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Expert Analysis

How Far Will Insurers Stretch the Absolute Pollution Exclusion?

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The insurance industry has spent more than three decades expanding the reach of the "pollution exclusion" through policy revisions and strenuous litigation. Current versions of the so-called "absolute" pollution exclusion are so expansive that literal application eviscerates swaths of intended coverage.

The hottest litigation issue is recent years is whether the absolute pollution exclusion bars coverage for *indoor* releases of substances not normally thought of as "pollutants," but which may fall within the exclusion's broad definition of the term. Many pending lawsuits focus specifically on applying the exclusion to indoor releases of sulfur from drywall manufactured in China.

Emboldened by successes with courts excluding the Chinese drywall cases from coverage, will insurers continue stretching the exclusion beyond any reasonable concept of "pollution," perhaps eventually being hoist by their own petard?

HISTORY OF THE POLLUTION EXCLUSION

The pollution exclusion has been a liability policy stalwart since 1973, and iterations of the exclusion have been litigated ever since.

Coverage litigation intensified in the 1980s, following enactment of major federal environmental statutes and the countless state environmental laws they spawned.[1]

For several years, the legal war centered on a version of the exclusion that precludes coverage unless a release of pollutants was "sudden and accidental."[2] A key issue was whether courts should construe "sudden and accidental" to bar coverage for gradual, long-term releases of hazardous substances into soil and groundwater.

Some courts concluded that a policyholder could reasonably expect "sudden and accidental" to mean "unexpected and unintended."[3] The courts that opted for this liberal, pro-insured construction granted coverage for both abrupt, short-term releases and gradual, long-term releases.

Some courts remain divided on the scope of the "sudden and accidental" version of the pollution exclusion although the matter has been resolved in most states.[4]

THE ABSOLUTE POLLUTION EXCLUSION

The insurance industry amended the pollution exclusion in response to adverse rulings concerning the "sudden and accidental" version of the exclusion. Today, virtually all commercial general liability policies contain a variation of the "absolute" pollution exclusion.

Although there are differences among insurers' versions of the exclusion, each broadly defines "pollutants" and has done away with the "sudden and accidental" exception. Most insurers have also eliminated language limiting application to releases "upon the land, atmosphere or water."

The most common definition of "pollutants" now encompasses "any solid, liquid, gaseous or thermal irritant or contaminant, including smoke, vapor, soot, fumes, acids, alkalis, chemicals and waste."

Although this definition enables insurers to urge application of the exclusion to a vast array of circumstances having little to do with conventional "pollution," some insurers have opted for an even broader definition.

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One prominent insurer, ACE American, defines "pollution" to include "the actual, alleged or potential presence in or introduction into the environment of any substance if such substance has, or is alleged to have, the effect of making the environment impure, harmful or dangerous."

Under the same policy provision, environment includes "any air, land, structure or the air therein, watercourse or water, including underground water."

This combined definition of "pollution" and "environment" theoretically allows the insurer to deny coverage of any alleged pollution claim based on the presence anywhere in the world of virtually any substance known to man.

Some courts reject such a construction as "absurd," because there is virtually no substance "in existence that would not irritate or damage some person or property."[5]

Indeed, insurers could attempt to invoke this version of the exclusion to bar coverage where a defective steam pipe bursts and burns a homeowner or where a defective container of household drain cleaner leaks and injures a child. Even the most militant insurance industry advocate would be unable to produce evidence that the any insurer intended the absolute pollution exclusion to bar coverage in this manner.

COURTS DISAGREE ON SCOPE

Appropriately, all courts enforce the absolute pollution exclusion to bar coverage for damage caused by the full range of traditional pollution of air, surface water, groundwater and soil, irrespective of whether the pollution was abrupt or gradual.

In cases involving non-traditional pollution, however, courts have arrived at "a dizzying array of results."[6]

There is a nationwide split of authority and national debate over whether the absolute pollution exclusion, despite its broad language, extends to losses caused by non-traditional environmental pollution.[7]

Under the law of states that do not limit the absolute pollution exclusion to traditional pollution, there is keen interest in how far insurers will be allowed to stretch the exclusion.

INDOOR RELEASES OF 'POLLUTANTS'

A major coverage battleground involves claims arising from bodily injury and property damage caused by *indoor* releases of "pollutants." Courts are sharply divided on whether indoor releases fall within the absolute pollution exclusion.

Some courts find the exclusion unambiguous and enforce the broad exclusionary language literally to bar coverage for a wide variety of indoor releases.[8]

Other courts refuse to enforce the exclusion in the context of indoor releases, finding that the inherent intent of the exclusion is to preclude coverage for traditional environmental pollution. Courts with this view have determined that an expansive construction of the exclusion would conflict with the insured's reasonable expectations or, at least, that aspects of a given version of the exclusion are ambiguous.[9]

Several courts have refused to apply to absolute pollution exclusion to bar coverage for claims arising from indoor releases of carbon monoxide from a pool heater,[10] apartment heating system,[11] wall heater,[12] restaurant oven[13] and bathroom heater.[14]

Courts have likewise rejected the exclusion in claims arising from indoor releases of mercury in a day care facility,[15] mercury in an apartment,[16] paint fumes in an office building[17] and fumes from a floor sealant.[18]

CHINESE DRYWALL

Several recent decisions concerning the absolute pollution exclusion have arisen from the numerous lawsuits claiming property damage and bodily injury caused by indoor sulfur releases from Chinese drywall.

In the aftermath of Hurricanes Katrina and Rita in 2005, domestic drywall manufacturers were unable to meet increased demand for their products. Some domestic drywall makers and other businesses responded by importing drywall from China.

As it turns out, much of the Chinese drywall emits levels of sulfur sufficient to cause property damage and alleged bodily injuries. Chinese drywall is believed to exist in more than 200,000 homes, most of which are located along the Gulf Coast.

Courts have thus far issued more that 20 reported decisions on application of the absolute pollution exclusion to damage caused by Chinese drywall. Most of these decisions have been based on Florida and Virginia law, which are insurer-friendly in application of the absolute pollution exclusion.

In 2009 a federal court applying Florida law allowed the exclusion to bar coverage for bodily injury caused by a child's ingestion of dirty swimming pool water.[19]

Also, a prominent insurer sued in Florida for a declaratory judgment that the absolute pollution exclusion bars a claim for injury caused by children's consumption of convenience store "Slush Puppies" tainted with gasoline.[20] The court has not yet ruled on this matter.

Consequently, insurers have been largely successful in avoiding coverage for indoor releases from Chinese drywall.[21]

The Louisiana federal court managing much of the Chinese drywall litigation, however, refused to apply the absolute pollution exclusion in the cases, saying "the presence of Chinese drywall in the plaintiffs' homes is outside the ambit of ... environmental pollution for purposes of the exclusion."[22]

There is a nationwide split of authority and national debate over whether the absolute pollution exclusion, despite its broad language, extends to losses caused by non-traditional environmental pollution.

Although the vast majority of coverage litigation involving Chinese drywall is in Florida, Louisiana and Virginia, a handful of coverage lawsuits involving both Chinese and domestic drywall are pending in states that have declined to expand the absolute pollution exclusion beyond traditional environmental pollution.[23]

Most recently, a Colorado state court considering a Chinese-drywall case recognized the "significant" difference between Florida and the law of states where the absolute pollution exclusion is construed in accordance with more traditional notions of "pollution."[24] Because of these differences among the states, Chinese drywall and other non-traditional pollution cases can turn on choice-of-law determinations.

Today, virtually all commercial general liability policies contain a variation of the "absolute" pollution exclusion.

The court noted that some states refuse to apply the absolute pollution exclusion "reflexively" to "accidents arising during the course of normal business activities simply because they involve 'discharge, dispersal, release or escape' of an 'irritant or contaminant.'"[25]

The court cited examples such as "injuries caused by the ingestion of lead paint, the death of a man who inhaled poisonous fumes when he applied a carpet adhesive and injuries caused by fumes emanating from cement used to install a plywood floor."[26]

CONCLUSION

States that do not limit the absolute pollution exclusion to traditional environmental pollution are fertile ground where insurers can rely on the exclusion in a growing variety of circumstances, particularly instances of indoor releases.

The nationwide split of authority makes choice of venue potentially outcome-determinative.

As the scope of the absolute pollution exclusion plays out in relation to Chinese drywall and other circumstances of non-traditional pollution, it will be interesting to see how ambitiously insurers attempt to stretch the exclusion.

If insurers push too hard (tainted "Slush Puppies"), they may become victims of their own success through judicial or legislative backlash.

NOTES

1 Comprehensive Environmental Response, Compensation and Liability Act, 42 U.S.C. § 9601; Resource Conservation and Recovery Act, 42 U.S.C. § 6901.

2 *Northern Ins. Co. v. Aardvark Assocs.*, 942 F.2d 189 (3d Cir. 1991).

3 *See, e.g., Cotter Corp. v. Am. Empire Surplus Lines Ins. Co.*, 90 P.3d 814 (Colo. 2004); *St. Paul Fire & Marine Ins. Co. v. McCormick & Baxter Creosoting Co.*, 923 P.2d 1200 (Or. 1996); *Am. States Ins. Co. v. Kiger*, 662 N.E.2d 945 (Ind. 1996); *Queen City Farms v. Cent. Nat'l Ins. Co. of Omaha*, 882 P.2d 703 (Wash. 1994); *Outboard Marine Corp. v. Liberty Mut. Ins. Co.*, 607 N.E.2d 1204 (Ill. 1992)

4 *See RSR Corp. v. Int'l Ins. Co.*, 612 F.3d 851 (5th Cir. 2010) (Under Texas law, the "sudden and accidental" exception "unambiguously excludes coverage for all pollution that is not released quickly, as well as unexpectedly and unintentionally."); *Northville Indus. Corp. v. Nat'l Union Fire Ins. Co.*, 679 N.E.2d 1044 (N.Y. 1997) (Under New York law, "sudden and accidental" has a temporal element, requiring the release to be "abrupt."); *Shell Oil Co. v. Winterthur Swiss Ins. Co.*, 15 Cal. Rptr. 2d 815 (Cal. Ct. App., 1st Dist. 1993) (same).

5 *Pipefitters Welfare Educ. Fund v. Westchester Fire Ins. Co.*, 976 F.2d 1037, 1043 (7th Cir. 1992); *see also Meridian Mut. Ins. Co. v. Kellman*, 197 F.3d 1178, 1182 (6th Cir. 1999); *Nautilus Ins. Co. v. Jabar*, 188 F.3d 27, 30 (1st Cir. 1999) (quoting Pipefitters); *Scottsdale Indem. Co. v. Village of Crestwood*, 784 F. Supp. 2d 988 (N.D. Ill. 2011); *Pac. Emp. Ins. Co. v. Clean Harbors Envtl. Servs.*, 2010 WL 438372 at *3 (N.D. Ill. 2010) (quoting Pipefitters); *Ocean Partners LLC v. North River Ins. Co.*, 546 F. Supp. 2d 101, 113 (S.D.N.Y. 2008) (quoting Pipefitters).

6 *Bituminous Cas. Corp. v. Sand Livestock Sys.*, 2005 WL 1476441 at *6 (N.D. Iowa 2005).

[7] *Auto-Owners Ins. Co. v. Potter,* 105 Fed. Appx. 484, 494 (4th Cir. 2004); *Apana v. TIG Ins. Co.,* 574 F.3d 679, 682 (9th Cir. 2009); *Janart 55 West 8th LLC v. Greenwich Ins. Co.,* 614 F. Supp. 2d 473 (S.D.N.Y. 2009).

[8] *See, e.g., Cincinnati Ins. Co. v. Becker Warehouse,* 635 N.W.2d 112 (Neb. 2001) (indoor release of xylene fumes from concrete sealant); *Firemen's Ins. Co. v. Kline & Son Cement Repair,* 474 F. Supp. 2d 779 (E.D. Va. 2007) (indoor release of fumes from floor sealant); *Deni Assocs. of Fla. v. State Farm,* 711 So. 2d 1135 (Fla. 1998) (indoor release of ammonia).

[9] Apana, 574 F.3d at 682-83; *Reg'l Bank of Colo. v. St. Paul Fire & Marine Ins. Co.,* 35 F.3d 494 (10th Cir. 1994); *Century Sur. Co. v. Casino West Inc.,* 2010 WL 762188 (D. Nev. 2010); *Wausau Bus. Ins. Co. v. IdleAire Techs. Corp.,* 2009 WL 413117 (Bankr. D. Del. 2009) (Tennessee law); Bituminous, 2005 WL 1476441 at *21-22.

[10] *Century*, 2010 WL 762188.

[11] *Stoney Run Co. v. Prudential-LMI Commercial Ins. Co.,* 47 F.3d 34 (2d Cir. 1995).

[12] *Reg'l Bank,* 35 F.3d 494.

[13] *Western Alliance Ins. Co. v. Gill,* 686 N.E.2d 997 (Mass. 1997).

[14] *Thompson v. Temple,* 580 So. 2d 1133 (La. Ct. App., 4th Cir. 1991).

[15] *Baughman v. U.S. Liab. Ins. Co.,* 662 F. Supp. 2d 386 (D.N.J. 2009).

[16] *Janart*, 614 F. Supp. 2d 473.

[17] *Belt Painting Corp. v. TIG Ins. Co.,* 100 N.Y.2d 377 (N.Y. 2003).

[18] *Meridian*, 197 F.3d 1178.

[19] *First Specialty Ins. Corp. v. GRS Mgmt. Assocs.,* 2009 WL 2524613 (S.D. Fla. 2009).

[20] *Certain Interested Underwriters at Lloyd's, London v. Jindani,* 2009 WL 5171755 (M.D. Fla. 2009).

[21] *See, e.g., Granite State Ins. Co. v. American Bldg. Materials,* 2011 WL 6025655 (M.D. Fla. 2011) (Massachusetts law); *Colony Ins. Co. v. Total Contracting & Roofing,* 2011 WL 4962351 (S.D. Fla. 2011); *Gen. Fidelity Ins. Co. v. Foster,* 2011 WL 3962646 (S.D. Fla. 2011); *Evanston Ins. Co. v. Harbor Walk Dev.,* 2011 WL 4495686 (E.D. Va. 2011); *CDC Builders v. Amerisure Mut. Ins. Co.,* 2011 WL 4454937 (S.D. Fla. 2011); *Dragas Mgmt. Corp. v. Hanover Ins. Co.,* 798 F. Supp. 2d 766 (E.D. Va. 2011); *Nationwide Mut. Ins. Co. v. Overlook LLC,* 785 F. Supp. 2d 502 (E.D. Va. 2011); *TRAVCO Ins. Co. v. Ward,* 715 F. Supp. 2d 699 (E.D. Va. 2010).

[22] *In re Chinese Manufactured Drywall Prods.,* 759 F. Supp. 2d 822, 843 (E.D. La. 2010) (applying Louisiana law).

[23] *See, e.g., New NGC v. ACE Am. Ins. Co.,* No. 3:10-CV-00022 (W.D.N.C.) (North Carolina law.)

[24] *Probuild Holdings v. Granite State Mut. Ins. Co.,* No. 10-CV-378 (Colo. Dist. Ct., Boulder County Jan. 17, 2012).

[25] *Id.,* citing *Western Alliance*, 426 Mass. 115.

[26] *Western Alliance,* 426 Mass. at 118-119.

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