insurer refused to defend. The manufacturer settled the claim for the pump explosion, in part, by assigning its rights against the excess coverage insurer to the plaintiff. The plaintiff sued the excess coverage insurer to recover on a claim of bad faith failure to defend.

On appeal, the court held that the excess coverage insurer was not required to defend the manufacturer despite the provision in the insurance contract. The court concluded that requiring the insurer to defend when the primary insurer became insolvent would shift a new risk of the primary carrier's insolvency to the excess coverage insurer. The court felt that shift would have two undesired effects. First, it would frustrate the provision of low cost excess coverage. Second, it would unduly complicate the insurance transaction by requiring the excess coverage insurer to investigate the solvency of the primary insurer. Since the excess coverage insurer had no duty to defend, it could not be liable for bad faith in its decision to withhold a defense for the manufacturer.

Damages for Bad Faith Failure to Settle Claim

Frankenmuth Mutual Insurance Co. v. Keeley, 1989 Mich. Lexis 2358 (Mich. S. Ct. 1989).

The Michigan Supreme Court concluded that an insurer's damages for a bad faith failure to settle a claim is not limited by its insured's ability to pay damages in excess of the policy limits. The insured party, Keeley, fired a gun at Boone, leaving Boone a quadriplegic. Boone offered to settle the claim for the $50,000 policy limit, but Frankenmuth, the insurer, refused. Boone then received a judgment against Keeley for $250,000. In a separate suit concerning Frankenmuth's duty to defend Keeley, Keeley counterclaimed alleging a bad faith failure to settle the claim within the policy limits. The court held that Frankenmuth had a duty to defend Keeley and that the insurer had breached its duty to settle the claim. The trial and appellate courts, however, limited Keeley's damages to the amount of Keeley's assets that would be available to pay Boone. The Michigan Supreme Court reversed.

The supreme court noted a split of authority concerning the proper amount of damages when the insured is not able to pay the amount of the excess judgment. On the one hand, a minority of courts have concluded that the insured is not damaged if the award is limited to the amount that he would have to pay absent any bad faith on the part of the insurer. These courts, therefore, held that the insurer is liable only when the insured has paid or could pay an amount more than the policy limits. The majority of courts, however, have concluded that the insurer's duty of good faith does not permit it to derive a windfall depending on the solvency of its insured. In these cases, the insurer was liable for the full amount of the excess judgment if it failed to settle in bad faith.

In this case, the court adopted the majority rule of full liability for two reasons. First, it felt the majority rule better promoted the use of good faith on the part of the insurer. Second, the court noted that the bad faith of the insurer resulted in other real injuries to the insured, such as injury to reputation and credit, forced bankruptcy, and the likelihood of garnishment, that could be avoided by using the majority rule.

Defense of Administrative Action against Insured

Avondale Industries, Inc. v. Travelers Indemnity Co., 887 F.2d 1200 (2d Cir. 1989).

The Second Circuit Court of Appeals concluded that an insurer was obligated to defend the insured in an administrative action that could result in liability for pollution cleanup costs. Avondale serviced ships and barges and removed oil from them. It sold the oil to a salvage company which recycled it. The salvage company's recycling plant and dump became the source of both private and administrative actions against Avondale. Avondale demanded that Travelers defend the actions based on its policy which included a duty to defend the insured against "any suit . . . seeking damages." Travelers sought to avoid the defense of the administrative action on the basis that it was not a suit for damages within the meaning of the policy.

The court of appeals rejected Travelers' argument. The court first found that the administrative procedure initiated against Avondale was a suit. The parties to the administrative action for the cleanup (the state and Avondale) were adverse to one another because the state demanded that Avondale take charge of the cleanup or be liable for the costs. Second, the court concluded that the action was one for damages. The cleanup costs were a form of restoration of a third party and, therefore, amounted to damages. Further, the court noted that the provision for defense of the insured should be viewed from the perspective of the ordinary business person. In that view, the insured would expect to receive a defense under these circumstances.

Pollution Liability Exclusion Applies to Inherited Problem

Powers Chemco Inc. v. Federal Insurance Co., 1989 N.Y. Lexis 3216 (N.Y. Ct. App. 1989).

New York's highest court affirmed an appellate division decision that concluded that a passive owner of a pollution cleanup site cannot look to its insurance carrier for financial assistance. Powers purchased land that contained hazardous wastes. The state ordered Powers to decontaminate and restore the property. Powers sought a declaratory order that the costs of the cleanup were within the terms of its general comprehensive liability insurance. Although the policy covered most events, it contained a provision that excluded pollution costs. The only exception to the pollution clause was for sudden and accidental events. The court concluded that the prior owner's intentional discharge onto the property was not accidental within the meaning of the policy. The court also rejected the argument that the exclusion did not apply because Powers did not cause the pollution. The court stated there was nothing in the language of the clause to suggest that it did not apply if the cause of the pollution was the act of a third party.