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Pennsylvania Court OKs Dismissal of $21 Million Judgment in Insurance Case

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The Pennsylvania Superior Court did not err when it overturned a $21 million judgment notwithstanding the verdict and set new standards for interpreting the known-loss doctrine, a divided state supreme court has ruled.

In the opinion announcing judgment of the court in *Rohm & Haas Co. v. Continental Casualty Co*., Chief Justice John P. Flaherty set the standard for known losses in Pennsylvania.

"We agree ... with the Superior Court's conclusion that the standard for the known-loss defense in this case should be 'whether the evidence shows that the insured was charged with knowledge which reasonably shows that it was, or should [have been], aware of a likely exposure to losses which would reach the level of coverage,' " Flaherty wrote.

The issue of the known-loss doctrine is one of first impression in Pennsylvania.

Justice Russell M. Nigro concurred in the decision. Justice Ronald D. Castille filed a lengthy dissent, in which he rebuked Flaherty's rationale.

"In summary, the majority not only has erroneously decided the three issues on this appeal, but, what is more troubling, in the process has summarily approved unwise expansions of extra-contractual defenses that will result in the unforeseeable forfeiture of otherwise legitimately bargained-for coverage in countless other cases," Castille wrote.

Justices Ralph J. Cappy and Thomas Saylor joined Castille in his dissent.

The case has been on the radar screen for many organizations for years now. Amici in the case included the Insurance Environmental Litigation Association, United Policyholders, Pennsylvania Chemical Industry Council, the Pennsylvania Chamber of Business and Industry, both the Philadelphia and Pittsburgh chambers of commerce, the Pennsylvania Trial Lawyers Association, Pennsylvania Environmental Council and a number of businesses, including Bethlehem Steel Corp. and Crown Cork & Seal.

Rohm & Haas had asked the high court to affirm Philadelphia Common Pleas Court Judge Paul L. Jaffe's decision ordering a number of insurers to indemnify the company for costs of cleaning up a Superfund site.

A Philadelphia County jury found in favor of the insurance companies, but Jaffe granted Rohm & Haas' motion for a directed verdict after a nonjury trial as to damages, awarding Rohm & Haas $21 million in damages for past expenses and a share of future cleanup costs.

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On appeal, the Superior Court reversed Jaffe's decision and, with a lengthy opinion, reinstated the jury's verdict. Rohm & Haas then appealed to the Pennsylvania Supreme Court.

John G. Harkins of Harkins Cunningham argued the case before the high court on behalf of Rohm & Haas. Jerome J. Shestack of Wolf Block Schorr & Solis-Cohen in Philadelphia argued on behalf of the insurers.

"I think one of the aspects of the opinion that I consider very beneficial is that it encourages openness and candor between the insured and insurer," Shestack said in a phone interview last Friday.

Shestack had no comment on Castille's dissent.

Harkins did not return a call seeking comment Friday afternoon.

WHITMOYER SITE

In 1964, Rohm & Haas bought Whitmoyer Laboratories Inc., a veterinary feedstock and pharmaceutical company located in Lebanon County. Soon after buying the property, Rohm & Haas realized that Whitmoyer had been dumping arsenic waste on the land since 1957, which contaminated soil and groundwater in the surrounding area.

Rohm & Haas conducted tests on water samples in 1964 and realized that arsenic levels in the wells for several surrounding off-site houses were very high.

In January 1965, F.O. Haas, chief executive officer of Rohm & Haas, ordered that the problem be solved and informed the commonwealth of the problem. The company began a cleanup program, supplied bottled water to nearby residences and settled the claims of some people who became sick.

In December 1964, Rohm & Haas had included that site under already existing liability policies with its insurers, retroactive from its purchase date.

Rohm & Haas informed its primary liability insurer and its insurance broker of the problem with the Whitmoyer site; they were in turn "free to pass that information on to the excess insurers." But the excess insurers claimed there was an effort to keep them from learning about the Whitmoyer problem.

The "excess" policies in question were comprehensive general liability policies intended to provide additional coverage beyond Rohm & Haas' primary insurance. The excess insurance policies provided that the companies indemnify Rohm & Haas for "liability to third parties above certain substantial thresholds, ranging from $500,000 to $40 million."

Rohm & Haas began a cleanup of the site in 1965. Throughout the cleanup process, Rohm & Haas continued to buy liability insurance from other insurance companies without voluntarily telling the insurers about the environmental pollution problem on the site. The company did not seek reimbursement for cleanup costs from the insurers.

Rohm & Haas sold the site to SmithKline Beecham in 1978. In 1980, Congress enacted the Comprehensive Environmental Response and Liability Act, and in 1986 the EPA informed Rohm & Haas that it would be liable for cleanup costs of the site under the stricter CERCLA standards.

In 1988, Rohm & Haas went to its insurers seeking coverage for the additional CERCLA-required cleanup. The insurers denied coverage, and Rohm & Haas sued them for indemnification.

After a nine-week trial, the jury decided that the insurers had no duty to indemnify Rohm & Haas because the company did not inform the insurers of the environmental problem on the site.

But Jaffe granted the plaintiff's motion for a J.N.O.V. and began a nonjury trial to determine damages, after which he found in favor of Rohm & Haas and granted $21,031,352 in compensation.

However, on appeal, the Superior Court said Jaffe was wrong to direct the verdict, ruling that there was sufficient evidence for a jury to decide whether Rohm & Haas had a duty to disclose information about the Whitmoyer site to the excess insurers. The jury said Rohm & Haas did indeed have that duty.

The opinion announcing judgment of the court from the state's highest court concurred with the Superior Court's decision reinstating the jury's findings.

KNOWN-LOSS DOCTRINE

Flaherty said that while the known-loss doctrine has not been formally adopted in Pennsylvania, the high court has long required insurance applicants to make a full and fair disclosure of items material to insurable risk.

Rohm & Haas had argued that the court should apply a narrow construction of the doctrine which would require "the existence of certain knowledge of a particular legal liability large enough to reach the excess layers of insurance at the time of contracting."

The insurers, however, urged the court to adopt a broad construction of the doctrine, one where "an insured's mere awareness of a substantial probability of liability large enough to reach the excess layers of insurance at the time of contracting is sufficient to satisfy the requirements of the doctrine."

Without really expanding on the Superior Court's rationale, the supreme court opted for the latter, more broad construction of the known-loss doctrine.

Flaherty said, therefore, that the standard for the known-loss defense should be whether the evidence showed that the insured had knowledge which reasonably showed that it was, or should have been, aware of a likely exposure to losses sufficient enough to reach the level of excess coverage.

The court said Rohm & Haas would lose even if the court were to adopt the more narrow version of the doctrine because there was sufficient evidence provided at trial for the jury to conclude the way it did.

OTHER ISSUES

Flaherty next turned to examining two other issues on appeal: whether the J.N.O.V. was properly granted with respect to the insurers' defense of fraud and whether the J.N.O.V. was properly granted with respect to the insurers' defense of late notice.

After examining evidence presented at trial, Flaherty concluded that there was sufficient evidence provided for the jury to conclude in the insurers' favor. Flaherty said the high court would not re-examine evidence and substitute its findings for those of the jury.

"The jury determined that at the times that Whitmoyer was added to existing policies or included in newly purchased policies Rohm & Haas deliberately withheld information it knew would be material to the insurers' decision to provide coverage," Flaherty wrote.

As for the late notice issue, Flaherty said there were material issues of fact that should have been presented to the jury with regard to whether the insurers were prejudiced by the decades of time elapsed between the acquisition of the Whitmoyer site and the claim for coverage.

Therefore, the court concluded, the Superior Court was correct in its ruling "in all respects."

Nigro filed a separate concurrence, asserting that he agreed with Flaherty as to the fraud claim, but did not believe the court had to delve into the known loss and late notice claims.

DISSENT

In his dissent, Castille said he did not believe that Rohm & Haas' failure to volunteer information the insurers never requested should result in a forfeiture of coverage.

Castille said he disagreed with Flaherty's view of the known-loss doctrine.

"There is no requirement under this formulation that the insured have knowledge of an existing legal liability to a third party, which is the actual risk being insured against in this sort of coverage," Castille wrote. "Instead, the majority focuses on mere 'losses,' and then requires only a 'likelihood' of exposure to the level of coverage."

"The majority does not explain why it embraces these multiple vacillations to undo the parties' agreement, rather than reasoning from our actual experience with fraud cases in the insurance area."

Castille called Flaherty's opinion a "radical change in the law" and a misapprehension of "the very nature of third party liability insurance."

"The peril being insured against by the policies here was not the certain arsenic damage at the Whitmoyer site, but rather the attenuated risk of third party legal liability -- here for government-ordered remediation of the contamination -- later arising ex post facto from that pollution," Castille wrote. "That loss, and its catastrophic extent, was not at all

'known' or knowable at the time these policies were issued."

Castille also said Flaherty's decision was an "unprecedented loosening of the fraud standard" and also disagreed with Flaherty's take on the late notice issue. Castille said he believed the directed verdict was the appropriate measure.