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Recent Court Decisions

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All Named Insureds Must Receive Adequate Notice of Cancellation or Policy Remains in Effect

Olivine Corporation v. United Capitol Insurance Co., 52 P.3d 494 (Washington Supreme Court—August 22, 2002)

Olivine Corporation owned and operated a waste incineration site. In 1997, it executed a lease-purchase agreement with Clearwater Resource Recovery, Inc. Under the arrangement, Clearwater was to lease the facility and eventually acquire it as an owner-operator. The lease agreement also required Clearwater to obtain pollution liability coverage. Clearwater purchased a one-year claims-made policy from United Capitol with an effective date of October 27, 1997. Initially, Olivine was an "additional named insured," but in early 1998, the policy language was changed to make both Clearwater and Olivine "named insureds." *See* 52 P.3d at 495-496.

Clearwater paid for the policy through a premium financing arrangement with TEPCO Premium Finance, LLC. As part of this process, TEPCO obtained a power of attorney from Clearwater that permitted TEPCO to cancel the policy should Clearwater fail to make payments on the premium financed. TEPCO had no similar arrangement with Olivine, the other named insured and the owner of the property covered under the policy. *See* 52 P.3d at 496.

Sure enough, Clearwater defaulted on its payments to TEPCO, which acted to cancel the policy, sending notice of intent to cancel to Clearwater—but not to Olivine. Clearwater did not respond to the notice (and did not pay the amount claimed). Clearwater cancelled the policy effective February 17, 1998, without notifying Olivine. *See* 52 P.3d at 496.

Less than a month later, Olivine was notified by the County Health Department that it would be required to clean up hazardous waste and toxic substances at the facility. Apparently, Clearwater was no more proficient at pollution control than it had been at premium payment and had "allowed the leachate tanks to fill and overflow, and had left ash and tires piled at the site." *See* 52 P.3d at 496.

The news got progressively worse for Olivine. Clearwater had also dumped the incinerator ash on a disallowed site, causing an inspection by the Washington State Department of Ecology. Because of Clearwater's operation of the incinerator, Olivine's

solid waste handling permit was eventually revoked. Olivine notified United Capitol of the health department's claim and requested that United Capitol pay for the cleanup costs. When United Capitol initially indicated that the claim was covered, Olivine began arranging to have the site cleaned up in early April. However, on May 19, 1998, United Capitol informed Olivine the policy had been canceled effective February 17, 1998. 52 P.3d at 496.

Olivine responded by suing for coverage—and won, eventually obtaining $434,300 in damages (presumably the cleanup costs it paid) and $40,000 in counsel fees incurred in prosecuting the coverage action (although it had claimed actual attorney fees of $144,000). The Court of Appeals affirmed, as did the Washington Supreme Court.

The Supreme Court recognized that premium financier TEPCO had a valid power of attorney vis-à-vis Clearwater. However, TEPCO had no such prerogative regarding Olivine. Thus, United Capitol as pollution liability insurer was required to give notice of cancellation to Olivine as a named insured under the policy. *See* 52 P.3d at 497-499. However, where there is a single policyholder, the Court suggested that the premium finance company's power of attorney would be sufficient to support its cancellation prerogatives, a result in keeping with other cases in which there was only one policyholder. *See* 52 P.3d at 499-501 (citing cases).

STATE EMPLOYER'S ACCEPTANCE OF LATE ENROLLMENT OF EMPLOYEE WITH CATASTROPHIC LOSS SITUATION NOT A BREACH OF GOOD FAITH AND DOES NOT ENTITLE GROUP HEALTH INSURER TO RESCISSION

Primary Health Network v. State of Idaho Department of Administration, 137 Idaho 663, 52 P.3d 307 (Idaho Supreme Court—June 7, 2002)

In most insurance coverage litigation involving allegations of bad faith, the policyholder makes the accusations. The tables were turned a bit—but not successfully—in the *Primary Health Network* case in that the insurer was arguing that the employer holding a group policy acted in bad faith by accepting an employee's late enrollment. The Idaho Supreme Court rejected the insurer's contention and consequently denied rescission of the agreement and the return of payments sought by the insurer.

Like most employers, the State of Idaho has a group health insurance program that provides for periodic "open enrollment" periods during which an employee may join the plan or change coverage. Idaho had an open enrollment from April 21, 1997, to May 21, 1997. Employee Penney Huffman never received notice of the open enrollment period during the period, apparently because she had been away from the workplace at that time. As a result, the state accepted her late enrollment on a form dated June 27, 1997, and forwarded it to group insurer Premier Health.

Premier Health was not thrilled about the late enrollment, but they accepted it after investigation, even knowing that Huffman was the mother of a seriously ill child (Julianne Prudhomme) who would require a great deal of medical care. Premier Health paid approximately $1 million to medical providers for treatment accorded the child. Two years later, it sought records from the state and subsequently asserted claims of breach of contract, mistake/reformation, business compulsion, negligence, and violation of 42 U.S.C. § 1983, a federal civil rights statute. The insurer contended

that Idaho had acted in bad faith by shoehorning Huffman into the group policy and sought rescission of the coverage and repayment of the funds paid on her behalf.

The Idaho Supreme Court unanimously rejected all of the Premier Health contentions, largely because it found the insurer to have accepted Huffman's late enrollment with open eyes. The state had not misrepresented the situation surrounding the late enrollment or the grave medical problems facing the child. Thus, although the language of the group health policy set firm deadlines for enrollment, the insurer was bound by the decision it made to accept the late enrollment even though it could have asserted its rights against late registrants under the contract. *See* 52 P.3d at 310-311. Consequently, there was no mutual mistake that might permit rescission. *See* 52 P.3d at 311-312.

The Court further found that the state had not acted in bad faith and had not unduly pressured or coerced the insurer into acceptance of the Huffman risk. *See* 52 P.3d at 312. Similarly, the Court also rejected the insurer's far-fetched claim that the state had deprived it of a constitutional property right. *See* 52 P.3d at 313.

CORROBORATIVE EVIDENCE REQUIREMENT IN PHANTOM DRIVER AUTOMOBILE CLAIM VIOLATES STATE STATUTE AND IS READ OUT OF POLICY

Walker v. GuideOne Specialty Mutual Insurance Co., 834 So.2d 769 (Alabama Supreme Court—May 10, 2002)

Laura Walker purchased an automobile policy from GuideOne that provided coverage pursuant to the underinsured motorist (UM) provisions of the policy but only also provided that if

> there is no physical contact with the hit-and-run vehicle the facts of the accident must be proved. We [the insurer] only accept competent evidence other than the testimony of a person making [a] claim under this or similar coverage.

834 So.2d at 770.

Walker was severely injured and her husband killed when her car swerved to avoid an oncoming car, left the road, and crashed into a tree, consuming her vehicle in fire. The other vehicle sped on and was never located. Walker was the only surviving witness to the accident. Consequently, when Walker sought UM coverage under her policy, the insurer refused, citing the corroboration requirement of the policy.

The Alabama Supreme Court upheld Walker's claim, finding that the policy's corroboration requirement was at odds with Alabama Code Section 32-7-23, which requires mandatory UM coverage in place of the liability coverage to which the policyholder would have been "legally entitled" had the negligent driver possessed auto insurance. Walker successfully argued that the corroborating evidence provision of the GuideOne policy operated to deny her coverage to which she was "legally entitled" (on the strength of her uncontested testimony) and therefore was in violation of the statute. 834 So.2d at 771-772.

The Alabama Supreme Court agreed that the policy language operated in the nature of an impermissible exclusion and was more than merely a standard of proof set forth

in the policy. According to the Court, it was an exclusion more restrictive than the UM statute and was therefore void and unenforceable. 834 So.2d at 772.

In reaching its decision, the *Walker v. Guide One* Court disagreed with federal court precedent applying Alabama law and with some state court decisions that had concluded that corroborating evidence provisions were enforceable and merely regulated the standard of proof rather than operating to impermissibly narrow coverage beneath the statutory minimum. *See, e.g., Moreno v. Nationwide Insurance Co.*, 114 F.3d 168 (11th Cir. 1997) (applying Alabama law) and *Hannon v. Scottsdale Ins. Co.*, 736 So.2d 616 (Ala. Civ. App. 1999). Precedents such as *Moreno* and *Hannon* now appear no longer to be good law, with *Hannon* specifically overruled. Because *Moreno* was a federal case, the Alabama Supreme Court could not overrule it but could only disapprove of the decision.

PHYSICAL CONTACT REQUIREMENT UPHELD IN PHANTOM DRIVER AUTOMOBILE CLAIM

Wold v. Progressive Preferred Insurance Co., 52 P.3d 155 (Alaska Supreme Court—August 2, 2002)

In contrast to the *Walker* decision in Alabama, the insurer in *Wold* was faced with a slightly different issue in a phantom driver claim (a physical contact requirement versus a requirement of corroborating evidence of a phantom driver accident in the absence of physical contact). In addition, the insurer had the benefit of a different state statute, one that required physical contact for a valid "hit-and-run" driver claim. Using this statute as its model for policy language, Progressive Preferred issued a policy that required physical contact for coverage of a hit-and-run accident.

The rationale for the physical contact requirement (like the corroborating evidence requirement) is that hit-and-run or phantom driver claims are subject to fabrication by policyholders who are injured in accidents due to their own negligence rather than that of a third party tortfeasor. By requiring physical contact, the insurer has some check on the veracity of the policyholder's claim. Even though the phantom driver cannot be located, the evidence of physical contact serves to corroborate the policyholder's claim.

In the absence of such a requirement clearly stated in the policy, policyholders have tended to prevail in the courts and obtain coverage on the strength of their individual testimony, as in *Walker v. GuideOne.* Even where there is policy language requiring physical contact, policyholders may prevail, as did Walker, by arguing that such a policy provision is inconsistent with the state's statutory UM scheme, unreasonably favorable to the insurer, or in violation of the insurer's reasonable expectations of coverage.

Consequently, insurers have urged legislatures to enact physical contact requirements in their UM statutes and have been successful in many states, as in Alaska. With such a statute in place (Alaska Statute 28.20.445(f)) and similar policy language, the insurer was able to defeat Wold's claim of UM coverage due to an accident involving a phantom driver. *See* 52 P.3d at 158-161.

However, in another, more complex portion of the case, Wold prevailed when the Supreme Court held that the policy limits of liability coverage for the policyholder

driver (plaintiff Wold was a passenger in the driver's car, which left the road and rolled after confrontation with the phantom vehicle) were exhausted through settlement of claims, making it likely on remand that Wold will be permitted to prove additional damages covered under the UM provisions of the policy in question. *See* 52 P.3d at 161-164.

EXCLUDED DRIVER/HOUSEHOLD EXCLUSION ENFORCED EVEN AFTER EXCLUDED DRIVER NO LONGER A RESIDENT OF THE POLICYHOLDER'S HOUSEHOLD

Williams v. Watson, 798 So.2d 55 (Louisiana Supreme Court—October 16, 2001)

Defendant Watson purchased an automobile insurance policy in April 1995. In order to reduce her premium based on having no unmarried driver under age 25 regularly use the vehicle, she accepted an endorsement that stated the following:

> I authorize the person(s) listed below to be excluded from my insurance policy: THIS MEANS THAT NONE OF THE COVERAGE AFFORDED BY THE POLICY WILL APPLY TO ANY DAMAGES, LOSSES, OR CLAIMS OF ANY PERSON OR ORGANIZATION CAUSED WHILE ANY MOTOR VEHICLE IS BEING USED OR OPERATED BY THE EXCLUDED DRIVERS(S) LISTED BELOW EXCEPT AS PROVIDES IN THE FOLLOWING PARAGRAPH. This exclusion applies regardless of any provision in the auto policy defining Insured Persons.
>
> NAME OF EXCLUDED DRIVERS(S)
>
> Name: DONALD WATSON
>
> Date of Birth: 1/31/78
>
> Relationship to the Insured: CHILD

See 798 So.2d at 56.

In October 1995, Donald Watson was using a leased vehicle rented by his mother while her car was being repaired. He struck another car from behind, resulting in suit by the victim (Jodi Williams) against Watson. Watson sought coverage under the State Farm policy issued to his mother in April 1995 (Watson had not purchased insurance specifically for the rental vehicle, so there was no additional insurance potentially applicable beyond her regular auto insurance). *See* 798 So.2d at 56.

State Farm denied coverage, citing the exclusion. Watson argued that the named driver exclusion was no longer applicable since it had been based upon his residing at home at the time the policy was procured. Since then, Watson had moved in with his girlfriend and was no longer a member of the policyholder's household.

The Louisiana Supreme Court rejected Watson's argument and held that the language of the exclusion was clear and clearly named Watson as an excluded driver. Even though Watson was no longer a member of the policyholder's household, he was still Donald Watson, a person not covered as a driver under his mother's automobile policy. Even if the rationale for excluding him had been his prior residence, the lan-

guage of the policy did not exclude him as a member of the household—it excluded him, period. *See* 798 So.2d at 58-59.

In its decision, the *Watson* Court resolved a split among the intermediate appellate courts in Louisiana and disapproved or overruled precedent that had accepted Watson's argument for coverage.

OKLAHOMA SUPREME COURT GIVES BROAD CONSTRUCTION TO ABSOLUTE POLLUTION EXCLUSION IN CGL POLICY

Bituminous Casualty Corp. v. Cowen Construction, Inc., 53 P.3d 34 (Oklahoma Supreme Court—April 30, 2002)

State supreme court decisions continue to trickle in regarding the construction of the absolute or total pollution exclusion contained in the standard commercial general liability (CGL) policy. The "total" pollution exclusion is distinguished from the "absolute" pollution exclusion in that the total exclusion contains an express exception for smoke from a hostile fire, thereby creating express coverage for this type of loss and ensuring that the exclusion will not negate traditional fire coverage. Oklahoma has now gone on record as favoring a broad approach to the exclusion that does not limit the exclusion to instances where the alleged injury and liability stem from environmental pollution.

Cowen Construction was sued when patients at the kidney dialysis center of the St. John Medical Center Hospital in Tulsa, Oklahoma, suffered lead poisoning, allegedly because Cowen's work has negligently permitted leached lead to percolate through the venting system of the hospital. The federal court in which suit was brought certified the following question to the Oklahoma Supreme Court:

> Under Oklahoma law, is the scope of the total pollution exclusion of a commercial general liability policy limited to "environmental pollution?"

55 P.3d at 1031.

The Court answered the question in the negative and thus, finding coverage seemingly precluded on the facts of the case, declined to answer another certified question regarding trigger of coverage under Oklahoma law. The Court did not go so far as to adjudicate coverage, however, and noted that in answering a certified question, its role was limited, both because the actual case to be adjudicated was located in a federal court and because the state supreme court usually does not possess the full factual record necessary to decide cases with finality. According to the Oklahoma Supreme Court:

> Because the case from which the certified question emanates is not before us for resolution, we refrain (1) from applying the declared state-law response to the facts elicited in the federal-court litigation and (2) from passing on the effect of federal procedure on the issues, facts and proof in the case. We have briefly outlined the case's factual underpinnings to place the certified questions in a proper perspective. It is for the United States District Court

> of the Northern District of Oklahoma to analyze our answer's impact on the case and facts ultimately before it.

55 P.3d at 1032-1033 (footnote omitted).

In deciding that the pollution exclusion was not limited to environmental pollution, the Court found that the language on its face was clear and that a court would be going beyond the language in affixing an outdoor or environmental pollution requirement for the exclusion to be effective. For that reason, the *Cowen Construction* Court was unwilling to consider the reasonable expectations of the policyholder. Under Oklahoma law, reasonable expectations analysis is done by a court only if the policy language at issue is ambiguous. *See Max True Plastering Co. v. U.S. Fidelity & Guaranty Co.*, 912 P.2d 861, 869 (Okla. 1996). The Court also noted the strong divergence among the states as to the apt approach to the pollution exclusion. *See* 55 P.3d at 1035.

However, consistent with its minimalist approach to answering certified questions, the *Cowen Construction* Court noted that there was no record before it by which questions of party conduct, party intent, or extrinsic evidence might be considered.

> The certified question in the federal declaratory action presented to us is bare of any evidence of the parties' intent other than as embodied in the language used in the policy and further is devoid of any factual record relative to approval of the policy's language by the Oklahoma State Insurance Commissioner. Hence, we have considered the insurance provision in issue by analysis focused upon the language employed by the parties in their contract.

55 P.3d at 1035.