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The I.S.O. Pollution Exclusion: How Far Does It Go?

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Anyone involved in insurance dispute resolution will sooner or later come across an issue involving pollution exclusions. Most carriers—even those operating on a non-admitted basis—use the Insurance Services Office standard form. Typically, the conflict will be whether a cause of loss falls within the exclusionary language.

When these exclusions first evolved in the early 1970s, those active in the industry at the time will recall the two significant features addressed. The first was that damage from pollution was excluded unless it was sudden and accidental; second, the focus was on costs to remediate air, land or water damaged by the pollutants. Thus the intentional polluter who contaminated large land areas or streams over many years or habitually released noxious airborne chemicals would not have coverage for the costs of cleanup. Insurers soon found that the requirement for sudden and accidental was often given wide latitude in favor of coverage. The different terms adopted across the industry were gradually tightened and narrowed into more standard forms, ultimately resulting in a standard ISO form in 1985 with an absolute exclusion.

In responding to judicial interpretations supportive of coverage, the language became quite restrictive. Two key clauses are the definition of pollutants and the exclusionary terms:

> "Pollutants" mean any solid, liquid, gaseous or thermal irritant or contaminant, including smoke, vapor, soot, fumes, acids, alkalis, chemicals and waste. Waste includes materials to be recycled, reconditioned, or reclaimed.
>
> This insurance does not apply to:
> f. Pollution
> (1) "Bodily Injury" or "Property Damage" which would not have occurred in whole or in part but for the actual, alleged, or threatened discharge, dispersal, seepage, migration, release, or escape of "pollutants" at any time.

A literal reading of these two provisions would produce the following denials of coverage:

- A steam room at a health club malfunctions, resulting in higher than intended temperatures, causing burns to a patron. The steam is "thermal," since it is formed by the heating of water and "discharged" or "dispersed" from the steam opening.

- A contractor leaves scrap lumber and gravel on a sidewalk, causing a jogger to trip and suffer

injury. This could be deemed "waste" that was "dispersed."

- Peanut allergies have been in the news recently due to severe reactions by a few, mostly children. If a restaurant patron suffered allergic reaction from exposure to peanuts in a meal, the act of serving could be strictly interpreted as "dispersal" of a "solid."

These are obviously exaggerated examples, and hopefully no insurer would attempt to invoke the exclusion in these instances. The real question is: When does logic and rational analysis trump specific policy language?

This was addressed when the absolute pollution exclusion was proposed. In testimony before the Texas State Board of Insurance in 1985, industry officials representing ISO testified regarding the intent. In that hearing, Member David H. Thornberry asked:

My reading of that language is so broad that the example I have been given in the past, the grocery store where the alkali or acid spills on the floor, either through negligent failure to clean it up or negligence, the child walks in and falls in it, is disfigured. My reading of that exclusion is that's pollution excluded from the policy and there is no coverage. And that I guess is the correct reading.

In response, Wade Harrel, Director of Miscellaneous Liability for Liberty Mutual Insurance Company, testified in part:

That is a reading, yeah. It can be read that way, just as today's policy the pollution exclusion can be read in context with the rest of the policy to exclude any products liability claim. You can read today's CGL policy and say that if you insure a tank manufacturer whose tank is put in the ground and leaks, that that leak is a pollution loss. And the pollution exclusion if you read it literally would deny coverage for that. I don't know anybody that's reading the policy that way, and I think you can read the new policy just the way you read it. But our insureds would be at the State Board—someone said yesterday—quicker than a New York minute if, in fact, everytime a bottle of Clorox fell off a shelf at a grocery store and we denied the claim because it's a pollution loss.

Mr. Harrel's testimony continued:

We have overdrafted the exclusion. We'll tell you, we'll tell anybody else, we overdrafted it. But anything else puts us back where we are today. [1]

In the quarter century since that testimony, the intent, purpose and breadth of the exclusion has been tested and ruled on by courts in many jurisdictions. An interpretation regarding pollution from a leaking tank as described by Mr. Harrel would be quite surprising today. Pragmatically, this evolution from "overdrafting" and "I don't know anybody that's reading the policy that way" is not surprising. Adjusters and claim officers far removed from the 1970s and 80s will unsurprisingly look to the terms of the contract, without the historical perspective of the original purpose and intent.

A recent situation that generated notice in the press showed just how far some would like to take this coverage limitation. In a brief in a Houston federal court, Great American Insurance Company argued that deaths in a building fire resulted from smoke inhalation, which is a form of pollution, and not from the fire itself. According to an article in the *Houston Chronicle* on December 17, 2008, similar arguments had been made by insurers regarding fire deaths in Connecticut and for damages in grocery stores in a Kansas case.

Given the broad wording, combined with state and federal jurisdictions across the country dealing with countless individual circumstances, contradictions and

[1] Transcript of Proceedings, Hearing to Consider, Discuss, and Act on Commercial General Liability Policy Forms Filed by The Insurance Services Office, Inc. Volume III, Board Docket 1472, October 31, 1985, pages 7-10.

differing applications are virtually inevitable. In one instance, the California Supreme Court described competing interpretations:

> Although fragmentation of opinion defies strict categorization, courts are roughly divided into two camps. One camp maintains that the exclusion applies only to traditional environmental pollution into the air, water, and soil, but generally not to all injuries involving the negligent use or handling of toxic substances that occurs in the normal course of business. These courts generally find ambiguity in the wording of the pollution exclusion when it is applied to such negligence and interpret such ambiguity against the insurance company in favor of coverage. The other camp maintains that the clause applies equally to negligence involving toxic substances and traditional environmental pollution, and that the clause is as unambiguous in excluding the former as the latter. *MacKinnon v. Truck Ins. Exch.*, 3 Cal Rptr. 3d 228, 233 (Cal 2003).

According to *MacKinnon*, it would appear that the fate of any given policyholder would depend upon the particular camp into which its insurer chose to pitch a tent.

The argument regarding the historical genesis of environmental damage as the target of the exclusion was addressed in *Firemen's Ins. Co. v. Kline & Son Cement Repair, Inc.*, 474 F. Supp. 2d 779, 793 n.5 & 6 (E. D. Va. 2007). The court rejected this interpretation because "[n]owhere in the Policy is there any reference to the word 'environment,' 'environmental,' 'industrial' or any other limiting language suggesting the pollution exclusion is not equally applicable to both 'traditional' and indoor pollution scenarios."

As the original environmental focus of the 1970s becomes an ever more distant memory, the controversy can only be expected to continue. Exactly where the lines will be drawn between strict interpretation of the contract and realistic intent will continue to be debated. One could hope for practicality and reason rather than attempts to include deaths from smoke inhalation in a fire or the hypothetical burns from steam in a health club under the umbrella of pollution.

Perhaps a guiding principle could be reference to the initial objectives, motivation, and limitations in determining the balance between literal reading and reasonable purpose. In the meantime, the above examples show the considerable disparity among the courts.

In retrospect, it should not be surprising to see the contrasting interpretations when an industry executive testifies to a state insurance official that a term or clause is *overdrafted*. As with beauty and art, it would seem that what is overdrafted lies within the eyes of the beholder.

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