided for “expected and intended” damage.³¹ The court noted that the industry’s own construction of the language demonstrated the ambiguity

638 N.E.2d 847, 850 (Ind. Ct. App. 1994); Prop. Owners Ins. Co. v. Hack, 559 N.E.2d 396, 402 (Ind. Ct. App. 1990).

29. See, e.g., *Riverside Oil, Inc. v. Federated*, 1994 U.S. Dist. LEXIS 20394 (C.D. Ill., Aug. 19, 1994) (discussing pollution and “owned property” exclusions and “personal injury” coverage); *Sam Winer & Co. v. Commercial Union*, No. 20D01-9207-CP-247 (Elkhart Super. Ct., Feb. 19, 1994) (discussing what constitutes a “suit” which triggers an insurers’ duty to defend).

30. 662 N.E.2d 945, 947 (Ind. 1996).

31. *Id.* at 948.

of the phrase, “ambiguity that requires the Court to construe the insurance policy in favor of the insured and against the insurer who drafted it.”³² Thus the vast bulk of claims are covered unless the damage was expected and intended.

The court also assessed the “absolute” exclusion found in policies after 1985. This exclusion barred coverage for claims resulting from the discharge of “pollutants.” “Pollutants” was defined as “any solid, liquid, gaseous or thermal irritant, or contaminant, including smoke, vapor, soot, fumes, acids, alkalis, chemicals, and waste. Waste includes materials to be recycled, reconditioned or reclaimed.” The court held this definition is so overbroad that it is unenforceable since it would bar coverage for any claim involving virtually any substance.³³

The supreme court’s reasoning rested on the Indiana rules of insurance policy construction detailed above that favor coverage wherever that is reasonably possible, and which require that any ambiguity be interpreted in favor of the policyholder and in favor of coverage.³⁴

Kiger has had an enormous impact.³⁵ It has made hundreds of millions of

32. *Id.*

33. *Id.*

34. *Id.* at 947.

35. The Indiana legislature also rejected the insurance industry’s effort to ensure enforcement of the absolute pollution exclusion in a literal, all-encompassing way. A bill was passed during the first 1997 legislative session, House Enrolled Act 1583, which attempted to reverse, prospectively, *Kiger*’s absolute pollution exclusion ruling and to codify broad application of the insurance industry’s absolute pollution exclusion. The policy language at issue was identical in all important respects to the policy language in EMI’s policies. Governor O’Bannon’s veto message resoundingly rejected the bill:

A strong insurance industry is vital to the economic health of this state. The legislative and executive branches should encourage stability and clarity in the insurance market. Nevertheless, I am today vetoing House Enrolled Act 1583, which deals with environmental insurance.

House Enrolled Act 1583 would codify what should be a private contractual matter between an insurer and its insured. The bill provides that if an insurance policy contains certain prescribed language, or “substantially similar” language, then there is no coverage for losses arising out of the discharge or release of “pollutants.” I believe that the definition of “pollutants” in this bill may increase the risk that insurers could deny coverage for claims having nothing to do with pollution in the ordinary sense of the word.

This bill could adversely affect large and small Indiana businesses who manufacture or use products that would be considered pollutants under this bill. A cross section of these businesses oppose this bill in its current form. No other state has enacted legislation of this type. The insurance industry can address the problem by drafting a clear and unambiguous contractual pollution exclusion. I am therefore vetoing House Enrolled Act 1583.

H.R. Enrolled Act 1583, 109th Gen. Assem., 1997 Sess. (Ind. 1997) (Governor O’Bannon’s veto

dollars available to clean up the environment. It means that virtually any CGL policy applies to pay an environmental liability or property damage claim. Pollution exclusions at most apply only to limit claims under pre-1985 policies where the damage was expected or intended.³⁶

Shortly after *Kiger*, the supreme court decided *Seymour Manufacturing Co. v. Commercial Union Insurance Co.*³⁷ *Seymour* addressed the insurer's duty to defend its policyholder against environmental claims. CGL policies contain two promises. The first is to defend the policyholder against any suit; the second is to indemnify the policyholder for amounts it must pay to resolve a claim. The policyholder in *Seymour* was the entity that had run the now-infamous solvent recycling facility in Seymour, Indiana that became the Seymour Superfund Site. The insurer presented evidence that the policyholder had

stored multiple barrels of liquid waste at its facility, did not identify or otherwise label the barrels in order to assure the proper method of disposal, did not make any attempt to separate wastes from other incompatible wastes, permitted barrels to rust or otherwise deteriorate, did not clean up open and obvious spills, did not properly cover many barrels, and received some types of waste for which it had no treatment facility.³⁸

Despite this evidence, which ultimately could have supported an expected or intended coverage defense, as well as other defenses not connected to this evidence, the supreme court held that the insurer had a duty to defend its policyholder against the federal government's environmental claims as a matter of law.³⁹ The court entered summary judgment on defense costs in favor of the policyholder. The court centered its decision on the ambiguity identified in *Kiger* and the well established principle that "the duty to defend is broader than the duty to indemnify."⁴⁰

The court of appeals struck down two additional key insurer defenses in

message). An over-ride vote during the next legislative session did not succeed. A similar bill, Senate Bill 309, which attempted to codify a similarly broad application of the absolute pollution exclusion, was introduced and defeated in that session. *See also* *Great Lakes Chem. v. Int'l Surplus Lines Ins. Co.*, 638 N.E.2d 847 (Ind. Ct. App. 1994), *trans. withdrawn*. After having argument on this case the same day as *Kiger*, the supreme court withdrew its initial grant of transfer and reinstated a court of appeals decision rejecting application of pollution exclusions to product liability claims and holding excess insurers liable for defense costs. *See id.*

36. *See also* *Great Lakes Chem.*, 638 N.E.2d at 847, *trans. withdrawn*. After hearing argument on this case the same day as *Kiger*, the supreme court withdrew its initial grant of transfer and reinstated a court of appeals decision rejecting application of pollution exclusions to product liability claims and holding excess insurers liable for defense costs.

37. 665 N.E.2d 891 (Ind. 1996).

38. *Id.* at 893.

39. *Id.*

40. *Id.* at 892.

1997. In *Hartford Accident & Indemnity Co. v. Dana Corp.*,⁴¹ it held that the “suits” insurers must defend under *Seymour* included all adversarial administrative proceedings as well as courthouse lawsuits. Insurers had insisted only courthouse proceedings are included in the term “suit,” which was not defined in their policies.⁴² The court also ruled that the “damages” an insurer must pay under a CGL policy includes amounts paid by policyholders to comply with a cleanup order.⁴³ Insurers had argued that “damages” in their insuring clauses meant only “legal” damages contained in a money judgment. The court held both terms, “suit” and “damages” were ambiguous.⁴⁴

Dana I also rejected insurers’ claims that “containment costs” were not damages, because those sums are not spent to “fix” anything.⁴⁵ Containment measures, to prevent further damage, are often key components of remedial actions, as they prevent further damage and allow the damaged environment to recover. The court, recognizing that “damages” should not be construed to encourage further environmental degradation in order to be covered by insurance, agreed: “The cost of containment as a remedial action taken to prevent further release of hazardous substances would be considered damages.”⁴⁶

The court of appeals handed down two more major decisions in 1999. In the first, *Travelers Indemnity Co. v. Summit Corp.*,⁴⁷ the court found that “personal injury” coverage applied to environmental liabilities. “Personal injury” coverage is not the same thing as “bodily injury” coverage. It is a special coverage part insuring claims for certain specified wrongs, including “wrongful entry” and “invasion of the right of private occupancy.”⁴⁸ After examining dictionary definitions and the multitude of conflicting cases on this point around the country (a split in authority was important evidence of ambiguity), the court found that these provisions “must be construed to cover the environmental damages” included in the wide range of cleanups in that suit.⁴⁹

*Employers Insurance of Wausau v. Recticel Foam Corp.*⁵⁰ affirmed an insurer’s duty to defend, but it is mainly noteworthy on procedural grounds. It affirmed denial of the insurer’s *forum non conveniens* motion and application of Indiana law to the sole cleanup site in Tennessee. *Forum non conveniens* is a doctrine that allows dismissal of litigation in favor of a more conventional forum. It is expressed in Indiana Trial Rule 4.4(C) and Indiana common law.⁵¹ On the

41. 690 N.E.2d 285 (Ind. Ct. App. 1997) (“Dana I”).

42. *Id.* at 294-97.

43. *Id.* at 297-98.

44. *Id.*

45. *Id.* at 298.

46. *Id.*

47. 715 N.E.2d 926 (Ind. App. 1999).

48. *Id.*

49. *Id.* at 938. *Summit* also affirmed the ambiguity of both pollution exclusions and of “suit” and “damages.”

50. 716 N.E.2d 1015 (Ind. App. 1990).

51. *McCracken v. Eli Lilly & Co.*, 494 N.E.2d 1289 (Ind. Ct. App. 1989).

forum non conveniens issue, *Recticel* ruled that great weight is given to a policyholder-plaintiff's choice of forum which is to be disturbed only to avoid "substantial injustice."⁵² That case recognized the modern reality of litigation between multi-state parties, that it will necessarily involve movement of witnesses and evidence across state lines.⁵³

Recticel's choice of law holding must be read together with similar affirmation of the application of Indiana law in *Dana I* and *Summit*.⁵⁴ All three decisions assess the factors set forth in section 188 (contracts) and section 193 (insurance policies) of the Restatement (Second) of Conflicts of Laws.⁵⁵ Some factors, such as the place of domicile of the parties or where the insurance policies were countersigned, are entitled to little weight, since they are so various and insignificant in the acquisition of insurance policies from multiple insurers from all over the United States. Instead, the courts have placed emphasis on the significance of the Indiana connection to the cases—*Dana I* (more cleanup sites and Dana plants than any other state), *Summit* (more cleanup sites), and to *Recticel* (headquartered in Indiana and one plant here during a major portion of the coverage period). A substantial Indiana connection supports application of Indiana law.⁵⁶

In *Allstate Insurance Co. v. Dana Corp.*,⁵⁷ the Indiana Supreme Court held that the "all sums" language which exists in the insuring clauses of most CGL policies allows a policyholder facing environmental liabilities to select which of the policies involved in a multi-year occurrence to use to respond to a loss. In the typical policy's insuring clause the insurer promises to pay "all sums" the policyholder becomes obligated to pay as damages on account of property damage or bodily injuries caused by an occurrence. Thus, when multiple insurance policies are triggered by contamination spanning several years—which is typical in cases involving gradual environmental contamination—the insurers are jointly and severally liable for the loss, subject only to policy limits.⁵⁸ This is an exceptionally important holding. Insurers used to insist they would pay only for damage the policyholder could prove occurred in their policy period, or only a "pro rata" share of the entire loss. If the policyholder was unable to find all possibly applicable policies, or had used up coverage on other claims, or had an insolvent insurer, or was self-insured, it would be stuck with less than a complete recovery. Under *Dana II*, insurers can no longer escape paying their full policy limits.

The Indiana Supreme Court also adopted an "injury in fact" approach to the

52. 716 N.E.2d at 1021.

53. *Id.* at 1022-23. The trial court in *Dana I* reached a similar conclusion.

54. *Id.* at 1023-25; *Summit*, 715 N.E.2d at 930-33; *Dana I*, 690 N.E.2d at 291-94.

55. RESTATEMENT (SECOND) OF CONFLICTS OF LAWS §§ 188, 193 (1971).

56. The *Recticel* court also instructed how a policyholder must prove defense costs and deferred application of an estoppel against coverage defenses for breach of duty to defend in favor of an existing bad faith claim. 716 N.E.2d at 1027-29.

57. 759 N.E.2d 1049 (Ind. 2001) ("Dana II").

58. *Id.* at 1057-58.

“trigger” of policies by environmental contamination; if damage takes place in the policy period, coverage is triggered. If environmental damage spars a number of years, all the policies are available to apply to the loss.⁵⁹

Finally, the *Dana II* court held that the “owned property” exclusion which exists in most liability policies does not bar coverage for environmental liability claims.⁶⁰ This exclusion was used by insurers to refuse all pay for on-site cleanups at policyholder plants. The supreme court held the exclusion simply did not apply to claims for cleanup liability on owned property resulting from property damage (which is not for the benefit of the policyholder, but is an imposition of a liability on the policyholder).⁶¹

In 2002 the Indiana Supreme Court spoke once more on the absolute pollution exclusion. In *Freidline v. Shelby Insurance Co.*,⁶² the court summarily affirmed the holdings of *Kiger* and *Seymour* that the absolute pollution exclusion (here applied by an insurer against a carpet fume claim) was overbroad and unenforceable. The insurer had claimed the exclusion was enforceable because the definition of “pollutants” included the word “fumes,” but the court disagreed. The *Freidline* court overturned the lower court’s grant of a bad faith award to the policyholder for the insurer’s continued use of the exclusion after *Kiger*, noting the relatively recent litigation over the conclusion.⁶³ The next insurer to rely on that exclusion may not be so fortunate.

All of this appellate work has been mirrored in the trial courts. A host of Indiana trial courts have applied these principles to a wide range of claims and costs. Numerous summary judgments have been issued in policyholder’s favor on the duty to indemnify⁶⁴ or the duty to defend⁶⁵ their policyholder with respect

59. *Id.* at 1060.

60. *Id.* at 1056.

61. *Id.* (applying the reasoning of *Patz v. St. Paul Fire & Marine Ins. Co.*, 15 F.3d 699, 705 (7th Cir. 1994)).

62. 774 N.E.2d 37 (Ind. 1002).

63. As noted above, insurers in Indiana may be held liable for the tort of bad faith claims handling under *Erie Insurance Co. v. Hickman*, 622 N.E.2d 515, 518 (Ind. 1993), and the court of appeals, citing *Kiger*’s clear precedent on the exclusion, had imposed such an award.

64. See, e.g., *Muncie Sanitary Dist. v. Harleysville Ins. Co.*, No. IP-94-1401-C-D/F (S.D. Ind. Jan. 7, 1999); *Governmental Interinsurance Exch. v. City of Angola*, 8 F. Supp. 2d 1120 (N.D. Ind. 1998); *CGB Enter., Inc. v. Old Republic Ins. Co.*, No. 65D01-0002-CP-00014 (Posey County Cir. Ct. May 15, 2002); *EMI Co. v. Royal Ins. Co. of Am.*, No. 49D06-9811-CP-1550 (Marion County Super. Ct. Aug. 22, 2000), *vacated by agreement*; *Gen. Housewares Corp. v. CNA Ins. Co.*, No. 49D06-9706-CP-920 (Marion County Super. Ct. Jan. 6, 2000); *Henschen Oil, Inc. v. Burris Equip. Co., Inc.*, No. 20C01-9805-CT-036 (Elkhart County Cir. Ct. June 15, 2000); *Contractors United, Inc. v. Commercial Union Ins. Co.*, No. 49C01-9406-CP-2003 (Marion County Cir. Ct. Oct. 27, 1999); *Crown Int’l, Inc. v. Great N. Ins. Co.*, No. 49D12-9704-CP-522 (Marion County Super. Ct. March 13, 1998).

65. See, e.g., *Muncie Sanitary Dist.*, No. IP-94-1401-C-D/F; *City of Angola*, 8 F. Supp. 2d 1120; *Lear Corp. Auto. Sys., Inc. v. Allianz Underwriters Ins. Co.*, No. 49D10-9805-CP-0729 (Marion County Super. Ct. Dec. 22, 2002); *Heritage Env’tl. Servs., LLC v. Sentry Ins.*, No.

to environmental claims.

Against this backdrop, the Indiana Court of Appeals examined five key issues in *PSI Energy, Inc. v. The Home Insurance Co.*⁶⁶ The *PSI* action arose from PSI's claims of substantial cleanup costs at the PSI's former manufactured gas plant ("MGP") sites.

1. *Lost Policies.*—Several of the insurers argued that because PSI had been unable to produce complete copies of their policies, PSI could not meet its burden of proving that coverage existed for its claims.⁶⁷ The trial court had agreed with the insurers. But the court of appeals reversed, holding that PSI did not have to produce policy language verbatim, but only the substance of the policies. The *PSI* court held that PSI could present the broad range of secondary evidence it had assembled to prove the policies, including its history of premium payments, employee testimony, and expert testimony concerning the likely terms in such form policies.⁶⁸ The court concluded that expert testimony, even where the expert could not testify with absolute certainty as to the likely terms in the lost policies, is admissible, when supported by the kind of other evidence that PSI had presented.⁶⁹

2. *Expected or Intended Damage.*—The *PSI* court held that the concept of "fortuity," meaning that the damage giving rise to a liability cannot be expected or intended by the policyholders, is inherent in all CGL policies.⁷⁰ However, a policyholder can prove this point based on a subjective, rather than objective, basis.⁷¹ The use of a subjective standard means that mere negligence or even recklessness on the part of the policyholder will not prove that the resulting damage was expected or intended and that such intent is based on what the policyholder actually believed.

3. *Trigger.*—The *PSI* court followed *Dana II* and held that where damage occurs over a multi-year period, each policy within that period is triggered and obligated to pay "all sums."⁷² This is so even where, as with PSI's earlier policies, the policy requires that the "occurrence" "commence during the policy period."⁷³ The court saw no difference between this language and the language in *Dana II* requiring that an "occurrence" take place during the policy period.⁷⁴ In a few later policies which define "occurrence" as "one happening," a "series of happenings," or "one event," the court held that PSI must show an event

49F12-0112-CP-004803 (Marion County Super. Ct. Dec. 18, 2002); *CGB Enter.*, No. 65D01-0002-CP-00014; *Contractors United*, No. 49C01-9406-CP-2003.

66. 801 N.E.2d 705 (Ind. Ct. App. 2000).

67. *Id.* at 717.

68. *Id.* at 717-22.

69. *Id.*

70. *Id.* at 722-24.

71. *Id.* at 727-30.

72. *Id.* at 732-33.

73. *Id.* at 733-34.

74. *Id.*

causing damage during the policy period.⁷⁵

4. *Notice.*—The insurers also argued that some of PSI's claims should be denied because of alleged "late notice." The insurers argued that PSI should have provided notice as soon as it became aware of any potential liability. The *PSI* court held that "the duty to notify an insurance company of potential liability is a condition precedent to the company's liability to its insured" and that "noncompliance with notice of claim provisions, which results in an unreasonable delay, triggers a presumption of prejudice to the insurer's ability to prepare an adequate defense."⁷⁶ However, the court also found that environmental liability cases are unique in that they require "lengthy site investigation and expert opinion" to determine exactly when the covered occurrence actually took place, unlike the automobile and personal injury cases upon which the insurers had based their argument.⁷⁷ This information, the court ruled, was "essential to PSI's determination of which insurers were potentially liable under the numerous policies it had purchased between 1950 and 1985."⁷⁸ Thus, the court concluded that there were issues of fact concerning the timeliness of PSI's notice. Moreover, because the insurers had not alleged any specific prejudice there also was an issue as to whether the insurers were actually prejudiced by the timing of the notice.

5. *Justiciability.*—Are the insurance questions ripe for review? The issue was raised by an excess insurer whose policies it claimed incepted well above the current cost of the cleanup. The *PSI* court held that under Indiana's Declaratory Judgment Act, PSI had the right to proceed against this excess insurer for a declaration as to the parties' rights and obligations under even high-level excess policies because, while current costs had not yet reached the level of those policies, site investigations were still on-going and the state environmental agency had not determined what level of cleanup would be required.⁷⁹

The fact the policyholders can prove the contents of lost policies by secondary evidence and expert testimony about likely form provisions is of critical importance, since many policyholders are unable to retrieve policies they purchased many years ago, and insurers do not retain copies. The clarification that a subjective standard applies also is very important, and is consistent with the norm that even unwise or grossly negligent acts are covered.

Insurance funds, obtained through the cases cited above, are literally reshaping Indiana. Sites can be cleaned up without destroying companies. Abandoned polluted sites in our cities can be addressed. The risk of unanticipated social costs are now spread across a much wider body of assets, which now includes the entities which collected premiums to provide just this protection.

The full scope of our investment in cleaning the environment remains

75. *Id.* at 735-36.

76. *Id.* at 715-16.

77. *Id.* at 716-17.

78. *Id.* at 717.

79. *Id.* at 713-15.

unclear. In the past year, Indiana courts turned attention to the air and to wetlands. In each case, challenging issues remain unsettled.

II. NEW SOURCE REVIEW LITIGATION IN INDIANA

Clean Air Act ("CAA") enforcement lawsuits continue to hold center stage in Indiana's environmental law arena. Until recently, two lawsuits brought by the federal government against Indiana utilities were pending in the U.S. District Court for the Southern District of Indiana. *United States v. Southern Indiana Gas & Electric Co.* ("SIGECO"),⁸⁰ which settled by Consent Decree on June 6, 2003, spawned six important decisions on aspects of this highly controversial and hotly litigated federal enforcement initiative. *United States v. PSI Energy, Inc.* still pends.⁸¹

A. The Federal Regulatory Framework

SIGECO and *PSI* are part of a federal initiative aimed at enforcing the New Source Review ("NSR") and Prevention of Significant Deterioration ("PSD") provisions of the CAA. The initiative targets principally midwestern coal-burning utilities. The CAA Amendments of 1970 required the U.S. Environmental Protection Agency ("USEPA") to establish National Ambient Air Quality Standards ("NAAQS") for listed pollutants that are found in ambient air as a result of stationary or mobile sources and that "cause or contribute to air pollution which may reasonably be anticipated to endanger public health or welfare."⁸² So far, USEPA has identified six such pollutants, referred to as "criteria" pollutants: sulfur dioxide, particulate matter, carbon monoxide, ozone, nitrogen dioxide, and lead.⁸³ The 1977 Amendments to the CAA established the NSR/PSD program.⁸⁴ The program aims to spur achievement of the NAAQS in non-attainment areas and to prevent significant deterioration in attainment areas.⁸⁵ The program applies to new major stationary sources and major modifications to existing major sources.⁸⁶ The NSR/PSD program only applies to the criteria pollutants.⁸⁷

A modification triggers PSD/NSR review if the modified source is a major source and if the net emission increase is significant.⁸⁸ Modification to a minor source triggers the program if the modification itself would constitute a major stationary source.⁸⁹ A physical change in or change in the method of operation

80. *United States v. S. Ind. Gas & Elec. Co.*, No. IP99-1692-C-M/F.

81. No. IP99-1693-C-M/S.

82. 42 U.S.C. § 7408(a)(ii)(A) (1998).

83. 40 C.F.R. §§ 50.4-50.12 (2003).

84. 42 U.S.C. §§ 7501-7515; 7470-7492.

85. *Id.*

86. *Id.*

87. *Id.*

88. 40 C.F.R. § 52.21(a)(2) (2003).

89. *Id.*

of a stationary source triggers PSD/NSR review if there is a significant net increase in emissions.⁹⁰ The regulations do not define what constitutes a physical change or change in the method of operation. They do, however, exclude certain categories of activities that are not a physical or operational change. These include modifications that constitute “routine maintenance, repair or replacement” (“RMRR”).⁹¹

PSD permits require that Best Available Control Technology (“BACT”) be installed.⁹² The analysis that must be performed requires extensive and frequently expensive testing and analysis. The PSD permit application generally requires a BACT demonstration that follows USEPA’s “top-down” BACT approach. A demonstration is required if installation of the most effective available control technology is not feasible for a particular project. Energy, economic or environmental reasons may be considered. New or modified sources in non-attainment areas require that lowest achievable emissions rate (“LAER”) technology be installed.⁹³ A LAER determination generally may not consider energy, economic or environmental reasons for non-availability. Emission offset requirements also are imposed in non-attainment areas. Both BACT and LAER determinations are reviewed on a case by case basis. EPA issued “guidance” in 1998 that articulated EPA’s position that the BACT/LAER determination is made as of the time of application rather than the time when the modifications at issue were performed.

USEPA proposed new NSR rules on July 23, 1996. Numerous drafts and records of comments followed. USEPA published the new NSR regulations on December 31, 2002. The new rules became effective on March 3, 2003. The new rules aim to streamline the NSR program which generally is acknowledged to be unwieldy and overly complex. The new rules only apply to modifications at existing sources.

One of the most significant aspects of the new rules is their modification of the options available for calculation of whether a project will result in significantly increased emissions. For NSR to apply under the new regulations, major sources must undergo a major modification.⁹⁴ “[A] project is a major modification for a regulated NSR pollutant if it causes two types of emissions increases—a significant emissions increase . . . and a significant net emissions increase”⁹⁵ There are four ways to determine whether a “significant emissions increase” has occurred for modified units: (1) the actual-to-projected-actual test, (2) the actual-to-potential test, (3) the Clean Units Test, and (4) the hybrid test.⁹⁶

The new rules allow the owner of a facility to establish an emissions cap,

90. *Id.*

91. *Id.* § 52.21(b)(2)(iii)(a).

92. 42 U.S.C. § 7475 (1977).

93. 42 U.S.C. § 7503 (1990).

94. 40 C.F.R. § 52.21(a)(2)(ii).

95. *Id.* § 52.21(a)(iv)(a).

96. *See id.* §§ 52.21(a)(iv)(b)-(f), (b)(41)(ii)(d).

called a Plantwide Applicability Limit ("PAL").⁹⁷ Once the PAL is established, new or modified units within the facility trigger NSR only if the facility's actual emissions exceed the PAL.⁹⁸ The new rules establish a clean unit designation for units that have installed technology that is equivalent to BACT or LAER.⁹⁹ Modification to these clean units does not require approval for a period of ten years unless a permit condition must be changed.¹⁰⁰ The new rules also exempt from NSR certain types of pollution control projects that are presumed to be beneficial to the environment.¹⁰¹

USEPA also published a RMRR rule that became effective on December 31, 2002.¹⁰² Under the new rule, a project is RMRR if it meets three criteria: (1) the replacement component must be identical to or must serve the same purpose of the replaced component; (2) the fixed capital cost of the new component plus certain ancillary costs must not exceed twenty percent of the current replacement value of the replaced component; and (3) the replaced component must not alter the basic design parameters of the replaced unit or cause the replaced unit to exceed any enforceable emission or operational limitation.¹⁰³

These new rules have been challenged in court and their effectiveness is stayed until the challenges are complete. While EPA asserts that the new rules do not apply to the existing litigations, if they did virtually all of EPA's claims would have to be withdrawn.

B. *The SIGECO Case*

Judge McKinney issued six published opinions in *SIGECO*.¹⁰⁴ In his July 18, 2002 decision, Judge McKinney examined the issue of whether a showing that there was no actual emission increase after a project is completed exempts the project from the PSD preconstruction requirement and denied SIGECO's motion for summary judgment on this defense. The government argued that it would encourage a wait and see approach by regulated sources if pre-construction review could be avoided by construction that does not result in an actual emissions increase.¹⁰⁵ Relying on the Environmental Appeals Board's decision in *In re Tennessee Valley Authority*,¹⁰⁶ Judge McKinney concluded that Congress intended NSR to require a pre-construction rather than a post-construction review

97. 40 C.F.R. § 52.166 (1998); 40 C.F.R. § 52.21 (2003).

98. *Id.*

99. *Id.*

100. *Id.*

101. *Id.*

102. 40 C.F.R. § 51.165 (2002).

103. *Id.*

104. *United States v. S. Ind. Gas & Elec. Co.*, No. IP99-1692-C-M/F, 2002 WL 1629817 (S.D. Ind. July 18, 2002).

105. *Id.* at *2.

106. No. OAA-2000-04-008, 2000 WL 1358648 (E.A.B. Sept. 15, 2000).

process.¹⁰⁷

In a July 26, 2002 decision, Judge McKinney examined SIGECO's claim that some of the government's claims for civil penalties are barred by the applicable statute of limitations.¹⁰⁸ The statute is 28 U.S.C.A. § 2462: "Except as otherwise provided by an Act of Congress, an action, suit or proceeding for the enforcement of any civil fine, penalty or forfeiture, pecuniary or otherwise, shall not be entertained unless commenced within five years from the date when the claim first accrued"¹⁰⁹ The court entered summary judgment in favor of SIGECO on this issue. Judge McKinney adopted the majority position across the country by holding that an alleged failure to obtain a CAA pre-construction permit is a one-time violation that does not continue through time. The court noted that the government had alleged violations of the Clean Air Act's "preconstruction permit requirements contained in 42 U.S.C. § 7475 rather than a violation of the Act's operating permit requirements as set forth in 42 U.S.C. § 7661."¹¹⁰ Judge McKinney held that a PSD violation "occurs when construction is commenced, but does not continue on past the date when construction is completed."¹¹¹

In another July 26, 2002 decision, Judge McKinney considered whether the Indiana Department of Environmental Management's ("IDEM") determination that a particular project did not trigger PSD permit requirements affected the federal government's ability to allege that the project did trigger PSD.¹¹² SIGECO had approached IDEM regarding the project and had made a formal written request for a determination that the project was exempt pursuant to the RMRR exception. Shortly after the project was completed, IDEM formally determined that the project did not trigger PSD; a determination that has not been withdrawn. Judge McKinney determined, however, that IDEM's determination did not bind the federal government.¹¹³ The court reasoned that the plain language of Section 7413 indicates that the federal government's claim against SIGECO was not precluded by IDEM's determination.¹¹⁴ The court noted, however, that "equitable considerations may play an important part in the consideration of any remedy."¹¹⁵

In an October 24, 2002 decision, Judge McKinney examined the issue of whether the government's claims were barred by the Congressional Review of Agency Rule Making Act ("CRA")¹¹⁶ by establishing a new agency rule without submitting a report to Congress about the rule.¹¹⁷ SIGECO designated testimony

107. *Id.* at *3.

108. *SIGECO*, 2002 WL 1760725 (S.D. Ind. July 26, 2002).

109. 28 U.S.C.A. § 2462 (West 2004).

110. *SIGECO*, 2002 WL 1760725, at *5.

111. *Id.*

112. *SIGECO*, 2002 WL 1760699 (S.D. Ind. July 26, 2002).

113. *Id.* at *6.

114. *Id.* at *4.

115. *Id.*

116. 5 U.S.C. § 801 (West 2004).

117. *SIGECO*, 2002 WL 31427523 (S.D. Ind. Oct. 24, 2002).

by former government officials and consultants to support its position that the USEPA in its late 1990's "enforcement initiative" that culminated in these NSR lawsuits had changed its policy regarding application of the NSR rules, in particular the RMRR exception, to utility sources.¹¹⁸ Initially, the court disagreed with two other federal district court decisions by finding that the judicial review provisions of the CRA or the CAA did not bar SIGECO's motion for summary judgment on this issue. The court proceeded, however, to exclude the expert testimony that SIGECO had presented.¹¹⁹ The court relied, instead on the language of the statute and rules and on the Seventh Circuit's decision in *Wisconsin Electric Power Co. v. Reilly* ("WEPCO") and USEPA guidance prior to WEPCO.¹²⁰ In WEPCO the Seventh Circuit applied a fact-intensive test to determine whether the RMRR exception applied to each project at issue. The decision was preceded by an EPA memorandum by Don Clay (the "Clay Memorandum") that detailed USEPA's approach. Judge McKinney ruled, based on these considerations and the evidence presented, that USEPA's actions did not constitute a new rule subject to review under the CRA.¹²¹

In a February 13, 2003 decision, Judge McKinney examined the issues of whether the USEPA's interpretation of the RMRR exception was reasonable and whether SIGECO had fair notice of this interpretation.¹²² USEPA argued that the frequency factor in its analysis of whether a project is subject to the RMRR should be determined by looking at the history of the unit at issue.¹²³ SIGECO argued for an industry-wide analysis regarding the frequency of the particular type of project at issue. The court held that the EPA's interpretation was reasonable and would receive deference.¹²⁴ Judge McKinney also held that the RMRR exemption was sufficiently ambiguous to require fair notice to the regulated public of how the regulation would be interpreted.¹²⁵ The court held that the regulation itself was ambiguous, but that the 1988 memorandum by USEPA official Don Clay regarding projects that were later adjudicated in the WEPCO case, followed by the Seventh Circuit's WEPCO decision, gave the utility industry notice of USEPA's position on application of the RMRR exception. The court examined whether IDEM's 1998 determination that one of the projects at issue did not trigger PSD constituted contrary notice. Judge McKinney concluded that SIGECO could not rely on the 1998 determination as notice because it was issued after construction of the project at issue was completed.¹²⁶

In a February 18, 2003 decision, Judge McKinney held that certain of

118. *Id.* at *1.

119. *Id.* at *7.

120. 893 F.2d 901 (7th Cir. 1990).

121. *SIGECO*, 2002 WL 31427523, at *8.

122. *SIGECO*, 245 F. Supp. 2d 994 (S.D. Ind. 2003).

123. *Id.* at 1008.

124. *Id.* at 1010.

125. *Id.* at 1011.

126. *Id.* at 1023.

SIGECO's related defenses had become moot due to the court's various rulings in the case.¹²⁷ On SIGECO's equitable defense of laches, the court held that SIGECO was not prejudiced by any delay on the part of the government.¹²⁸ On SIGECO's claim of waiver, the court held that SIGECO had not demonstrated that the government had intended to relinquish its right to pursue its CAA claims.¹²⁹ The court also granted summary judgment to the government regarding SIGECO's remaining defenses that pertain to the alleged new regulatory interpretation by USEPA, including violation of the Administrative Procedures Act, ultra vires administrative action, retroactive rulemaking, violation of the Federal Register Act, substantive due process, and arbitrary and capricious administrative action.¹³⁰ The court again noted, however, that evidence such as IDEM's determination that SIGECO's 1997 project did not trigger PSD would bear on any penalty imposed on SIGECO.¹³¹

In an April 11, 2003 decision, Judge McKinney ruled that a census commissioned by several utilities, including SIGECO, and governmental entities was not admissible as an objective study of maintenance practices throughout the utility industry.¹³² The court reasoned that the census was not reliable because the census takers and respondents knew that the questionnaire was circulated for purposes of developing a defense in *SIGECO* and related cases, and because the census sought information about activities that might have taken place up to sixty years ago.¹³³

On June 6, 2003, the U.S. Department of Justice ("DOJ") announced its settlement with SIGECO. The settlement required SIGECO to install technology to reduce particulate matter emissions and continuous operation of a control device to remove nitrogen oxide emissions. By 2006, SIGECO will upgrade its oldest unit by repowering it with natural gas, installing state of the art emission controls, or permanently retiring the unit. These measures are expected to cost approximately \$30 million. SIGECO will pay a civil penalty of \$600,000 and will spend at least \$2.5 million to install and operate technology to reduce emissions of sulfuric acid from SIGECO's Culley plant in Newburgh, Indiana.¹³⁴

C. Other Recent U.S. District Court Decisions on NSR/PSD Enforcement

*United States v. Duke Energy Corp.*¹³⁵ and *United States v. Ohio Edison*

127. 2003 WL 446280, at *2 (S.D. Ind. Feb. 18, 2003).

128. *Id.* at *4.

129. *Id.*

130. *Id.* at *5.

131. *Id.* at *5-6.

132. *United States v. U.S. Ind. Gas & Elec. Co.*, 258 F. Supp. 2d 884 (S.D. Ind. 2003).

133. *Id.* at 895.

134. Southern Indiana Gas and Electric Company (SIGECO) F.B. Culley Plant Clean Air Act Settlement (June 6, 2003), at <http://www.epa.gov/compliance/resources/cases/civil/caa/sigecofb.html>.

135. 278 F. Supp. 2d 619 (M.D.N.C. 2003).

*Co.*¹³⁶ contain rulings that both complement and conflict with the *SIGECO* rulings. Contrary to *SIGECO*, *Duke Energy* holds that the test for determining whether a modification was routine maintenance, repair, or replacement was whether the modification was routine in the industry rather than at a particular generating unit.¹³⁷ *Duke Energy* also holds, contrary to *SIGECO*, that a utility's failure to obtain a pre-construction permit before making the modification was a continuing violation for statute of limitations purposes.¹³⁸ *Ohio Edison* held that the plain language of the CAA, read together with the routine maintenance exemption, put the industry on notice that the exemption would be narrowly construed by government.¹³⁹ Judge McKinney reached a different conclusion on the character of the regulation, but the same result in *SIGECO*.

The diversity of district court rulings, on top of the tremendous complexity of the underlying facts, makes it difficult to predict how appellate courts will resolve the governing issues. This is particularly true given government ambivalence in the form of new regulations that remove many of the projects at issue from the reach of the NSR/PSD program. The uncertainty imposed on utilities and other industries by these divergent rulings underscores the appeal of fair and consistent forward-looking regulation by clearly worded statutes and rules rather than retroactive litigation that in many cases involves projects completed decades ago, in some cases by entirely different entities than the present target of NSR/PSD enforcement.

A decision from the Western District of New York highlights the implications of such ownership changes. In *New York v. Niagara Mohawk Power Corp.*,¹⁴⁰ the court granted the defendants' motion to dismiss because those defendants neither owned nor operated the facilities at issue at the time the modifications that allegedly violated PSD took place. The court examined the pre-construction requirements of the federal PSD program and determined that "[p]reconstruction obligations are imposed only upon the person who actually seeks to construct or modify a facility within the meaning of the Act."¹⁴¹ The court stated that:

It is simply counterintuitive to construe the Clean Air Act in such way as to impose liability for failure to follow the Act's pre-construction requirements on a person for whom compliance would have been impossible. The State cites no cases standing for this proposition, and this Court has been unable to find any.¹⁴²

The court concluded that even if the facilities were unlawfully modified, third-party after-the-fact purchasers were not liable for the pre-construction violations.

136. 276 F. Supp. 2d, 829 (S.D. Ohio 2003).

137. *Duke Energy*, 278 F. Supp. 2d at 638.

138. *Id.* at 652.

139. *Ohio Edison*, 276 F. Supp. 2d at 888.

140. 263 F. Supp. 2d 650 (W.D.N.Y. 2003).

141. *Id.* at 668-69.

142. *Id.* at 669.

D. The Eleventh Circuit's TVA Decision

The Eleventh Circuit Court of Appeals recently evaluated and set aside an administrative decision critical to the DOJ's NSR enforcement initiative against utilities.¹⁴³ As part of its NSR enforcement initiative against utilities, USEPA issued an administrative compliance order ("ACO") to the Tennessee Valley Authority ("TVA") requiring the TVA to undertake costly and burdensome compliance initiatives. USEPA delegated the task of evaluating TVA's legal challenge of the ACO to USEPA's Environmental Appeals Board ("EAB"). The EAB issued an order (the "EAB order") concluding that the projects undertaken by the TVA had violated NSR, as USEPA had alleged.¹⁴⁴

In federal court, the TVA challenged the EAB order as unlawful and the product of arbitrary and capricious decision-making pursuant to the federal Administrative Procedure Act ("APA").¹⁴⁵ The Eleventh Circuit held that it lacked jurisdiction to review the EAB Order because the ACO was not a "final" agency action.¹⁴⁶ The court determined that USEPA "must prove the existence of a CAA violation in district court; until then, TVA is free to ignore the ACO without risking the imposition of penalties for noncompliance with its terms."¹⁴⁷ Central to the Eleventh Circuit's ruling was its conclusion that the statutory scheme that resulted in issuance of the ACO is "unconstitutional to the extent that severe civil and criminal penalties can be imposed for non-compliance with the terms of an ACO."¹⁴⁸

The Eleventh Circuit first discussed USEPA's enforcement options when it found that a regulated party had engaged in unlawful activity. The USEPA can: (1) request that the Attorney General commence a criminal prosecution under 42 U.S.C. § 7413(a)(3); (2) file suit in federal court and seek injunction relief and civil penalties under 42 U.S.C. § 7413(a)(1)(C) or (a)(3)(C); (3) after a final adjudication consistent with the APA and 40 C.F.R. § 22, assess civil penalties pursuant to 42 U.S.C. § 7413(d); or (4) issue an ACO directing the regulated party to comply with various requirements pursuant to 42 U.S.C. § 7413(a)(1)(A), (a)(2)(A), (a)(3)(B) or (a)(4).¹⁴⁹ Under 42 U.S.C. § 7413(a)(1)(4), an ACO must meet three conditions: (1) it must be based upon "any information available to the Administrator"; (2) it must be issued within thirty days after the issuance of a Notice of Violation; and (3) the regulated party must be given an "opportunity to confer" with the USEPA.¹⁵⁰ The court noted that "[t]he problem with ACOs stems from their injunction-like status coupled with the fact that they are issued without an adjudication or meaningful judicial

143. *Tenn. Valley Auth. v. Whitman*, 336 F.3d 1236 (11th Cir. 2003).

144. *Id.* at 1239.

145. *Id.*

146. *Id.*

147. *Id.* at 1239-40.

148. *Id.* at 1239.

149. *Id.* at 1241.

150. *Id.*

review.”¹⁵¹

The court then reviewed the USEPA’s case against the TVA. The court noted that between 1982 and 1996, TVA implemented projects involving replacement of various boiler components at its coal-fired plants.¹⁵² In 1999, the USEPA concluded that the projects did not constitute “routine maintenance” activities, and hence the projects triggered NSR requirements.¹⁵³ On November 3, 1999 the USEPA issued its first ACO to the TVA.¹⁵⁴ The ACO required the TVA to identify modifications undertaken without NSR permits, to apply for the permits, and to enter into a compliance agreement with the USEPA.¹⁵⁵ Negotiations took place that led to six amendments to the ACO.¹⁵⁶ TVA held to its position that its projects did not trigger NSR. The USEPA then attempted to adjudicate the issue of whether TVA had violated the CAA by asking the EAB to reconsider the sixth ACO.¹⁵⁷ The EAB “crafted a reconsideration procedure which, to say the least, lacked the virtues of most agency adjudication.”¹⁵⁸ The ALJ was instructed by the EAB not to make findings of fact and conclusions of law.¹⁵⁹ The EAB acted both as adjudicator and as USEPA’s delegatee.¹⁶⁰ The TVA was not entitled to full discovery.¹⁶¹ Testimony at the hearing was limited at USEPA’s request. The proceeding was rushed, limiting the time for TVA to prepare its defense. USEPA and the EAB “manufactured the procedures they employed on the fly, entirely ignoring the concept of the rule of law.”¹⁶² Ultimately, the EAB affirmed most of the sixth amended ACO.¹⁶³

The next part of *TVA v. Whitman* reviewed the “finality doctrine.” Citing *FTC v. Standard Oil of California*,¹⁶⁴ the court identified five factors for determining finality:

- (1) whether the agency action constitutes the agency’s definitive position;
- (2) whether the action has the status of law or affects the legal rights and obligations of the parties;
- (3) whether the action will have an immediate impact on the daily operations of the regulated party;
- (4) whether pure questions of law are involved; and
- (5) whether pre-

151. *Id.*

152. *Id.* at 1244.

153. *Id.*

154. *Id.*

155. *Id.*

156. *Id.*

157. *Id.* at 1245.

158. *Id.*

159. *Id.* at 1246.

160. *Id.*

161. *Id.*

162. *Id.*

163. *Id.*

164. 449 U.S. 232, 239-43 (1980).

enforcement review will be efficient.¹⁶⁵

The court noted that Congress may not have intended ACOs to have the status of law.¹⁶⁶ The court noted that 42 U.S.C. § 7603 gives the USEPA emergency powers when a pollution source presents an imminent and substantial endangerment to public health, welfare, or the environment.¹⁶⁷ An order issued pursuant to this provision attains an injunction-like status only for an extremely short time period.¹⁶⁸ An order issued pursuant to section 7413, on the other hand, provides that the defendant must have an “opportunity to confer” with the USEPA.¹⁶⁹ The Eleventh Circuit concluded that Congress intended orders issued under section 7413 to be “complaint-like devices used to avoid litigation.”¹⁷⁰ The court further noted that judicial review of such orders is not available because ACOs are issued without a record.¹⁷¹

Based on this analysis, the Eleventh Circuit concluded that an ACO that has the status of law violates the Due Process Clause of the Fifth Amendment.¹⁷² Under the CAA, the findings in an ACO can be based on “any information available.” If ignored, an ACO leads automatically to the imposition of severe civil penalties and possibly imprisonment. On appeal, the reviewing court could only review whether the ACO had been validly issued, i.e., whether the issuance of the ACO was based on “any information.”¹⁷³ There would be no judicial review of whether the conduct underlying issuance of the ACO actually took place and whether the alleged conduct was a CAA violation.¹⁷⁴ The Eleventh Circuit stated that the constitutional problem cannot be cured by USEPA’s submission to a voluntary adjudication prior to issuance of an ACO.¹⁷⁵ This would “delegate judicial power to a non-Article III tribunal.”¹⁷⁶ Hence, the Eleventh Circuit stated that “[t]he Clean Air Act is unconstitutional to the extent that mere noncompliance with the terms of an ACO can be the sole basis for the imposition of severe civil and criminal penalties.”¹⁷⁷ Because USEPA’s ACOs lacked the force of law, they did not constitute a final agency action subject to judicial review under the APA.¹⁷⁸

The *Whitman* decision did far more than dismiss the TVA’s challenge to a series of ACOs alleging violations of NSR/PSD requirements. The Eleventh

165. *Whitman*, 336 F.3d at 1248.

166. *Id.*

167. *Id.* at 1249.

168. *Id.*

169. 42 U.S.C. § 7413(a)(4) (West 2004).

170. *Whitman*, 336 F.3d at 1250.

171. *Id.* at 1251.

172. *Id.* at 1258.

173. *Id.*

174. *Id.*

175. *Id.* at 1259.

176. *Id.*

177. *Id.* at 1260.

178. *Id.*

Circuit's jurisdictional ruling had the effect of invalidating a pro-government decision frequently cited by government against utilities in NSR litigation. Several courts, including the Southern District of Indiana in *SIGECO*, had applied the now-invalidated EAB decision against utilities in NSR disputes. State and federal environmental agencies must evaluate the constitutionality of their enforcement mechanisms and approaches in light of the *Whitman* decision. The Eleventh Circuit's rejection of USEPA's willingness to make up procedures as it went along, to the detriment of a regulated entity, should guide federal and state agencies' efforts to identify and prosecute alleged PSD/NSR violations.

E. PSD/NSR Enforcement by IDEM

IDEM also has initiated enforcement actions that addressed alleged PSD/NSR violations. States may include PSD programs in their State Implementation Plans ("SIP").¹⁷⁹ If a state does not have an EPA-approved PSD program as part of its SIP, then it is delegated the authority to implement and enforce the federal program contained in 40 C.F.R. § 52.21. IDEM has been delegated the authority to implement the federal PSD program since September 30, 1980.¹⁸⁰ On March 3, 2003, the EPA published a conditional approval of Indiana's revised SIP which included Indiana's PSD program contained in title 326, rule 1.1 of the Indiana Administrative Code, making the SIP revision effective as of April 3, 2003.¹⁸¹

IDEM's NSR enforcements have been challenged. One challenge resulted in a trial court decision that invalidated IDEM's demand that a northern Indiana foundry apply for and obtain PSD permits for projects implemented in the mid-1980's by a prior owner.¹⁸² IDEM's Order, dated February 17, 2003 ("2003 Order"), purported to require a foundry owned by Dalton Corporation ("Dalton") to seek pre-construction permits under the CAA's PSD rules for projects implemented in 1984-1985 by a prior owner of the foundry. IDEM's objective was to force Dalton to install emission control equipment that would meet the CAA's BACT standards. The 1984-1985 projects were implemented by the prior owner to make the foundry more economically viable and safer to operate. The projects included replacement of portions of the cupola charge handling system, the raising of the cupola shell stack height, and replacement of two molding lines by a single new molding line.

Dalton petitioned for administrative review but filed a declaratory judgment action in the Marion County Superior Court. IDEM sought to dismiss the court proceeding on the grounds that the dispute must first be adjudicated before the OEA under the "exhaustion of administrative remedies" doctrine. Dalton resisted, citing a recent Indiana Supreme Court decision, *Indiana Department of*

179. 40 C.F.R. § 51.166.

180. See 68 FR 1970 (January 15, 2003) for a history of IDEM's PSD program.

181. IND. ADMIN. CODE tit. 326, r. 1.1 (2003).

182. *Dalton Corp. v. Ind. Dep't of Env'tl. Mgmt.*, No. 49D06-0307-PL-001204 (Marion Super. Ct. Nov. 20, 2003).

Environmental Management v. Twin Eagle LLC,¹⁸³ which held that exhaustion of administrative remedies was not required because the issues raised were issues of law.¹⁸⁴ The Marion County Superior Court rejected IDEM's exhaustion claim and held it could rule on the legality and enforceability of IDEM's February 17, 2003 order.¹⁸⁵

In granting Dalton's motion for summary judgment, the Marion Superior Court cited six reasons why the 2003 order could not be enforced. First, the projects at issue, and the specific issue of whether the projects triggered PSD requirements, had been raised in a prior lawsuit that involved IDEM and the former owner that implemented the projects in 1984-1985.¹⁸⁶ In May 1986 a citizen group gave notice to IDEM of its intent to file a lawsuit against the prior owner and IDEM pursuant to the citizen suit provisions of the CAA. The citizen suit was filed in 1987 and resolved and dismissed with prejudice in March 1990 without action on the PSD issue. However, the determination of whether PSD requirements applied to the 1984-1985 projects was at issue, and in the three years the matter was pending could have been determined in that litigation. The Marion County Superior Court held that the claim preclusion branch of the doctrine of *res judicata* barred the 2003 order as a matter of law.¹⁸⁷

The Marion County Superior Court also held that IDEM's order was barred by Indiana's statute of limitations for environmental enforcement actions.¹⁸⁸ Indiana statutes require that IDEM seek enforcement of environmental statutes and regulations within three years of the time that IDEM discovers a violation.¹⁸⁹ IDEM argued that its 2003 order was a "permitting" rather than an "enforcement" action, and thus was not subject to the three year limitation and also that Dalton's failure to obtain a PSD permit was a "continuing" violation. The Marion Superior Court rejected both of these arguments. It held that the substance of the action rather than IDEM's label determined the applicable statute of limitations.¹⁹⁰ Citing *SIGECO*,¹⁹¹ the court also held that the violation of a PSD construction permit requirement does not continue past the completion date of construction.

The court's third reason that the February 17, 2003 order could not be enforced was that it was not directed to the entity that actually implemented the projects at issue.¹⁹² The Marion County Superior Court cited the New York District Court decision, discussed above, that also concluded, based on statutory interpretation, that third party after-the-fact purchasers are not liable for alleged

183. 798 N.E.2d 839 (Ind. 2003).

184. *Id.* at 844.

185. *Dalton Corp.*, slip. op. at 6.

186. *Id.* at 2-3.

187. *Id.*

188. *Id.* at 8.

189. IND. CODE § 13-14-6-2 (2003).

190. *Dalton Corp.*, slip op. at 10.

191. *Id.* (citing *SIGECO*, 2002 WL 1760699 (S.D. Ind. July 26, 2002)).

192. *Id.* at 11.

pre-construction violations under the CAA.¹⁹³

The equitable doctrines of laches and estoppel also were held to bar the 2003 order. Laches applies when there is inexcusable delay in asserting a right, an implied waiver from knowing acquiescence in existing conditions and prejudice due to the delay.¹⁹⁴ Estoppel requires a representation or concealment of material facts, made by a party with knowledge of the facts to a party ignorant of the facts, and detrimental reliance by the receiving party.¹⁹⁵ The Marion County Court held that the elements of both doctrines were met based on the undisputed facts.¹⁹⁶

The final reason why the 2003 Order could not be enforced is that the Order sought to force Dalton to perform an impossible task.¹⁹⁷ Dalton submitted expert testimony that detailed the unreliability of existing data and the impossibility of determining or even reliably estimating base emissions or the net emission change needed to determine whether or not the 1984-1985 projects triggered PSD requirements.¹⁹⁸ IDEM did not submit counter-evidence on this point. Citing an Indiana decision excusing compliance with a regulatory requirement made impossible by the death of the claimant, *Pedigo v. Miller*,¹⁹⁹ the court held that Dalton was excused from compliance with the February 17, 2003 order on impossibility grounds.²⁰⁰

F. Future Indiana NSR/PSD Litigation

Further heated debate and litigation over alleged PSD/NSR violations are a certainty at both the federal and state levels. Numerous cases pend at both appellate and state levels. Many fundamental issues remain unresolved. One such issue is whether the five-year limitations period that applies to federal PSD/NSR claims applies when the federal government seeks equitable relief as opposed to civil penalties. The majority position imposes the five-year limitations period to claims for civil penalties. The “continuing violation” theory does not rejuvenate the federal government’s claims regarding projects that took place outside of the limitations period. However, equitable relief, in particular the imposition of modern BACT on old projects, has the potential to impose tremendous costs on defendant facilities. The federal government will argue that statutory limitations periods do not apply to the equitable claims. However, USEPA’s and IDEM’s stance that they may impose modern BACT on projects completed long ago is punitive or compensatory rather than equitable in nature. The fundamental policy reasons for barring stale claims, including the inevitable

193. *Id.* (citing *New York v. Niagara Mohawk*, 263 F. Supp. 2d 650 (W.D.N.Y. 2003)).

194. *Bd. of Zoning Appeals v. Beta Tau Housing Corp.*, N.E.2d 780, 782 (Ind. Ct. App. 1986).

195. *Advisory Bd. of Zoning Appeals for the City of Hammond v. Found. for Comprehensive Mental Health Inc.*, 497 N.E.2d 1089, 1092 (Ind. Ct. App. 1986).

196. *Dalton Corp.*, slip op. at 12-13.

197. *Id.* at 14.

198. *Id.*

199. 369 N.E.2d 1100 (Ind. App. 1977).

200. *Dalton Corp.*, slip op. at 14.

loss of evidence needed to prove or disprove the claim, and in environmental cases the regulated public's substantial need for stability and predictability in the way government interprets and applies environmental laws, apply equally to NSR/PSD claims that seek equitable relief as opposed to civil penalties. The impact of USEPA's new regulations on pending NSR/PSD claims remains uncertain and likely will be explored by the litigants in pending and new NSR/PSD cases.

III. OTHER DEVELOPMENTS IN INDIANA ENVIRONMENTAL LAW

A. Development Activities in Isolated Wetlands

A tempest of controversy regarding regulation of development activities in isolated wetlands followed the United States Supreme Court's decision in *Solid Waste Agency of Northern Cook County v. U.S. Army Corps. of Engineers*.²⁰¹ Moreover, Indiana developers are part of the fray.²⁰² *Twin Eagle* reversed and remanded the trial court's entry of summary judgment in favor of a developer as to whether or not the Indiana Department of Environmental Management ("IDEM") has statutory authority to regulate isolated wetlands.

Wetlands are regulated by the federal Clean Water Act ("CWA") which prohibits "the discharge of any pollutant" into "waters of the United States" without a permit.²⁰³ Such permits are issued under the National Pollutant Discharge Elimination System ("NPDES"). Section 404 of the CWA provides for issuance of permits for dredge and fill activities in wetlands under a program ("Section 404 Program") administered by the U.S. Army Corps of Engineers. Although Indiana administers its own NPDES program, it has not sought permission to issue wetlands permits under the section 404 Program.

SWANCC held that "waters are 'waters of the United States' for purposes of the CWA only if they are either navigable or tributaries of or wetlands adjacent to navigable waters."²⁰⁴ Isolated wetlands fall outside of this definition. Because *SWANCC* removed isolated wetlands from the reach of the section 404 Program, IDEM attempted to fill the regulatory gap by "stating its intention, until new rules were approved, to regulate" isolated wetlands "through an 'interim regulatory process' whereby it would apply its state NPDES permitting process to applications for permits for dredged and fill material."²⁰⁵ This process was announced by press release, with no promulgation of a rule and with no articulation of any standards under which a permit would be issued. *Twin Eagle* sought and obtained a declaratory judgment to prevent IDEM from enforcing state environmental laws against a proposed project calling for fill activities in

201. 531 U.S. 159 (2001) ("*SWANCC*").

202. See *Ind. Dep't of Evtl. Mgmt. v. Twin Eagle LLC*, 798 N.E.2d 839 (Ind. 2003).

203. 33 U.S.C. § 1342 (2003).

204. *Twin Eagle*, 798 N.E.2d at 842 (citing *SWANCC*, 531 U.S. at 171, 174).

205. *Id.*

certain isolated wetlands on Twin Eagle's land.²⁰⁶

The Indiana Supreme Court first evaluated IDEM's argument that Twin Eagle's claims could not be adjudicated in court because IDEM must first resolve whether the particular twenty-one acres of isolated wetlands involved are subject to regulation and because the developer had not exhausted its administrative remedies.²⁰⁷ This issue is of crucial significance to members of the regulated community. If they must submit to unlawful regulatory commands in order to apply for or obtain permits, then go through an application process and an administrative appeal only to then obtain a court determination that the entire exercise was unlawful, it will substantially compromise a citizen's ability to resist unlawful government demands.

The court first affirmed that the Declaratory Judgments Act is to be given a liberal construction, and may address an issue only when the "ripening seeds of a controversy" are present.²⁰⁸ It recognized the utility of prompt adjudication of a challenge to the validity of a regulatory process that, if it is found to be illegal, can and should be avoided altogether.²⁰⁹

The court also affirmed the exception to the exhaustion of administrative remedies for purely legal issues.²¹⁰ The capacity to make such a challenge is a crucial check on a government's over-zealous expansion of its power. Purely legal questions also do not require application of agency expertise or a developed administrative record and actually can save time and money both for citizens and agencies.²¹¹

The supreme court held, however, that IDEM has statutory authority to regulate isolated wetlands pursuant to laws enacted prior to the enactment of the federal CWA in 1972.²¹² The court did not accept the developer's argument that IDEM's statutory authority to adopt rules necessary to implement the CWA²¹³ was a "jurisdictional confinement of the waters to be regulated to those subject to the CWA."²¹⁴ The court cited various statutes that give IDEM general authority to protect the environment and to prevent pollution.²¹⁵ None of these authorize the state to require an NPDES permit for an isolated non-federal wetland, but the court held that general authority was sufficient to support IDEM's actions.

The next question addressed was whether the isolated ponds at issue fit Indiana's statutory definition of "waters." The definition excluded "private ponds" from regulation. The supreme court agreed with Twin Eagle's argument

206. *Id.*

207. *Id.* at 844.

208. *Id.* at 843.

209. *Id.* at 844.

210. *Id.*

211. *Id.*

212. *Id.* at 845.

213. IND. CODE § 13-18-3-2(a) (2003).

214. *Twin Eagle*, 798 N.E.2d at 846.

215. *Id.* (citing IND. CODE §§ 13-18-4-3, 13-18-3-1, 13-18-4-4).

that “private ponds” are bodies of water wholly on the property of one owner not connected with any public water.²¹⁶ The court held that the “private pond” and “wetland” determinations present fact issues that require administrative determination.²¹⁷ The court also noted that the term “wetlands” has no statutory definition, only a general regulatory definition under title 327, rule 6.1-2-62 of the Indiana Administrative Code, and that wetlands can “by their very nature vary in the amount of water they contain at a given time, and their boundaries can change depending on the season and the weather.”²¹⁸

The court said this “somewhat unsatisfactorily legal framework” provided Twin Eagle with two options: apply for a permit and challenge any adverse determination, or if it “is sufficiently confident,” do the project and fight any enforcement activity.²¹⁹ The court implicitly acknowledged the ambiguity of the statutory definition without any rules that would clearly inform a citizen if it needed a permit, but stated it saw “no alternative” since a recent statute prohibited IDEM from making new wetland rules before a legislative study commission reported.²²⁰

Finally, the Indiana Supreme Court accepted IDEM’s position that it can regulate isolated wetlands pursuant to an “interim process” rather than regulations promulgated pursuant to the Administrative Orders and Procedures Act (“AOPA”).²²¹ The court concluded no rulemaking was needed because IDEM already had a rule requiring an NPDES permit for “[a]ny discharge of pollutants into waters of the state.”²²² The court ignored (1) that an NPDES permit is not a creation of state law; it is a federal permit issued as to the Federal Clean Water Act waters, and (2) that IDEM had announced it was intending to promulgate new rules for isolated wetlands. If IDEM did not actually need to promulgate a new rule to regulate isolated wetlands, why did it announce this prospect or call its own authority “interim?” The only way the court could leave IDEM with a capacity to save wetlands which IDEM claims were at risk was to find IDEM already had a sufficient rule in place.

Twin Eagle retains viability for its procedural holdings, but the legislature has sapped its substantive sway. The legislature overruled Governor O’Bannon’s veto and enacted a new structure to clarify what isolated wetlands are subject to IDEM permit requirements.²²³ Wetlands are classified according to size, location, and ecological value, and only the most significant are required to seek IDEM permits. Private ponds (the vast majority of Twin Eagle’s wetlands) remain exempt from regulation.

216. *Id.* at 846-47.

217. *Id.* at 847.

218. *Id.*

219. *Id.*

220. *Id.*

221. IND. CODE § 4-22-2 (2003).

222. *Twin Eagle*, 798 N.E.2d at 848.

223. H.E.A. 1798, 113th Gen. Assem., 1st Reg. Sess. (Ind. 2004).

B. Standing in Administrative Proceedings

Under the AOPA, a person who is “aggrieved or adversely affected” by an agency’s action may seek administrative review.²²⁴ The Indiana Court of Appeals reviewed and clarified this standard, in an environmental context, in *Huffman v. IDEM*.²²⁵ The Indiana Supreme Court granted transfer, vacating the court of appeal’s decision on November 19, 2003. The case involved a property owner’s petition for administrative review of IDEM’s decision to renew a National Pollutant Discharge Elimination System (“NPDES”) issued pursuant to the CWA to Eli Lilly & Co. (“Lilly”).

The property owner alleged she was “aggrieved or adversely affected” because she is a citizen of Indiana whose family owned an interest in property located contiguous to Lilly’s facility.²²⁶ Lilly moved to dismiss the property owner’s petition under the judicial doctrine of standing, which requires a showing of direct injury. The OEA’s dismissal of the petition on this ground was affirmed by the trial court.

The court of appeals had reversed these rulings. It held that the judicial doctrine of standing was not the proper formulation of the AOPA’s “aggrieved or adversely affected” standard.²²⁷ The court held that to meet the standard a person must show “a substantial grievance, a denial of some personal, pecuniary or property right or the imposition . . . of a burden or obligation.”²²⁸ The court based this ruling on legislative intent as manifested by the “clear, unambiguous language of the AOPA.”²²⁹ The court rejected, however, the property owner’s additional claim that she qualified for administrative review as an “aggrieved or adversely affected” person merely by her status as a citizen of Indiana.²³⁰

The court went on to evaluate whether there was substantial evidence to support the OEA’s decision to deny the property owner’s standing to seek administrative review. The court’s reversal turned on a procedural point. Lilly filed its motion to dismiss the property owner’s petition based on Indiana Trial Rule 12(B)(1). The OEA considered materials outside of the property owner’s petition, converting the motion to dismiss into a motion for summary judgment to be adjudicated pursuant to Indiana Trial Rule 56. Lilly’s evidence in support of dismissal consisted of unsworn statements in its motion to dismiss. Lilly claimed, for example, that the property in which the property owner claimed an interest was located upstream from the point where Lilly’s facility discharged water pursuant to the NPDES permit.²³¹ The court of appeals held that such unsworn statements did not constitute substantial evidence sufficient to support

224. *Huffman v. Ind. Dep’t of Env’tl. Mgmt.*, 788 N.E.2d 505, 507 (Ind. Ct. App. 2003).

225. *Id.*

226. *Id.*

227. *Id.* at 508 (quoting *Bagnall v. Town of Beverly Shores*, 726 N.E.2d 782, 786 (Ind. 2000);

BLACK’S LAW DICTIONARY 43 (6th ed. 1991)).

228. *Id.*

229. *Id.*

230. *Id.*

231. *Id.* at 509.

dismissal of the property owner's petition under AOPA.²³² Although vacated, *Huffman* demonstrates the breadth of the "aggrieved or adversely affected" standard in Indiana administrative law and further emphasizes the importance of adherence to the Indiana Trial Rules in administrative proceedings.

C. Admissibility of Expert Testimony in Environmental Cases

Environmental cases, including toxic tort cases, frequently turn on highly technical issues that invite battles of the experts and challenges to expert opinions on reliability/admissibility grounds. Recent Indiana appellate decisions confirm that these battles rage on.

The dispute in *Armstrong v. Cerestar USA, Inc.*²³³ involved a truck driver's fall from the top of a tanker truck allegedly caused by his exposure to hydrogen sulfide fumes during a sludge removal operation. The plaintiff's expert opined that the plaintiff was exposed to a hazardous concentration of hydrogen sulfide gas while pumping the sludge into his tanker, that as a result of the exposure the plaintiff became disoriented and/or lost his balance and fell, and that under the Occupational Safety and Health Administration ("OSHA") guidelines, the sludge material being removed met the definition of hazardous material.²³⁴ The trial court found the opinions to be unreliable and inadmissible pursuant to Indiana Evidence Rule 702.²³⁵ The Indiana Court of Appeals identified relevant factors in the reliability/admissibility determination:

While there is no absolute test for determining when testimony is reliable, some factors are: 1) whether the theory or technique can be or has been empirically tested; 2) whether the theory or technique has been subjected to peer review and/or publication; 3) whether there is a known or potential rate of error, as well as the existence and maintenance of standards controlling the theory or technique's operation; 4) whether the theory or technique is generally accepted within the relevant scientific community.²³⁶

The court reviewed the expert's qualifications which included sixteen years with OSHA and his status as a Certified Safety Professional and Certified OSHA Instructor for General Industry and Construction.²³⁷ The expert admitted: (1) he did not conduct any of his own tests at the plant at issue; (2) he did not attempt to calculate the level of hydrogen sulfide to which the plaintiff might have been exposed; (3) no one could conduct such a test with any degree of confidence; (4) environmental conditions about which no data was available could have affected the level of hydrogen sulfide in the air at the time of the plaintiff's fall; (5) he did not know how tall the plaintiff was or what he had weighed at the time of the fall;

232. *Id.* at 511.

233. 775 N.E.2d 360 (Ind. Ct. App. 2002).

234. *Id.* at 366.

235. *Id.* at 368 (citing *Daubert v. Merrell Dow Pharm.*, 509 U.S. 579, 593-95 (1993)).

236. *Id.* at 366.

237. *Id.* at 367.

(6) he did not know the tanker make and model and had not examined the tanker; (7) he had never been involved in a similar case; and (8) that he had not read the plaintiff's deposition.²³⁸ Based on these admissions, the fact that the expert was not a licensed physician with training, knowledge and experience to make the proximate cause determination that the plaintiff became light-headed due to exposure to hydrogen sulfide gas and the expert's failure to exclude other possible causes of the plaintiff's fall, the court of appeals affirmed the trial court's ruling granting the defendant's motion to strike the expert's testimony.²³⁹

The dispute in *Outlaw v. Erbrich Products Co.*²⁴⁰ arose from injuries allegedly caused by workplace exposure to a toilet bowl cleaner. The case prompted two trips to the court of appeals, which remanded both times followed by a third trip to the court of appeals. Three experts sparred over whether the claimant's injury resulted from chemical exposure in the workplace as opposed to the claimant's many years of smoking cigarettes. The court of appeals ultimately affirmed the Indiana Worker's Compensation Board's ("Board") conclusion that the claimant was not entitled to benefits because her severe respiratory problems did not appear to be caused by the exposure to chemicals involved in the claimant's job of producing toilet bowl cleaner.²⁴¹ The pitfalls encountered by the claimant's experts are instructive.

The claimant worked on assembly lines producing and bottling products ranging from mustard and vinegar to bleach and toilet bowl cleaner.²⁴² The claimant mostly worked on the line that produced toilet bowl cleaner.²⁴³ She began medical treatment for severe respiratory problems in 1991 and eventually quit her job.²⁴⁴ She saw one Dr. Schaphorst who referred her to Dr. Garcia.²⁴⁵ Dr. Garcia examined the claimant and issued a report that linked the claimant's respiratory problems to toilet bowl cleaner that the claimant had indicated contained ammonia, hydrochloric acid, acetic acid, formaldehyde, and fabric softener. In Dr. Garcia's report, the claimant indicated that she had smoked one to two cigarettes per day for almost twenty years but had quit smoking in 1992. Dr. Garcia attributed the claimant's health problems to a combination of cigarette smoking and chemical exposure at work. He assigned her a partial impairment rating of forty percent.²⁴⁶

A third doctor, Dr. Waddell, entered the picture in 1994. Dr. Waddell reviewed the claimant's medical records. He noted that, although the claimant claimed to have quit smoking before her respiratory problems ensued, her tests (on December 17, 1992 and February 25, 1993) showed levels of

238. *Id.*

239. *Id.* at 368.

240. 777 N.E.2d 14 (Ind. Ct. App. 2002).

241. *Id.* at 31.

242. *Id.* at 17.

243. *Id.*

244. *Id.*

245. *Id.* at 17-18.

246. *Id.*

carboxyhemoglobin consistent with the consumption of two to three packs of cigarettes per day.²⁴⁷ Dr. Waddell challenged the claimant's assertion, reflected in Dr. Garcia's report, that the toilet bowl cleaner contained ammonia and formaldehyde. Apparently these two substances, as a matter of general chemistry, would have neutralized each other. When the dispute turned to whether exposure to hydrochloric acid fumes caused the claimant's lower respiratory distress, Dr. Waddell noted that the claimant did not have the upper respiratory injuries consistent with exposure to hydrochloric acid fumes. Dr. Waddell noted further that the concentration of hydrochloric acid in the toilet bowl cleaner was characterized by such low vapor pressure that a spill would not lead to vaporization of the acid.²⁴⁸ Dr. Duane Houser, an asthma expert, then joined the dispute in 1998. While generally supporting Dr. Garcia's opinions, Dr. Houser acknowledged that there was no clear connection between exposure to the constituents of the toilet bowl cleaner and the claimant's injuries.²⁴⁹ At the Board's hearing on this matter, a fellow employee testified that there were frequent spills of the toilet bowl cleaner and that the claimant had quit smoking in 1988.²⁵⁰

The Board issued two sets of findings that stated there was not a sufficient connection between any workplace chemical exposure and the claimant's injuries. The court of appeals, in reviewing the Board's findings, noted that a causation analysis based primarily on a temporal connection between exposure and alleged effect is insufficient:

[A]n expert's opinion is insufficient to establish causation when it is based only upon a temporal relationship between an event and a subsequent medical condition. In particular, when an expert witness testifies in a chemical exposure case that the exposure has caused a particular condition because the plaintiff was exposed and later experienced symptoms, without having analyzed the level, concentration or duration of the exposure to the chemicals in questions, and without sufficiently accounting for the possibility of alternative causes, the expert's opinion is insufficient to establish causation because it is based primarily on the existence of a temporal relationship between the exposure and the condition and amounts to subjective belief and unsupported speculation.²⁵¹

The court of appeals concluded, under the standard applicable to judicial review of Worker's Compensation Board determinations, that "the pertinent evidence in the record does not convince us that the evidence leads inescapably to the conclusion opposite to that reached by the Board such that reasonable persons

247. *Id.*

248. *Id.* at 18-19.

249. *Id.* at 19-20.

250. *Id.* at 20.

251. *Id.* at 29 (citations omitted).

would be compelled to reach the contrary conclusion.”²⁵²

In *PSI Energy, Inc. v. The Home Insurance Co.*,²⁵³ also discussed earlier in Part I, the Indiana Court of Appeals ruled that expert testimony by the policyholder on causes and timing of contamination was admissible. The policyholder presented expert testimony and reports of an environmental consultant, Thomas Helfrich. Mr. Helfrich opined that leaks of tar and tar-related constituents from subsurface containment structures resulted from the masonry and concrete materials used to construct the structures, the age of the structures (mostly built in the late 1800s), and “the cumulative effect of disruptive events that caused the separation of mortar joints and new and wider cracks to develop continuously in these structures, including during the years 1950 to 1985.”²⁵⁴ Mr. Helfrich relied on his training and experience as an engineer and his areas of specialization which include “the performance of engineered structures in soils and the investigation and remediation of subsurface contamination.”²⁵⁵ He also relied on evidence of conditions at the sites in issue and his knowledge of hydraulic pressure inside a fully saturated structure.²⁵⁶ The expert had personally inspected some of the subsurface containment structures at each site and observed cracks in structure walls.²⁵⁷ He also relied on his observations at over 150 manufactured gas plant sites not at issue in the case.²⁵⁸ While admitting that it was not possible to verify his cumulative effects theory through specific observations, measurements, or calculations, he opined that the “cumulative effect of small disruptive events is the only logical explanation for this subsequent separation of mortar joints and cracking and breaking of the structures.”²⁵⁹

The insurers, who were seeking to avoid coverage, moved to strike Mr. Helfrich’s “cumulative effects” theory because it could not be empirically tested, it had not been peer-reviewed or even written down, it contained no standard or other bases for applying the theory, and because the theory was not shown to be accepted or even heard of within the relevant scientific community.²⁶⁰ The policyholder’s response was that the issues involved do not involve complex scientific principles and that its expert had, based on his educational training and expertise and his review of relevant data, “developed a reasoned opinion of the general causes for these subsurface escapes” of contaminants.”²⁶¹ The court of appeals quoted *McGrew v. State*,²⁶² a case involving forensic analysis of hair

252. *Id.* at 31.

253. 801 N.E.2d 705 (Ind. Ct. App. 2004).

254. *Id.* at 739.

255. *Id.*

256. *Id.*

257. *Id.*

258. *Id.* at 740.

259. *Id.*

260. *Id.*

261. *Id.*

262. 682 N.E.2d 1289, 1291 (Ind. 1997).

specimens, for the proposition that some types of scientific analysis were “more a matter of the observations of persons with specialized knowledge than a matter of scientific principles governed by Indiana Evidence Rule 702(b).”²⁶³ The court of appeals agreed with the policyholder that its expert’s theory is “reliably based on his observations and application of his specialized knowledge to those observations.”²⁶⁴ The court noted that the expert’s theory would be subject to cross-examination at trial.²⁶⁵

The underlying reasoning of *Armstrong*, *Outlaw*, and *PSI* is consistent. The more closely linked health effects are to the type, amount, and duration of exposure, the better. Matters of observation based on an expert’s background and training need not be empirically tested or peer-reviewed. Explicit evaluation of different possible causes for an effect enhance the reliability of an opinion. Although further debate about the reliability of scientific evidence that litigants seek to introduce to prove or disprove the validity of chemical exposure and other types of environmental claims is a certainty, the utility of common sense and careful advocacy in these scientific matters is clear.

C. The Scope of Public Nuisance Claims—*Gary v. Smith & Wesson*

In *City of Gary v. Smith & Wesson*,²⁶⁶ a decision with both national significance and intriguing potential application to environmental matters, the supreme court allowed Gary to sue gun manufacturers under the public nuisance statute and for negligence.

City of Gary is a suit in which Gary seeks damages from gun manufacturers, distributors, and dealers for damages and injunctive relief for conducting their business in a way which unreasonably interfered with public rights in the City of Gary. The nuisance claim arises under both section 821B of the Restatement (Second) of Torts and section 32-30-6-6 of the Indiana Code. The statute reads: “Whatever is: (1) injurious to health; (2) indecent; (3) offensive to the senses; or (4) an obstruction to the free use of property; so as essentially to interfere with the comfortable enjoyment of life or property, is a nuisance, and the subject of an action.”²⁶⁷

Applying the common law rule of reasonableness, the court concluded that an actionable nuisance is “an activity that generates injury or inconvenience to others that is both sufficiently grave and sufficiently foreseeable that it renders it unreasonable to proceed at least without compensation to those that are harmed.”²⁶⁸

The City claimed the gun manufacturers, distributors and dealers know that the foreseeable laxness of dealers and their employees and the ingenuity of criminals will result in guns finding their way to illegal uses. The defendants

263. *PSI*, 801 N.E.2d at 741 (internal quotations omitted).

264. *Id.*

265. *Id.*

266. 801 N.E.2d 1222 (Ind. 2003).

267. IND. CODE § 32-30-6-6 (2003).

268. *City of Gary*, 801 N.E.2d at 1231.

asserted that a public nuisance must involve violation of a statute, the use of land, or an independent tort. The court rejected these supposed prerequisites, as well as the claim that state gun law regulation pre-empted local litigation.²⁶⁹ While noting the challenges the City faced in proving specific damages, the court declined to hold that damages from illegal gun sales are too remote to be actionable.²⁷⁰ The court also reversed the court of appeals' dismissal of the City's negligence claim, holding that all persons in the chain of distribution have a duty not to facilitate illegal gun ownership.²⁷¹

The decision has important implications for environmental litigation and regulation. Nuisance and negligence theories have added vitality. Municipal entities may use the nuisance statute and the common law to compel cleanups even for activities that once were completely legal and from persons which do not own the land but are in some way responsible for its condition. This in turn may facilitate pursuit of former owners' insurers.

CONCLUSION

PSI and its predecessors have given Indiana an important boost in addressing the vast costs of cleaning an industrial environment. That law is a consistent application of principles arising from the unique nature of liability insurance.

The frontiers of environmental obligation continue to expand and contract. Clean air litigation, in particular, shows how difficult it is to develop consistent, equitable standards for the cleanliness of our environment in cases over statutes and regulations which are unclear.

269. *Id.* at 1231-41.

270. *Id.* at 1240-41.

271. *Id.* at 1241-47.