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'Ward Sand' Is Sandbagged

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In *Ward Sand and Materials Co. v. The Transamerica Ins. Co.*, A-1479-13T1 (App. Div. 2016), the New Jersey Supreme Court ruled in favor of the insurance industry on the long-contested issue of how to allocate responsibility for losses in claims involving multiple insurance companies, some of which are insolvent.

Beginning in 1970, the plaintiff (Ward) accepted municipal waste from Pennsauken at its sand-mining property. Ward ended up liable to the New Jersey Department of Environmental Protection for the subsequent cleanup. Ward had purchased comprehensive general liability and excess policies for each year from 1970 to 1986 for a coverage total of about $100 million. Ward's liability at the landfill was $5.5 million. However, Ward only received $1,938,200 from its insurance companies. How could a policyholder that purchased primary and excess insurance in every year receive less than 40 percent from its insurance companies?

The answer is that Ward had the particular misfortune of choosing several primary and excess insurance companies that entered liquidation. Out of 16 implicated coverage years, the primary insurance companies in seven were in liquidation. There is no indication that Ward knowingly chose insurance companies that were in financial straits. Ward chose well-known insurance companies—and simply had bad luck.

'Owens-Illinois' and 'Carter-Wallace'

The issue that the court in *Ward* confronted was how to allocate Ward's recoverable damages among insurance policies when some of those insurance companies were in liquidation. *Owens-Illinois v. United Ins. Co.*, 138 N.J. 437 (1994), is the leading New Jersey case addressing the issue of allocation. In that case, the New Jersey Supreme Court had to choose between two conflicting theories of allocation.

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The first construct, championed by policyholders, is known as "all sums" (or "joint and several"). Under this theory, the policyholder can choose any one year in the continuous trigger period and collect all of its loss in that year. That chosen insurer then can re-allocate the loss among other triggered insurance companies pursuant to other insurance clauses and equitable considerations. The insurance company cannot re-allocate to the policyholder when there are liquidations, deductibles or other self-insurance. Thus, under the "all sums" methodology, the policyholder would avoid the problem of insurance companies in liquidation and leave the question of allocation to the solvent insurance companies from which it purchased policies.

The second construct is known as pro-rata allocation. Under this construct, the loss is allocated equally to each year. Pro-rata jurisdictions normally assign periods of self-insurance or liquidation to the policyholder.

The New Jersey Supreme Court, in *Owens-Illinois,* found little difference between the two approaches: "no great difference in principle divides *Keene* and *Forty-Eight Insulations* [the leading joint-and-several and pro-rata decisions]. Using either method, allocation will exist among the insurance companies on the risk." The court adopted a modified pro-rata approach, based upon the public policy ground of encouraging people to purchase insurance. The court was concerned that, for example, a company might choose to purchase insurance in only one out of five years. Then, under an "all sums" approach, it could place its loss in the one year in which it bought insurance.

The court did not intend to set these rules in stone. Rather, allocation was meant to be an evolving concept. *Owens-Illinois* stated "if, after experience, we are convinced that our solution is inefficient or unrealistic, we will not hesitate to revisit the issue." "We do not expect that this case will be the 'last word' in this area. Environmental liability insurance law, like any other area of law, will have to develop over time and trial courts must be flexible in responding to new fact situations." (Citation omitted.)

Carter-Wallace v. Admiral Ins. Co., 154 N.J. 312 (1998), was the Supreme Court's next allocation decision, and it followed the course laid out in *Owens-Illinois*. Noting that "our resolution of the [allocation] issue was guided by our concern for the efficient use of resources to address the problem of environmental disease and by the demands of simple justice," the court found that in calculating the amount of insurance that a policyholder purchased each year, the court should consider both primary and excess coverage. Primary insurance companies were not happy with this holding, because it meant that the primary insurance company's allocation was based on how much excess insurance the policyholder chose to purchase that year. However, allocation was based on how much risk the policyholder externalized.

'Spaulding' and 'Benjamin Moore' Put Policyholder on the Hook in Liquidations

Spaulding Composites Co. v. Aetna Cas. & Sur. Co., 176N.J. 25 (2003), was the first case to opine, albeit in dicta, that years in which the insurance company was in liquidation should be allocated to the policyholder. The court quoted Donald Erickson, in an article entitled "Emerging Primary and Excess Coverage Issues in Continuous Trigger Regimes," 28 Brief 18 (1999), to the effect that "[u]nder that [continuous trigger] scheme, the insured is obligated to pay its 'aliquot' share of both defense and indemnification on account of years in which it was uninsured, self-insured or its coverage was exhausted or bankrupt."

Spaulding concerned a "nonaccumulation clause" in the policy. That clause stated that when multiple insurance policies applied to a single occurrence, only one policy limit applied. The court rejected this clause, which would have tremendously reduced the insurance industry's exposure. The court adopted the legal fiction that there was a separate occurrence in each year.

Benjamin Moore & Co. v. Aetna Cas. & Sur. Co., 179 N.J. 87 (2004), followed *Spaulding*. The case concerned the application of successive deductibles in successive policies triggered by the continuous trigger. Here too, the court relied upon the theory that a separate occurrence took place in every year. The court reiterated the same quote from Erickson, and then stated in dicta, "Likewise, policyholders are required to underwrite the risk of insurer insolvency or bankruptcy."

'Farmers' Mutual'

In 2004, the legislature enacted a statute stating that in multiple trigger situations in which more than one insurance company had exposure, and the Guaranty Association was one of the parties, the Guaranty Association would not be liable until all other insurance had been exhausted. The state Supreme Court confronted N.J.S.A. 17:30 A-5 in *Farmers Mutual Fire Ins. Co. of Salem v. NJ Property Liability Ins. Guar. Assn*., 215 N.J. 522 (2013), and found that, as a statute, it overrode the common law. As a result, the aliquot share of the Guaranty Association was re-assigned to the solvent insurance companies. The Appellate Division in *Ward* did not apply *Farmers Mutual* because it found that the statute was only prospective. However, *Farmers Mutual* provides solid support for the re-allocation of the insolvent insurance company's share of liability to the solvent insurance companies.

Conclusion

Ward should not have had an *Owens-Illinois* issue of allocation. It purchased insurance in every year. However, the trial court and Appellate Division looked to the dicta in the later Supreme Court decisions in *Spaulding Composite* and *Benjamin Moore* to hold that the burden of the years in which an insurance company was in liquidation should fall on Ward. The Appellate Division affirmed, and Ward has filed a petition for certification.

The Appellate Division recognized the "unfairness" of its holding. However, an unjust answer is out of step with *Owens-Illinois* and *Carter-Wallace*, which expressly anchored their holdings in the concept of "simple justice." The whole purpose of *Owens-Illinois* was to act equitably and consistently with public policy. The fundamental goal of *Owens-Illinois* was to encourage companies to purchase insurance, and to reward those who did. Ward purchased insurance in every year. The Appellate Division in *Ward* erred in affording it only 40 percent of coverage. *Owens-Illinois* did not adopt a modified pro-rata approach because it was "right." Rather, the Supreme Court rejected both pro-rata and all-sums. It fashioned a unique equitable remedy. The courts should not frustrate *Owens-Illinois* by woodenly and mechanically applying a pro-rata scheme.

The purpose of insurance is to insure. Ward purchased insurance in every year. It should be provided coverage for every year. ■