



INTERNATIONAL INSURANCE BROKERS

CORPORATE HEADQUARTERS • NEW YORK, NY • TEL 212 432 1234
EASTERN REGIONAL OFFICE • MELVILLE, NY • TEL 516 228 1234
PERSONAL LINES CENTER • VALHALLA, NY • TEL 914 773 4321

THE INSURANCE NEWSLETTER

Winter 2014

Pollution

Probably the single most overlooked exposure facing almost any insurance buyer is that created by risk of loss from environmental impairment or contamination, i.e., “pollution”, in both property and liability policies. Most folks are aware by now that pollution is a standard exclusion in almost all insurance policies of any kind, but it’s worth looking a little more closely at what that means.

A little background: Up until the early 1970’s insurance policies generally did not contain pollution exclusions. The standard form of the Comprehensive (as it was then known) General Liability (CGL) policy, in particular, did not exclude claims arising from pollution. In recognition of the increasing public awareness of that time of environmental issues the Insurance Services Office 1973 CGL policy form revision incorporated for the first time a pollution exclusion, but only for gradual pollution; claims arising from “sudden and accidental” pollution were still covered.

Fast forward: the Comprehensive Environmental Response, Compensation, and Liability Act (CERCLA, commonly known as Superfund), was enacted by Congress in 1980. Among other things the law established requirements for closed and abandoned hazardous waste sites and established liability on the part of the originators of hazardous waste at these sites. As a result the previous trickle of pollution related lawsuits and claims against general liability policies soon became a flood. Insurance companies who had never foreseen these types of claims for long term or gradual pollution type events now were presented with huge pollution claims against policies that were often written decades in the past. While they found it difficult to deny coverage under old policies that lacked a pollution exclusion, insurers thought the exclusion against any but sudden and accidental type

claims added in 1973 gave them some protection against long term pollution type claims, while still providing policyholders with some important coverage.

Not for long, though. At the behest of policyholders looking for coverage lawyers and courts began to scrutinize the term “sudden and accidental” found in the 1973 CGL policy pollution exclusion. As is so often the case, words that seem clear enough to a layman were found to have layers of meaning when subjected to the scrutiny of the legal profession. An average person might look at the term “sudden and accidental” and reasonably conclude that meant something like a pipe suddenly rupturing or a tank bursting, but after years of litigation some courts managed to conclude that each and every drip from a leaky pipe full of contaminants was, in and of itself, a sudden and accidental event that triggered coverage. Not only that, but as these individual drips continued over a period of years (i.e., multiple policy periods) two or more sets of policy limits could be available to cover claims arising from these events as they continued over time.

It can often be hard to feel much sympathy for insurance companies, but there’s no question they drew the short straw here. They had tried to exclude coverage for gradual or long term pollution type claims while still offering their policyholders important coverage for sudden and accidental spills, but the lawyers did them in. The insurance industry reacted predictably; the 1985 CGL policy form revision introduced an “absolute pollution exclusion” in the new policy form. As a practical matter it’s effect was muted, because once they had seen which way the wind was blowing insurance companies had already started introducing total pollution exclusions as endorsements to all their policies.

These first exclusions were so broad that some coverage that policyholders might reasonably have expected to have was excluded, so over time some carvebacks to the total pollution exclusion in the CGL policy were introduced. The first one was an exception allowing pollution claims from a hostile fire (A hostile fire is one that occurs somewhere where it shouldn't be; basic example, your building catches fire.) Smoke and fumes from a hostile fire were carved out and covered as an exception to the total pollution exclusion.

Remember Legionnaires Disease? That was found to emanate from bacteria growing in heating and cooling ductwork. Again, policyholders might reasonably expect to be covered for claims of that type, so another exception, for claims arising from building heating and cooling equipment, was added.

Another example of coverage for a common type of pollution event is found in both the CGL and auto policy. Autos and mobile equipment by their nature carry around quantities of hazardous materials, such as fuel, lubricants, hydraulic fluids, etc. Such vehicles collide or overturn with predictable regularity, often causing spills of those pollutants. A carve back on these policies does provide coverage for spills of this type, unless the pollutant is being carried as a cargo.

But for most policyholders, that's about it. Any other claims arising from "Pollutants", defined as "any solid, liquid, gaseous or thermal irritant or contaminant, including smoke, vapor, soot, fumes, acids, alkalis, chemicals and waste" is excluded.

That's bad, but as bad as that sounds, it gets worse. Insurers now routinely add several other exclusionary endorsements to liability policies. For starters, even though the pollution exclusion built into the CGL policy is pretty broad, as often as not you'll still see a total pollution exclusion being added to policies; that takes away even the limited coverage exceptions mentioned above. You'll also usually find asbestos and silica exclusions; both are solid irritants and arguably covered in the wording of the pollution exclusion, but just to be sure the point is made, you'll see specific exclusions for both of these. The asbestos exclusion makes some sense, but the silica exclusion is a puzzler; silica is, after all, more commonly known by another name...sand.

The worst culprit by far, though, is the fungi or bacteria exclusion you'll find on almost every policy. Mold

claims had been percolating as a concern in the insurance industry for some time, but really came to the forefront after Hurricane Katrina in late August of 2005. Torrential downpours and widespread flooding left much of the Gulf coast wet. Mold is a natural consequence of moisture meeting up with modern building materials. Drywall in particular is a wonderful product and used in building construction almost everywhere, but along with its many useful properties it has one less attractive feature; its a natural food source for mold. Get drywall wet, mold will grow; as Katrina illustrated, get it wet in late summer in the South, with natural high temperatures and humidity, and mold will grow with amazing speed. Of course, there are a lot of ways that drywall can get wet other than the obvious peril of flood. Insurance companies, paying close attention to this, noticed how often relatively small property claims became very large claims once mold got involved, and decided they didn't want to have anything to do with that, so starting from around 2004-2006, fungi (a.k.a., mold) and bacteria exclusions became another fact of life in most property and liability policies.

This ramps up the severity of pollution exclusions by another order of magnitude. That's because the worst pollutant you're exposed to is also the most common: water. A nationally accredited standard development organization has created definitions for three categories of water, based on the range of contamination to be found in it. Category 1 water is that which comes from your faucet, potable, safe and sanitary. There is no problem with category 1 water, until it leaves the pipe or faucet. Category 2 and 3 water is water that is contaminated, the primary difference between them being that Category 3 contemplates contamination with fungi or bacteria where Category 2 does not. As a practical matter, in most situations water is either Category 1 or 3, and once Category 1 water contacts something other than a normal or appropriate container its assumed to have become contaminated and becomes Category 3.

Examples of Category 3 water include, by definition, sewage or toilet backflows; all forms of flooding, from seawater, accumulation of ground surface water or rising water from rivers or streams; and any other contaminated water entering the indoor environment. This last would include wind driven rain from weather related events, or even just a leaky roof. By this definition almost any water that is not in a sanitary water line is Category 3 water. Once water is Category 3 it becomes a pollutant, and if you have a fungi and bacteria exclusion in your policy you have no insurance.

Here's the wording of the standard exclusion in the CGL policy that does all the damage (italics added):

"This insurance does not apply to:

Fungi or Bacteria

a. "Bodily injury" or "property damage" which would not have occurred, in whole or in part, but for the actual, alleged or threatened inhalation of, ingestion of, *contact with, exposure to, existence of, or presence of*, any "fungi" or bacteria on or within a building or structure, including its contents, *regardless of whether any other cause, event, material or product contributed concurrently or in any sequence to such injury or damage"*

Pretty remarkable. Notice the last few lines, addressing what the insurance industry calls concurrent causation; what that is saying is if this exclusion can apply to any aspect of a claim, then even if other parts of the claim might have been otherwise covered, the *entire claim* is excluded. As a practical matter, since by definition Category 3 water has bacterial contamination, if something gets wet, your insurance disappears.

This is all relatively new stuff. As mentioned earlier the fungi and bacteria exclusion only started to see widespread use in CGL policies within the last ten years, and has flown pretty much below the radar screen for most policyholders since then. The definitions of water described above are still in a public comment stage prior to being finalized. Put them together, though, and the practical effect is to eliminate a lot of insurance that policyholders think they have. Whether that is in fact the intent of the insurance industry, whether these proposed definitions will achieve widespread recognition and acceptance, whether insurance company claim departments will interpret these exclusions so rigidly, whether any of this will survive the inevitable litigation and court challenges...answers to these questions all lie in the future.

Here's the point we want to leave you with. Pollution exclusions are found in virtually all policies these days; the definition of what is considered a pollutant goes far beyond what you would expect or what common sense would indicate, to the point where mundane substances like sand and water fall under that definition. Unless you are specifically buying an environmental insurance policy to cover pollution type claims, you should expect

that you have *no coverage in any policy for any claims* arising from pollution or contamination events.

If you are not comfortable with the way this uninsured exposure might affect you there is good news; solutions are available. The insurance industry is in the business of taking risk in return for a premium. All these pollution exclusions on policies exist not because underwriters are unwilling to cover these types of claims, they simply think that pollution insurance requires separate underwriting and policy forms. Coverage is readily available, there are a lot of insurance companies writing it, its usually reasonably priced, and we can help you with it. If you have any concerns or think you have a need, let's talk.

The Alternate Employer Endorsement

Businesses often depend on staffing companies or temp agencies to supply workers. From filling temporary staffing needs during busy times, temp to hire strategies and other needs, there can be many advantages to using these types of services. The contract between the staffing company and the client business typically will have a provision for workers' compensation insurance coverage, and its common to find the staffing company assuming the responsibility to provide this insurance.

You should be aware there is a potential downside to this type of arrangement for you as a client. Consider this scenario: you lease an employee from a staffing company. They are in your building, working for you and you are directing their activities, but their employer is in fact the staffing company, not you.

That employee suffers a work injury. Workers compensation benefits are properly paid by the staffing company's workers compensation insurance policy. However, the injured worker turns around and files a liability suit against you, alleging it was your negligence that caused or contributed to their injury. Injured workers like to do this when they can, and its a no lose situation for them; they get workers compensation benefits, but they also get a shot at the legal lottery.

This is a situation that's easy to imagine, and its a headache that's just as easy to avoid with a little forethought and planning. There is a little-known endorsement available for workers compensation insurance policies known as the "alternate employer endorsement" that can allow businesses who hire temporary workers to have coverage under the staffing company's workers' compensation

insurance policy. It extends primary coverage to employees of the named insured (the staffing company) while they are in the temporary or special employment of another company (you, the client business); it recognizes the client company as the alternate employer.

Workers compensation is intended to be the sole remedy in work injury situations. This endorsement brings that back, and can short circuit any effort by a temp worker to sue you as described. And because the alternate employer endorsement includes both workers compensation and employers liability, even if a suit should somehow find a way to proceed, you can look to the staffing company's policy to defend you, rather than your own policy.

The way it works is simple. You want the staffing company to agree they will provide workers compensation coverage for temp employees they send you; you also want them to have you specifically endorsed on their WC policy with the alternate employer endorsement. You'll want a copy of that endorsement for your records; you'll also want a hold harmless clause in your agreement with the staffing company.

You still need to maintain your own workers compensation policy, but with evidence in your possession of a properly written alternate employer endorsement from your staffing company you should be able to confidently turn to them to handle any work injury claims from the temp employees they supply.



INTERNATIONAL INSURANCE BROKERS

68 South Service Road
Melville, NY 11747-2357

PRESORTED STANDARD
US POSTAGE
PAID
PERMIT NO 231
WINSTON SALEM, NC