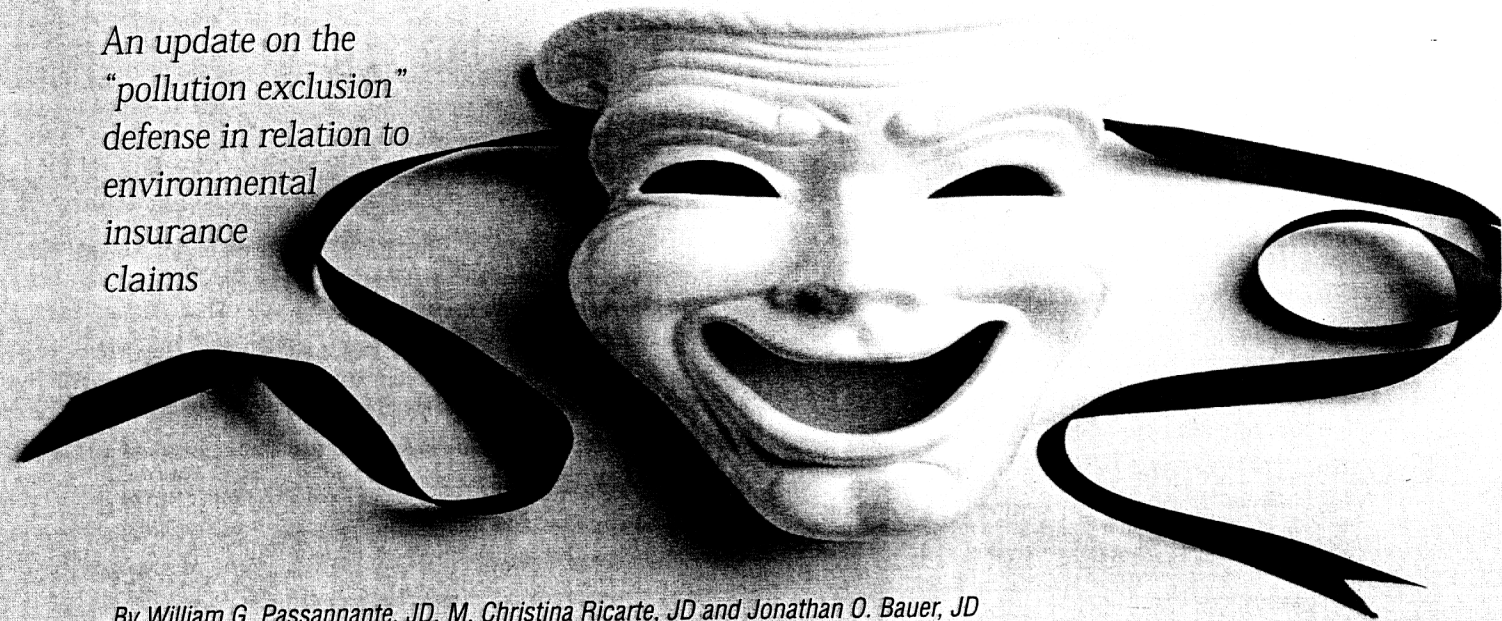


Environmental Insurance: The Fat Lady Has Not Yet Sung

An update on the
"pollution exclusion"
defense in relation to
environmental
insurance
claims



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Your company submits an environmental insurance coverage claim to its insurance company. They do not pay the claim. Are you surprised? If you've been down this road before, then you know that insurance companies take a "no pay" position on environmental claims and assert a laundry list of purported defenses to coverage. You also know that you will not get your insurance dollars without a fight. Well, here is some new ammunition for that fight.

Incidentally, if you haven't been down this road — definitely keep reading.

When a policyholder submits an environmental claim to its insurance company, the insurance company's knee-jerk reaction is to assert several common coverage defenses regardless of whether they are valid under the law that would be applied to the claim. Chief among these purported coverage defenses is what is commonly referred to as the so-called "pollution exclusion."

*This insurance does not apply * * * (f) to bodily injury or property damage arising out of the discharge, dispersal, release or escape of smoke, vapors, soot, fumes, acids, alkalis, toxic chemicals, liquids or gases, waste materials or other irritants, contaminants or pollutants into or upon land, the atmosphere or any water course or body of water; but this exclusion does not apply if such discharge, dispersal, release or escape is sudden and accidental.*

The so-called "pollution exclusion" was a Trojan Horse. The insurance industry slipped it into their standard policy forms by telling state insurance commissioners — who are charged with reviewing and approving policy forms — that the exclusion was a "mere clarification of coverage" in Comprehensive General Liability (CGL) policies. See *Morton International v. General Accident Insurance Co.*, 134 N.J. 1, 629 A.2d 831 (1993). Of course, had the insurance industry characterized the addition of the so-called "pollution exclusion" to its policies as anything other than a "clarification" of exist-

ing insurance coverage, then the insurance industry would have had to acknowledge that the so-called "pollution exclusion" was a reduction in the scope of the insurance coverage provided by the CGL policies. But a reduction in insurance coverage would have required a reduction in premium, and that was not something that served the insurance industry's interest. Thus, the "clarification" explanation was born. The Supreme Court of New Jersey documented this regulatory history and concluded as follows:

Stated accurately, the pollution-exclusion clause, as construed today by the industry, eliminates all coverage for unintended pollution-caused damage that the occurrence-based policy had provided, except for the unusual "boom-event" type case in which the discharge of the pollutants was both sudden — meaning abrupt — and accidental. To describe a reduction in coverage of that magnitude as a "clarification" not only is misleading, but comes perilously close to deception. Moreover, had the industry acknowledged the true scope of the proposed reduction in coverage, regulators would have been obligated to consider imposing a correlative reduction in rates.

134 N.J. at 38-39, 629 A.2d at 853.

Typically, insurance companies must seek approval from each state's insurance regulators before new policy terms can be included in insurance policies sold in each respective state. The so-called "pollution exclusion" first was submitted to insurance regulators in 1970. In some states, the insurance commissioners did not approve the new endorsement for two basic reasons. First, they were suspicious of purported "clarifying" language. That is to say, why do we need to clarify policy language that had been represented to us as clear in the first place? Second, if it wasn't just a "clarification" but was a reduction in coverage, then there should be a concomitant reduction in premiums.

The states that did not approve the so-called "pollution exclusion" were New Hampshire, Vermont, North Carolina and Mary-

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land. The Maryland insurance commissioner specifically disapproved of the so-called "pollution exclusion" in 1970 because his office called the bluff of the insurance industry's "clarification" explanation:

During the early 1970's, while ISO and insurance company representatives sought approval for the [pollution exclusion], I suggested to ISO, as well as to individual insurance companies, that they submit their proposed PEC [pollution exclusion clause] to a formal rate hearing for a determination of whether it was only a clarification endorsement (as they represented) or whether it was ambiguous, unclear, and could also be interpreted as a reduction in coverage. Neither ISO nor any insurance company was willing to risk a rate hearing by the Maryland insurance commissioner on the issue of whether or not the PEC [pollution exclusion clause] was ambiguous and might reduce coverage.

Between 1970 and 1982 — despite repeated attempts by the insurance industry to reverse the Maryland insurance commissioner — the Maryland insurance commissioner refused to approve the endorsement. In fact, the Maryland insurance commissioner never specifically approved the so-called "pollution exclusion." In 1983, the so-called pollution exclusion was permitted for use in Maryland only because the Maryland legislature repealed that portion of its insurance laws that required prior approval by the insurance commissioner before a policy provision could be added to the policy.

Ignoring its prior statements to the insurance commissioners, including the Maryland insurance commissioner, the insurance industry unleashed its army of lawyers to advance the "it's not covered" position. Indeed, at the behest of those very lawyers, the so-called "pollution exclusion" has been interpreted by Maryland courts as being a significant reduction in coverage, not the "clarification" that they said it was when it was slipped past the insurance commissioners of most states. *AMICO v. ARTRA Group Inc.*, 659 A.2d 1295 (1995). Based on *ARTRA*, insurance companies now routinely argue that the so-called "pollution exclusion" bars insurance coverage in pre-1983 policies for environmental damage in Maryland.

The insurance companies argument begs the following question: How can the so-called "pollution exclusion" be applied to pre-1983 policies when the Maryland insurance commissioner specifically disapproved and disallowed it between 1970 and 1982? This question was raised and answered in favor of policyholders in *Glidden v. Aetna Casualty & Surety, et. al.*

Glidden was an environmental coverage action brought in New Jersey against the usual cast of insurance companies. In *Glidden*, the policyholder faced environmental liabilities at 56 environmental sites located in more than a dozen states. Four of the environmental sites were located in Maryland. The defendant insurance companies argued that the Maryland sites should be dismissed from the case because of the so-called "pollution exclusion" in certain of the policies sold to the policyholder. The insurance companies' argument was premised on the interpretation of the so-called "pollution exclusion" under their view of Maryland law. The New Jersey court, following the New Jersey Supreme Court *Pfizer* trilogy (*Pfizer v. Emp. Ins. Of Wausau*, 154 N.J. 187 (1998)), ruled that Maryland law governed the Maryland sites. Under Maryland law, and the restrictive interpretation of the so-called "pollution exclusion" in the *ARTRA* decision, the court granted the insurance companies summary judgment motion and dismissed the Maryland sites from the case.

The policyholder did not give up. *Glidden* pressed the court to reconsider its dismissal of the Maryland sites in light of the Maryland insurance commissioner's specific disapproval of the so-called "pollution exclusion." In its motion for reconsideration, the policyholder argued that if Maryland law controlled, then the insurance company was bound by the actions of the Maryland insurance commissioner. Specifically, the insurance company was bound by the Maryland insurance commissioner's disapproval of the so-called "pollution exclusion" endorsement. While no court had ever directly addressed the issue, a decision from Maryland's highest court recognized, in dicta, that the so-called "pollution exclusion" was not enforceable in Maryland prior to 1983. In *Glidden*, the policyholder argued that if the Maryland Insurance Commissioner disapproved of the endorsement between 1970 and 1982, and if such disapproval rendered the endorsement unenforceable, then the insurance companies could not assert it to bar insurance coverage under the policies in force during those years. The court agreed and reinstated the Maryland sites as to all the insurance companies who sold pre-1983 insurance policies to the policyholder.

In its March 20, 2001, decision, the court held that:

The Maryland insurance commissioner disapproved of the 'sudden and accidental' clause during the 1970s-1982 period.

The Maryland Special Court of Appeals specifically noted that the clause was not approved until January 1983. Bentz v. Mutual Fire...The Bentz court suggested

in dicta that the "sudden and accidental" clause was not enforceable in Maryland prior to that time. This court agrees with the Bentz court...

In further describing its reasoning, the court explained that the Maryland Insurance Department's judgment "should be given effect." The court also reasoned "the insurance law in effect at the time that the insurance company's policies were written provide that

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unapproved clauses appearing in policies were unenforceable and that the policies should be construed as if the clause had been deleted." Finally, the court stated that it intended to "give the [Maryland] statute its full effect, particularly in light of the Maryland Legislature's express strong public policy regarding the protection of land and the citizen's of Maryland from pollution." See *Bausch & Lomb, Inc. v. Utica Mutual Insurance Co.*

The decision in *Glidden* marks the first time a court has specifically addressed and ruled on this issue.

This court decision means that policyholders with environmental risks in Maryland now can defeat claims by insurance companies that the so-called "pollution exclusion" bars insurance coverage under pre-1983 insurance policies. If your insurance company argues the so-called "pollution exclusion" in pre-1983 insurance policies means you do not get coverage in Maryland — let them know that you know better.

The decision in *Glidden* also is important for another reason — it shows how much can be accomplished when policyholders start to look at old problems with fresh eyes.

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