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STATE OF LOUISIANA
ADVISORY LETTER NUMBER 97-01
June 4, 1997

LSA-R.S. 22:620 - 621
LSA-R.S. 22:1211 et seq.

TO: ALL PROPERTY & CASUALTY INSURERS

Re: Use of Standard Pollution Exclusions

INTRODUCTION

The Louisiana Department of Insurance (LDOI) has undertaken an extensive three year review of the use of standard pollution exclusions in various lines of Commercial Insurance.[1] This review has included the taking of two days of testimony from members of the insurance industry and the public. The Department also convened an eighteen-member Absolute Pollution Exclusion Task Force consisting of representatives from the insurance industry, industry trade associations, agent associations and policyholder associations and/or representatives. The Task Force has focused on two principle areas: (1) policy form language and (2) claims settlement practices.

Our review shows that standard pollution exclusions have been included in an extremely wide variety of policy forms.[2] These exclusions are inappropriate for many types of coverage and/or for certain classes within particular coverage lines. Many insureds do not present a pollution risk obviating the need for the broad exclusionary language found in standard pollution exclusions.[3]

Further, our review has disclosed a number of incidents where the standard pollution exclusions have been used to disavow coverage even though there was no underlying pollution incident which would

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[1] As used herein the phrase "standard pollution exclusions" encompasses both the original absolute pollution exclusion developed by ISO as well as its subsequent revisions and its progeny, including the total pollution exclusion and similar such exclusions developed independently by other insurers.

[2] For example, the LDOI received a form filing designed to provide errors & omissions coverage for small to mid-sized accounting firms which utilized the ISO absolute pollution exclusion. When the necessity for the exclusion was questioned the company chose to withdraw the form filing.

[3] The use of pollution exclusions in personal lines insurance policies is addressed in LDOI Directive 137 which was issued on June 28, 1996.

justify use of the exclusion.[4] We are also concerned that the broad definition given to the term "pollutant" creates an opportunity for abuse. This is a particular concern as regards commercial enterprises whose ongoing business activities do not present a risk to the environment. For example, we have found instances where it has been argued that any thing and/or matter that harms a person, whether or not it has toxic or hazardous properties, is de facto an irritant and therefore a pollutant, thereby triggering the pollution exclusion.

The appropriate use of standard pollution exclusions in claims handling is an issue of grave concern. The LDOI will take such action as is necessary to assure that the integrity of the regulatory process is not undermined. It is of critical importance that such exclusions are used in a manner which is consistent with their stated purpose.

After giving due consideration to other options, the LDOI believes that the issuance of this Advisory Letter is in the best interest of the insurance industry and policyholding public. The LDOI believes that the insurance industry will act in good faith and will adhere to the intent of this Advisory Letter thereby eliminating the need for further regulatory action.

STATUTORY AUTHORITY

LRS 22:620 prohibits the use of policy forms until they have been filed with and approved by the commissioner of insurance (COI). The purpose for "prior approval" is to protect the public. This section also gives the COI authority to withdraw approval at any time for cause.

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[4] The term "pollution incident" refers to an incident which causes "environmental damage". These terms are generally defined as follows:

> "Pollution incident" means emission, discharge, release, or escape of pollutants into or upon land, the atmosphere, or any watercourse or body of water provided that such emission, discharge, release or escape results in "environmental damage". Pollutants means any solid, liquid, gaseous or thermal irritant or contaminant, including smoke, vapor, soot, fumes, acids, alkalis, chemicals and waste.
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> "Environmental damage" means the injurious* presence in or upon the land, the atmosphere, or any watercourse or body of water of solid, liquid, gaseous or thermal contaminants, irritants, or pollutants. (*injurious to the environment, not the claimant.)

Under the forms designed to replace the coverage deleted by the Absolute Pollution Exclusion coverage was triggered only if the incident resulted in demonstrable "environmental damage". The exclusion should not be construed any broader than the forms designed to restore the deleted coverage.

LRS 22:621 provides the mandatory grounds for disapproval of policy forms by the COI. It calls for the disapproval of any policy, rider or endorsement or withdrawal of any previous approval if among other reasons, the policy contains exceptions and conditions which unreasonably affect the risk purported to be assumed in the general coverage of the contract.

LRS 22:1214(14)(a) and (n) make it an unfair claims settlement practice to misrepresent policy provisions relating to coverages at issue or to fail to provide a reasonable explanation in relation to the facts and law of the basis in the policy for the denial of a claim.

ADVISORY NOTICE

In view of the above, the LDOI is hereby advising insurers to take steps (1) to reduce the use of standard pollution exclusions in policy forms by adopting the new pollution exclusions developed and filed by ISO or by developing and filing their own new exclusions to tailor coverage to address the pollution risks actually posed; and (2) to assure that in the event of a denial of coverage there is a reasonable basis for the application of the policy's pollution exclusion.

Policy Forms

ISO has recently developed and filed for approval three new pollution exclusions. These new exclusions are designed to give underwriters more flexibility in tailoring coverage packages for policyholders which present at most a minimal pollution risk. And, ISO has also developed a revised absolute pollution exclusion designed to clarify the applicability of the exclusion to heating unit malfunctions. Because underwriters will not have to rely on the "one size fits all" standard pollution exclusions use of such exclusions will be carefully scrutinized during the policy form review approval process.

The LDOI strongly urges the insurance industry to continue to undertake efforts to develope additional endorsements and to devise more precise policy language to address the pollution risk.

Claims Settlement Practices

The parameters for a reasonable denial of coverage and/or refusal to provide a defense under a standard pollution exclusion, are set by (1) the regulatory record which establishes the stated purpose of the exclusion and (2) the dictates of the Louisiana Supreme Court found in South Central Bell v. Ka-jon Food Stores of Louisiana, Inc., 644 So.2d 357 (La. 1994).[5]

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[5] Followed in Bituminous Fire & Marine v Fontenot, 907 F.Supp. 193, 196 (M.D.La. 1995) and in In Re: Combustion, Inc., 94MDL4000 (W.D.La. 3/12/97).

Therefore, in handling claims the LDOI strongly advises insurers to consider the following in deciding whether or not a claim triggers a policy's pollution exclusion.

1) Does the claim involve an incident which caused an environmentally significant discharge of pollutants resulting in environmental damage?

2) Do the policyholder's regular business activities place it in the category of an "intentional active industrial polluter"?

3) Does the claim involve an injury alleged to have been caused by a product, including exposure to fumes, which was being used in accordance with its intended purpose?

4) Does the claim involve an injury alleged to have been caused by exposure to asbestos or lead?

If the answer is "NO" to (1) or (2) or "YES" to (3) or (4) of the above the denial of coverage and/or refusal to provide a defense may result in administrative action.

CONCLUSION

Although progress is being made important areas of concern remain. The LDOI plans to continue its work with industry representatives and other interested persons. It is hoped that this Advisory Letter will be of assistance to the industry in the development of resolutions to the dilemmas posed by pollution exposure.

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