

Pollution and Intentional Loss Exclusion, Malicious Prosecution Insurance Coverage Update

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The e-POST

Pollution Exclusion – Fifth Circuit (Texas Law)

Eastern Concrete Materials, Inc. v. Ace Am. Ins. Co.

--- F.3d ---, 2020 WL 254822 (5th Cir. Jan. 17, 2020)

The U.S. Court of Appeals for the Fifth Circuit held that Great American Insurance Company (GAIC) had no duty to defend or indemnify Eastern Concrete Materials, Inc. (Eastern Concrete) in cleanup and other enforcement proceedings brought by New Jersey environmental regulators. Eastern Concrete owned and operated a rock quarry in Glen Gardner, New Jersey. One product of the quarry was a substance made up of small crushed rocks called rock fines. The rock fines were placed in designated ponds onsite to settle before being removed for sale or use as fill at the quarry.

In July 2017, a bout of heavy rainfall was expected at the quarry, so Eastern Concrete decided to lower the water level of the ponds in anticipation of flooding. In doing so, Eastern Concrete allowed "substantial amounts of rock fines" to enter a nearby stream. State environmental authorities determined the rock fines caused damage to fish habitats in the stream, increased flood risk in the area, and required remediation. Eastern Concrete sought coverage from GAIC under, among other policies, an umbrella policy issued to Eastern Concrete's parent company (GAIC Policy). GAIC commenced a declaratory judgment action, alleging that there was no coverage due to a pollution exclusion in the policy.

The district court found that the dispute should be decided under Texas law, rejecting Eastern Concrete's argument that New Jersey law should apply because the GAIC Policy was issued to Eastern Concrete's parent company in Texas. The district court also found that the pollution exclusion in the GAIC Policy applied to preclude coverage for the release of rock fines into the stream because the rock fines were "waste material generated in the rock-crushing process" that caused damage to the stream. According to the district court, the exclusion did not require the waste material to be an inherently harmful product such as a chemical in order to constitute a pollutant.

The appellate court affirmed the district court's decision on both the choice of law question and the applicability of the pollution exclusion. The appellate court determined that while the rock fines did not cause the water in the stream to become impure, "when we look at the effects on the overall

ecosystem, rock fines are contaminants.” The appellate court noted that both Eastern Concrete’s own expert and state authorities determined that the rock fines made the stream “‘unfit for use’ as a habitat for trout and other species,” which is why Eastern Concrete was required to remediate the rock fines contamination. The appellate court ultimately concluded that the rock fines were contaminants as contemplated by the pollution exclusion in the GAIC Policy such that GAIC had no duty to defend or indemnify Eastern Concrete.

Intentional Loss Exclusion – Massachusetts

Aquino v. United Prop. & Cas. Co.

--- N.E.3d ---, 2020 WL 289122 (Mass. Jan. 21, 2020)

The Massachusetts Supreme Judicial Court ruled that a United Property & Casualty Insurance Company (United) policyholder was entitled to partial coverage for the loss of her home, despite the fact that the home was lost in an intentional fire set by her fiancé, who was also an insured under the policy. The underlying case arose when Kelly Pastrana (Pastrana), the fiancé of policyholder Wenda Aquino (Aquino), intentionally set fire to their home following a domestic incident and subsequent gunfire exchange with police. Pastrana set the house on fire while inside, ultimately dying in the fire.

After the fire, Aquino sought coverage from United for the destruction of her home. United denied coverage under the policy’s intentional loss exclusion, which stated that if a policyholder deliberately caused a loss, no insured would be entitled to coverage. Aquino then sued United, asserting various claims, including breach of contract and bad faith. She also asked the court to reform the policy to make it conform with the state’s standard fire insurance policy, which does not allow an insurer to decline coverage for all insureds based solely on the intentional act of one insured.

The case went up to the Massachusetts Supreme Judicial Court, which affirmed the trial court’s ruling that United’s intentional loss exclusion was unenforceable. The court explained that “the standard fire insurance policy set by statute imposes several, rather than joint, rights and obligations on the insureds” and, therefore, United’s “redrafting of the statutorily defined policy language to make either insured responsible for the actions of the other in setting the fire was in violation of the statute.” The court concluded that Aquino was entitled to half of the insurance proceeds, the other half of which was forfeited by Pastrana’s actions, under the reformed policy.

Malicious Prosecution Coverage – California

Travelers Prop. Cas. Co. of Am. v. KLA-Tencor Corp.

No. H044890, 2020 WL 244200 (Cal. Ct. App. Jan. 16, 2020)

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The California Court of Appeals held that an insurer was not required to reimburse an insured for costs incurred in the defense of a patent antitrust lawsuit. In the underlying lawsuit, the insured, KLA-Tencor Corporation (KLA), was sued by a rival for allegedly obtaining a patent through fraudulent means. Specifically, it was alleged that KLA made fraudulent statements and failed to disclose material information to the U.S. Patent and Trademark Office (PTO) when it applied for a new patent for semiconductor measurement systems. KLA's insurer, Travelers Property Casualty Company of America (Travelers), denied coverage for the suit and, subsequently, filed a declaratory action in California state court, seeking a ruling of no coverage.

The trial court found that there was no coverage under KLA's policy with Travelers and granted summary judgment in favor of Travelers. KLA appealed and argued that coverage for the suit was available under the policy's coverage for malicious prosecution. The appellate court, however, rejected KLA's argument and ultimately held that the underlying suit did not allege malicious prosecution. Specifically, the appellate court noted that a claim of malicious prosecution is "commonly understood to be premised on actions in legal proceedings." The appellate court further noted that the underlying suit "arises from fraud on the PTO, not any court, and the use of a fraudulently procured patent to attempt to monopolize the market. Neither the fraud element nor the use element necessarily involves any legal proceedings." Therefore, the appellate court held that the policy did not provide coverage for the underlying suit.

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