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NEWSLETTER

Pollution Exclusion Bars Coverage for Suit Alleging Corporate Reorganization Designed to Avoid Paying Pollution Liabilities

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In an unreported decision, an Ohio appellate court has held that an insurer has no obligation to advance defense costs under a D&O policy to a policyholder alleged to have reorganized its business to avoid paying pollution-related liabilities because the policy's pollution exclusion bars coverage for these allegations.*Danis v. Great Am. Ins. Co.*, 2004 WL 2659132 (Ohio App. Nov. 19, 2004).

A third party alleged that the policyholder and certain of its directors and officers reorganized its business just before executing agreements to indemnify the third party for state-mandated environmental response costs arising out of the third party's operation of a landfill formerly operated by the policyholder's subsidiary. The reorganization allegedly left the policyholder without sufficient assets to satisfy its obligations. When the policyholder demanded defense costs under its directors, officers, insured entity and employment practices liability policy, the insurer denied coverage based on the policy's pollution exclusion. That exclusion barred coverage for any claim "based upon, arising out of, relating to, directly or indirectly resulting from, in consequence of, or in any way involving actual or alleged seepage, pollution, radiation, emission or contamination of any kind." Coverage litigation ensued.

The appellate court held that because the original pollution and related indemnity agreements were a necessary predicate for the third party's claim, that claim was "based upon, arising out of, relating to, directly or indirectly resulting from, in consequence of, or in any way involving ...pollution" for purposes of the policy's pollution exclusion and therefore excluded from coverage. The court rejected the company's argument that the claim by the third party was independent of any pollution. The court pointed to a prior decision in *U.S.F. & G. v. St. Elizabeth Medical Center*, 716 N.E.2d 1201 (Ohio App. 1998), in which the court held that a preliminary or concurrent act contributing to a loss is independent of an excluded cause only where the act: (1) can provide the basis for a cause of action in and of itself, and (2) does not require the occurrence of the excluded risk to make it actionable. The court found that the alleged business torts were not "independent causes of loss" because absent the excluded risk (pollution), the third party would have no grounds for a claim against the policyholder or its directors and officers.

The appellate court additionally found that the words "directly or indirectly" in the pollution exclusion indicated that an indirect causal relationship is sufficient for the exclusion to apply. The court thus held coverage for the third party's claims could be independently excluded as matters "indirectly related to ...pollution."

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