

Client Alert

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Pennsylvania Federal Court Finds Liability Policy's Pollution Exclusion Not A Bar To Coverage For Damages Resulting From A Petroleum Asphalt Spill

In *Travelers Indemnity Company v. MTS Transport, LLC*, No. 11-01567, 2012 U.S. Dist. LEXIS 127847 (W.D. Pa. Sept. 7, 2012), a federal court held that a pollution exclusion in an excess liability insurance policy was ambiguous and, therefore, did not bar a defense for claims arising out of a petroleum asphalt spill.

Background

On November 22, 2011, a tanker-truck leaked petroleum asphalt on the Pennsylvania Turnpike, damaging both the turnpike and more than 1,000 vehicles. The truck was owned by MTS Transport, LLC ("MTS").

MTS was insured under a \$1,000,000 commercial general liability policy, issued by Travelers Indemnity Company ("Travelers"), and a \$4,000,000 umbrella excess liability policy, issued by Hallmark Specialty Insurance Co. ("Hallmark"). After the spill and after acknowledging that the damages for cleanup claimed by the Pennsylvania Turnpike Commission would exceed the Travelers policy limits, Travelers filed an interpleader action in a Pennsylvania federal court, seeking to pay its policy limits into the court's registry in order to fulfill its obligations to MTS under its policy (the "Travelers action").

Hallmark, on the other hand, issued a reservation of rights letter to MTS, contending that the pollution exclusion in the Hallmark policy potentially barred any defense or indemnity obligations. The pollution exclusion in the Hallmark policy provided that coverage did not apply to any "injury, damage, expense, cost, loss, liability or legal obligation arising out of or in any way related to pollution, however caused." Pollution was defined as including the "actual, alleged or potential presence in or introduction into the environment of any substance, including pollutants, if such substance has or is alleged to have the effect of making the environment impure, harmful, or dangerous." Environment was defined to include any "air, land, structure or the air therein, watercourse or water, including underground water." Pollutants were defined to include any "solid, liquid, gaseous, or thermal irritant or contaminant including smoke, vapor, soot, fumes, acids, alkalis, chemicals and waste."

MTS filed a third-party complaint against Hallmark in the Travelers action, seeking a declaration that Hallmark was obligated to defend MTS for damages resulting from the spill. On cross motions for summary judgment, the parties addressed two principal issues: 1) what state's substantive law applied to the interpretation of the Hallmark policy; and 2) whether the pollution exclusion in the Hallmark policy barred coverage for the claims asserted against MTS.

Holding

After determining that Maryland law applies, the district court granted summary judgment in favor of MTS, finding that the pollution exclusion did not bar coverage for a defense and potential indemnification of MTS with respect to claims resulting from the spill.

First, the court applied Pennsylvania choice of law rules to determine which state's law applied to the Hallmark contract. MTS argued that Maryland law applied, while Hallmark argued for Pennsylvania law. The court explained that, since Pennsylvania and Maryland law are in conflict concerning the scope and application of the pollution exclusion, the conflict of law issues would be governed by the *Griffin* rule, which is a two-part test combining a "contacts" analysis with an "interests" analysis.

Under the *Griffin* rule's first prong — the contacts analysis — the court explained that, typically, the law of the state that is the principal location of the insured risk will be applied. However, where the insurance policy covers things such as ships, trucks, airplanes and railroad cars, the *Griffin* rule cannot be applied, since an object that regularly moves across state borders has no principal location. Instead, the court must look to a "general contacts test." The court concluded that Maryland's contacts with the parties and the contract were more significant than those of Pennsylvania, since Maryland was the place of contracting and also the place of domicile, residence and place of business of MTS, while Pennsylvania's only contact was that it was the place of injury. Thus, the first prong of the conflict of law analysis favored application of Maryland law.

With respect to the second prong — the interests analysis — the court explained that this prong "weighs the governmental interests of the states involved in the controversy to determine which state has the greatest interest in having its laws enforced." The court concluded that, like the first prong, Maryland has a more significant interest in the case, since Maryland has an interest in ensuring consistency and predictability for its citizens and businesses that purchase insurance policies, while Pennsylvania has an interest only in protecting insurers. Thus, the court held that Maryland law should be applied.

Next, the court addressed the coverage issues, which, under Maryland law, required that the court determine the intended scope and limitations of coverage under the insurance policy.

The court recognized that Maryland courts had previously found similar pollution exclusions to be ambiguous when applied to nontraditional environmental pollution. Consistent with those decisions, the court concluded that the pollution exclusion in the Hallmark policy was ambiguous both in its application to petroleum asphalt and in its application to a roadway spill. The court explained that a reasonably prudent person could consider petroleum asphalt an "irritant" or "contaminant," while another person could consider it neither. The court further explained that a reasonably prudent person could consider a petroleum asphalt spill on a roadway to have made the environment "impure, harmful or dangerous," while another person could consider it to have nothing to do with the environment. Accordingly, the court concluded that the pollution exclusion was fairly susceptible to more than one reasonable interpretation and, thus, ambiguous.

Finally, the court explained that, under Maryland law, a pollution exclusion bars coverage only in cases of "traditional environmental pollution." The court then concluded that a petroleum asphalt spill did not constitute "traditional environmental pollution" for at least three reasons. First, petroleum asphalt is not listed as a pollutant, contaminant or hazardous substance under CERCLA. Second, the petroleum asphalt spill did not impact the environment in the sense that it impacted a roadway rather than the water, land or air. Third, no suit had ever been brought under CERCLA or any other similar federal or state environmental statute in connection with the spill. Accordingly, the court determined that the pollution exclusion should not be interpreted to bar coverage, particularly where, as here, petroleum asphalt was being transported during the normal course of business operations for an asphalt trucking company.

Consequently, having determined that the pollution exclusion was ambiguous in its application to a petroleum asphalt roadway spill and also having determined that the proper scope of the pollution exclusion is to exclude coverage for "traditional environmental pollution," the court concluded that the pollution exclusion in the Hallmark policy must be construed against Hallmark. Thus, the court held that MTS was entitled to declaratory judgment, and Hallmark was required to defend and potentially indemnify MTS with respect to all claims resulting from the petroleum asphalt spill.

Implications

The scope and interpretation of pollution exclusions have been in dispute for decades, particularly in cases where the allegedly injurious substance is not viewed as a traditional environmental contaminant. While courts remain divided nationally on the application of pollution exclusions, particularly in nontraditional instances, *Travelers Indemnity* illustrates that even the so-called “absolute” pollution exclusion may not operate to bar coverage in every instance.

Travelers Indemnity also demonstrates that courts will consider the reasonable expectations of policyholders in interpreting insurance policies, including any applicable policy exclusions. To that end, if courts find that it is within the policyholder’s reasonable expectation that a substance is not a pollutant as that term is used in the insurance context, the pollution exclusion may be inapplicable and pose no hurdle to establishing coverage under general liability or excess liability policies.

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