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‘Total pollution exclusion’ doesn’t bar excess coverage for oil spill

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— Vincent J. Pisegna, Boston

Performance Trans., Inc., et al. v. General Star Indemnity Company

THE ISSUE Did an excess carrier breach its policy by denying coverage for cleanup costs associated with a gasoline spill when one of the policyholder’s trucks overturned?

DECISION Yes (1st U.S. Circuit Court of Appeals)

LAWYERS Syed S. Ahmad and David M. Parker, of Hunton, Andrews, Kurth, Washington, D.C., and Richmond, Virginia; Jared A. Fiore and Douglas T. Radigan, of Bowditch & Dewey, Worcester (plaintiffs)
Cara Tseng Duffield and Hume M. Ross, of Wiley Rein, Washington, D.C. (defense)

‘Special hazards’ endorsement in policy created ambiguity

by Eric T. Berkman

An excess carrier breached its policy by denying coverage for cleanup costs associated with a gasoline spill when one of the policyholder’s trucks overturned, the 1st U.S. Circuit Court of Appeals has ruled.

Plaintiff Performance Trans., Inc., a commodities transport company, had a $5 million excess policy with defendant General Star Indemnity Co. PTI’s primary insurer paid the $1 million policy limit, but General Star refused to cover additional costs, citing a “total pollution exclusion” disclaiming coverage for discharge of pollutants.

The policy also contained a “special hazards” endorsement stating that the policy did not cover losses from “drilling fluids unloading hazards,” but also listing “the unloading of drilling fluids” resulting from “upset or overturn of [an] auto” as the second of four exceptions to the exclusion.

Meanwhile, the endorsement included qualifying language after the fourth exception that, according to PTI, could be read multiple ways.

A U.S. District Court judge found lack of coverage, applying what he deemed a per se rule that an exception to an exclusion cannot create an affirmative coverage obligation when another provision, here the total pollution exclusion, unambiguously bars coverage. The 1st Circuit reversed, but on grounds that multiple possible interpretations of the endorsement itself gave rise to an overall policy ambiguity.

“Massachusetts law is unequivocal that faced with two plausible interpretations of the policy, we must construe all ambiguity in favor of the insured,” Judge Sandra L. Lynch wrote for the panel, adding that because it was an excess policy for a company that shipped petroleum products, interpreting the agreement to exclude a major risk in PTI’s business line contradicted the policy’s purpose.

The 16-page decision is Performance Trans., Inc., et al. v. General Star Indemnity Company, Lawyers Weekly No. 01-269-20.

Well-settled principle

Attorneys for the parties did not respond to requests for comment. But Vincent J. Pisegna, a civil litigator in Boston who handles coverage disputes, said the decision illustrates a well-settled principle that a contract is read in light of its purpose.

Here, he said, the policyholder shipped petroleum products, making spills one of its major risks.

“This is the reason you get insurance, especially excess insurance,” Pisegna said. “The court avoided the temptation offered by the insurance company to take a literal reading of a complex insurance agreement to effect a result which is not consistent with the purposes of the contract.”

Steven Torres of Boston, who also handles coverage cases, said the decision should be of interest to insurance attorneys, since the 1st Circuit issues so few coverage opinions. He also said the ruling reinforces the maxim that policy ambiguities are construed in favor of the insured.

“The lesson to insurers may be the need to eliminate contradictory policy terms,” Torres said.

Sara Perkins Jones of Boston agreed, pointing out the court’s observation that nothing in the record indicated it was a form policy, suggesting that the policy language in question, which is not commonly used, could have been negotiated by the insured or its broker.

“This decision appropriately places the onus and risk on the insurer that negotiated language will ultimately be determined to be ambiguous, without regard to who drafted it,” Jones said. “Underwriters negotiating such policies with brokers may point to this as a new reason to resist additions or edits that diverge from time-tested provisions.”

But Roslindale insurance attorney Nina E. Kallen said the possibility that it was a negotiated policy suggests that the court may have “overstated the maxim” that ambiguities are to be interpreted against the insurer.

“There is an exception to that rule if the policy was negotiated on a more equal footing between the insurer and a business, as opposed to a consumer,” Kallen said. “Here, the court did reference negotiations of the policy terms.”

Meanwhile, Boston insurance lawyer Michael F. Aylward said he was troubled by the court’s analysis “They refused to follow both Supreme Judicial Court and 1st Circuit authority, which explicitly says, ‘You don’t look at exceptions to find ambiguity,’” Aylward said. “And then they said that, having found an ambiguity, they didn’t need to consider the exception rule. They didn’t even cite the two leading cases and explain why they don’t apply here.”

Aylward was also concerned by the panel’s emphasis on the fact that an insured in the business of transporting petroleum would be concerned about covering oil spills.

“That may well be true, but they should have bought a policy without an absolute pollution exclusion in it,” he said, adding that such coverage is readily available. “[The 1st Circuit’s analysis] will make it harder to get summary judgment in these cases, while leaving the door open to a lot of result-oriented jurisprudence we haven’t seen up to now.”.

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Exception to exclusion?

On Feb. 19, 2019, a PTI tanker-truck overturned in upstate New York, spilling approximately 4,300 gallons of gasoline and diesel fuel onto the roadway and into a nearby reservoir.

The spill necessitated remediation work that has cost nearly $3 million to date.

At the time of the accident, PTI held about $1 million in primary coverage with Utica Mutual for its shipping operations; there was no dispute that its primary policy covered the incident.

PTI’s policy with General Star provided $5 million in excess coverage, and nothing in the record established that all terms of the excess policy were standard form insurance contracts.

The policy also contained 20 different riders, 15 of which were labeled exclusions. One of the exclusions, a “total pollution” exclusion, disclaimed coverage for any damages arising from discharge of pollutants, regardless of whether underlying insurance covered such harm.

Meanwhile, a rider entitled “Special Hazards and Fluids Limitation Endorsement” stated that the policy did not apply to “ultimate net loss or costs” from any event arising from any “special hazard” described in the endorsement and resulting from use of any auto. Among the listed special hazards was for “drilling fluid unloading.”

The endorsement also listed four exceptions to that exclusion, however. Item 2 created an exception for events arising from the unloading of drilling fluids resulting from “upset or overturn” of an auto.

Additionally, language appeared following Item 4 that created additional conditions for at least that exception, but possibly for all four.

In March 2019, General Star denied PTI’s claim for excess coverage, citing the total pollution exclusion.

When General Star rejected PTI’s claim two additional times, the insured, along with Utica — which had issued $1 million in provisional coverage on the condition that it be assigned PTI’s right to recover up to that amount from General Star — brought a breach of contract claim in U.S. District Court.

Judge Timothy S. Hillman granted summary judgment for the insurer, applying what he viewed as a per se rule in Massachusetts against finding an affirmative coverage obligation in an exception to an exclusion where another provision unambiguously bars coverage.

The plaintiffs appealed.

Ambiguous terms

The 1st Circuit found that it did not need to address whether the per se rule Hillman relied on exists under Massachusetts law, since the purpose and effect of the special hazards endorsement resulted in an ambiguous policy.

Lynch pointed out that the endorsement was susceptible to at least three interpretations: that the qualifying language following Item 4 was intended to apply to all four items; that the language created a limited coverage guarantee just for Item 4; or that none of the four exceptions applied if an exclusion elsewhere in the policy applied.

“The text of this agreement as a whole does not provide any context that resolves the ambiguity in the meaning of the Special Hazards Endorsement,” Lynch wrote. “In these circumstances, neither PTI’s nor General Star’s interpretation of the Special Hazards Endorsement is unreasonable.”

Given that any policy ambiguity must be construed in favor of the insured and that reading the agreement to exclude a major risk in PTI’s line of business was inconsistent with the purpose of the policy, Lynch said the panel concluded that coverage was available to PTI and reversed.