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of a medical nature would be responded to appropriately. Finally, it enabled defendants to close out future claims and extricate themselves from litigation.

Advantages of Trust Funds

Defense counsel should consider seriously the possibility of setting up medical trust funds, similar to that used in Love Canal, before personal injury claims reach trial. This form of structured settlement offers potential advantages to both sides and to the court. From the plaintiff's perspective, the structured settlement involves a trade-off between a certain settlement, which provides a reliable source of funds to defray actual out-of-pocket economic losses, and the uncertain possibility of a larger, lump-sum judgment. The structured settlement also greatly accelerates the payment to the injured party and potentially reduces large legal costs associated with protracted litigation. The defendant benefits from: increasing the probability of earlier, cheaper settlements; reducing uncertainties of litigation outcomes; eliminating the negative operational problems associated with large, pending liability cases; and contributing to the public's perception of its social responsibility. In hazardous substances litigation, a reasonable trust fund structure may be the best route to avoid bankruptcy or "bet the company" litigation.

Other inherent advantages of the structured settlement include overall reduction in legal fees, correlation of payouts with actual damage cost expenditures, and benefits of position that this type of solution can provide in pretrial negotiations.

The structured settlement is also likely to receive support from the judiciary in hazardous substances and other types of tort liability actions. Judges are interested in solutions that provide guaranteed compensation to victims and that are designed to meet their medical and economic needs as they arise. The structured settlement is an effective mechanism to compensate plaintiffs and dispose of cases efficiently, without clogging court calendars with expensive, drawn-out "battle of the experts" trials.

Structured settlements are most appropriate when there is great risk that the defendant will lose, or where even a victory would leave the defendant with a social pariah image. This is true particularly when liability may be clear, and the only questions remaining for trial concern the size to the judgment, and the time when final appeals will be exhausted. Under such circumstances, the defendant must weigh the probability of losing, the potential magnitude of award, pre-judgment and post-judgment interest, and date of final judgment, against factors such as the smaller, but certain, cost of a structured settlement and the benefits of the payment structure. The defendant can evaluate both options on a discounted cash flow basis, as well as from corporate policy and public relations perspectives.

The medical trust fund can also be used, in advance of any claim situation, to indemnify against potentially risky projects and to ameliorate "not in my backyard" concerns. For example, in locating hazardous waste disposal facilities, a trust fund could be established by the owner at the time the facility is built. Studies can be conducted to identify in advance the potential exposure and to estimate the potential costs of that exposure. An annuity can then be purchased and constructed to provide cash flow sufficient to meet the costs of any potential toxic exposures. The annuity can be used both to reduce community anxiety and to negotiate a limit on the legal liability of the facility owner.

The trust fund program can be fashioned from a variety of options. The richer the choices, the greater the degree of tort liability waiver a defendant would receive. For example, a program offering only medical expense reimbursement might lead only to a waiver of the collateral source rule. By contrast, a program that covered not only expenses but also pain and suffering, might lead to a complete tort waiver. This pain and suffering component could bear similarities to specific disease life insurance policies.

Cleanup Structures

The trust fund established by a structured settlement is also an appropriate means of paying claims in environmental cleanup cases. In theory, contributions to the annuity fund can be obtained from each defendant in some measure proportional to that defendant's responsibility for the damages. This would be attractive to the "deep pockets" client, who could otherwise be saddled with the entire settlement under the theory of joint and several liability. It could also appeal to the smaller client who, as a member of the "de minimis" group, may not have the resources to fund an expensive legal defense. The Environmental Protection Agency, and its state counterparts, should favor the annuity structure, because it provides a stable, reliable funding source independent of the continued financial viability of the defendants.

This solution will not let the major potentially responsible parties (PRPs) "off the hook," since they may face future liability if the cleanup is not successful, or if its cost runs over budget. To some extent, however, by funding above projected costs — a so-called "premium" — it may be possible, even for major PRPs, to negotiate a more favorable settlement or to enter into a limited covenant not to sue. In "de minimis" cases, it should be possible to use the structured fund to "cash out" and to obtain a full covenant not to sue as allowed under current law.

A fund based on a structured settlement will provide some dis-

tance between the PRP and the ongoing cleanup activities, improve the company's public image, decrease costs, and close out the contingency exposure item from corporate financial statements and SEC disclosures. The latter feature should be especially appealing, as it will simplify financial audits and could increase the company's allure to risk-averse investors.

The Role of Insurance Expertise

The insurance expert carries out several roles in the structured settlement process. First, the expert can play an effective role as a member of the defense's negotiating team, presenting the structured settlement as an option to the plaintiffs or the EPA. Second, since the annuity-backed structured settlement is designed to provide a cash flow tailored to the medical or economic requirements of the plaintiffs, actuarial services are needed to cost out and structure the fund. Third, the claims-handling mechanism must be designed, initiated, and monitored. Fourth, insurance skills are required to place the annuities advantageously within the investment community. In addition, in cleanup actions, insurance professionals must be involved to determine program costs and cash flow requirements, to arbitrate with the steering committee so as to establish the contribution levels of each defendant, and to coordinate with the EPA to obtain approval for the project.

Hurdles to Using Structured Settlements

The structured settlement procedure raises several problems defense counsel needs to consider. First, the negotiations may be quite lengthy, especially when there are multiple defendants and "hot" issues, such as Superfund. On the other hand, these are just the types of cases that also are most likely to continue for long periods within the court system. Second, under current tax treatment, the defendants will be allowed to write off contributions to the fund in the year they are made, rather than when fund payouts occur. This question is currently being considered by the IRS. Third, structured settlements should be pursued only where liability is clear — when injuries can be linked unambiguously to a given site or product, and where the epidemiology of the toxic exposure and injury is soundly established.

Some observers have objected to the structured settlement procedure, on the grounds that they undermine the judicial goal of deterrence. But these critics ignore the fact that, since the settlement cost remains substantial, the deterrent value remains as well, and the earlier and more predictable settlement amount is likely to increase the deterrent value. The structured settlement closely approximate the concept of social insurance that many commentators and courts have suggested in philosophical discussions of tort liability.

Conclusion

Structured settlements appear to offer significant promise in personal injury actions based on exposure to toxic substances. They provide potential benefits to both plaintiffs and defendants, and offer the possibility of reducing judicial costs and delays. In appropriate circumstances, the defense should consider the possibility of establishing trust funds for payment of justifiable claims.

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"TOXICS: TOO RISKY TO INSURE? - YES, NO, MAYBE SO"

AMERICAN BAR ASSOCIATION INSTITUTE
ON POLLUTION LIABILITY: STRATEGIES FOR
MANAGING THE COMBINED CHALLENGES
OF SUPERFUND AND TOXIC TORT CLAIMS
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INTRODUCTION

This paper addresses the question of whether toxics are insurable. Today, there is a sense that toxic exposures may be too risky for insurance to cover. The newness of the term "toxic tort" itself causes some uncertainty and ambiguity. We can speculate that if a prominent liability law school professor were asked in 1975, "what is a toxic tort?", the answer might well have been "a poisonous cake."

These days, it would be hard to find a lawyer who could not answer the question in some way that reflects the uncertainty and critical nature of these exposures. For purposes of this discussion, "toxics" will hold the broadest possible definition, since, traditionally, insurance has responded to a wide variety of liabilities.

In this paper, we will discuss liability for events arising from toxic exposures through common law actions and through special statutory creations. The inquiry will be to find whether it is possible to insure parties for liabilities arising from injuries and property damage caused by toxic substances regardless of whether those liabilities are found under the common law of torts or whether they arise from statutory frameworks such as the federal Superfund. Both liabilities are growing, but the statutory variety is leading the way and has seen more litigation.

MAGNITUDE OF THE PROBLEM

The American public has become all too aware of these liabilities in recent years. From newspaper, television and radio coverage Agent Orange and other major bodily injury cases--including Bhopal, Love Canal, asbestos injuries--have entered our collective conscience, the major among these liabilities involves the statute that is known as the federal "Superfund" or "CERCLA".[1]

The size and scope of these liabilities is without precedent in the liability system and in the insurance world. Reportedly, asbestos liabilities have consumed between $1 billion and $3 billion and one company. The Agent Orange settlement was in excess of $180 million. It is reasonable to anticipate that Bhopal's costs will reach the hundreds of millions. Some of the environmental clean-ups arising under the federal Superfund may involve costs in the billion-dollar range.

The Rand Institute for Civil Justice reports that experts agree that there were about 16,000 asbestos-worker injury claims in 1981 costing approximately $1 billion. Five years later, there were more than 30,000 asbestos cases in state and federal courts. Also, in 1981, there were an estimated 7,500 lawsuits pending over injuries from Dalkon Shields. By 1986, after A.H. Robins had sought protection under Chapter 11, more than 325,000 claims had been submitted to the bankruptcy court.[2,3]

Costs associated with liabilities arising from environmental clean-ups under the federal and state Superfund laws are even greater. Settlement of the Rocky Mountain Arsenal site, one of the nation's most contaminated toxic-waste sites, is reportedly in the $1 billion range. Of that sum, it is expected that Shell Oil Company will pay slightly less than one-half. The clean-up is expected to last until the year 2000.[4]

An interesting secondary aspect of this particular settlement is the litigation concerning insurance coverage. The coverage dispute involves a minimum of 120 lawyers and will take place in a building that has been redesigned at a cost of $350,000 paid for by the litigants, in order to accommodate litigation of this size and scope.[5]

It is not just the cost of individual clean-up sites that is a problem, but the cost of the average clean-up and the number of sites that might come within the environmental clean-up program. One EPA official has reported that the EPA's current estimate of $21 million per site may be somewhat low and that the average cost may be $30 million for each action.[6]

There is much squabbling about the number of sites that may need clean-up. A January 1988 report from the General Accounting Office finds that the number of potential Superfund sites may be 425,380. Interestingly, this number is up from the 378,000 estimated by the GAO in 1985. The EPA has derived numbers that

are considerably lower than the GAO Report, and has been adding approximately 2,000 sites per year to its list of sites that need to be studied. As of October 31, 1987, the EPA had conducted preliminary investigations at some 24,000 sites.[7]

CONDITION OF INSURERS

The economic state of the insurance industry has improved considerably over its disastrous state in 1984 and 1985. Experts estimate that the property and casualty insurance industry as a whole should register net after-tax income of $13.7 billion in 1987, a relatively modest increase over the $12.8 billion of net income recorded in 1986. These figures reflect an industry that despite continued improvement, still exhibits a rate of return of only 13.2%, which is below the average 15.4% rate of return reported by Standard & Poors 400 companies. By contrast insurers' underwriting returns show marked improvement. The overall combined ratio for 1987 is expected to hit 104.7, making it the best year since 1980.

This means that liability premiums and losses are approaching equilibrium. Part of the problem, however, is that toxic exposures fall within general liability. Although the general liability combined ratio has improved it remains a substantial loser, at 115.5. This is better than the ratio of 150 in the recent past, but is nevertheless a substantial distance from sound underwriting profit or even underwriting stability.[8]

These data reflect the insurance industry's inability to predict what losses will occur. There is academic support for the proposition that some components of the general liability line are extremely difficult to predict and that they are expanding and expensive. Some legal commentators have noted the substantial distinction between torts that are described as "routine" and those that are "salient". Salient torts are those for which the system has yet to develop a reasonable predictable methodology for their resolution.[9] The Rand Institute for Civil Justice has attempted to look at the distinctions between routine and salient tort litigation. Its conclusions are that auto accident cases, among the routine, are at a steady or declining percentage of court actions. Non-auto personal injury cases, such as medical malpractice and product liability, are growing moderately in state courts and more dramatically in federal courts. The outlook for toxic exposures is that mass latent injury cases have the potential for explosive growth as new evidence of harms develops.[10]

For insurers, the decision to insure toxic exposures must be based upon the experience of the past as well as a review of available evidence of the likely outcomes in the future. This attempt to determine the nature and extent of past and future exposures proves difficult in toxics. The Rand study substantiates the belief of many observers that there already are significant losses in the pipeline and the future does not indicate amelioration.

Insurance brokers do see insurance availability improving with generally enhanced competitiveness, but coverage for toxic exposure remains extremely difficult to locate. For the moment, it would appear that the insurance industry's financial improvement and increased capacity will manifest itself in increased availability of insurance for more routine exposures. Insurers are cognizant of the enormous exposure that exists in toxic liability and the potential if it were safe to underwrite it, for vast premium and associated profits. The difficulty is to find those areas of toxic exposure which are stable, equitable and predictable. Insurers must also be able to assure themselves that their willingness to venture forward will not be transformed by Congress or the courts and expanded into a vast new catastrophe.

PROBLEMS OF UNDERWRITING

In order to provide insurance coverage underwriting is necessary. The art of underwriting is not a process of avoiding all loss. To the extent that it is possible to avoid all loss insurance is not necessary. An insurance company that places its assets at risk must be knowledgeable about the liability system involved and be able to make reasonable predictions about how often and of what size payments will be required. After all, the financial security of an entire company may be exposed.

In the toxic liability area, underwriting difficulties go beyond its unparalleled magnitude. The liability system, its operations and what causes harm and what is harm--are in substantial flux and, therefore, present grave difficulties for the underwriter. This uncertainty, together with the continuing prospect of legal and scientific change, make the underwriter fearful of providing coverage.

In the environmental area, the magnitude and uncertainties are such that by providing real coverage, the financial security of an entire insurer may be exposed. As we will see later, there are some instances in which the combination of science, law, and social policy is sufficiently stable and may warrant some return of the market.

In the U.S. harmful substances and hazardous activities are well publicized. It is a rare day newspapers do not report exposures or new evidence of injurious associations with products and substances. There is a sense that we live in a contaminated world. The case is rarely made and less frequently acknowledged that "toxic" substances may, in fact, be less harmful than otherwise thought or that we may be overreacting.[11] Thus, the dioxin exposure incident in 1976 at Seveso, Italy, received much publicity in the U.S. and Europe, while the recently released study showing that the dioxin was not found to increase birth defects was left to relative obscurity.[12] Recently, the EPA's report that dioxin is 16 times less hazardous than previously

thought has been the subject of considerable contempt from some in the environmental community.[13] The Doll & Peto study, which made quantitative estimates concerning avoidable risks of cancer, has been similarly attacked, for it proposed that while environmental exposures are significant they are not quite so frightening as is generally believed. [14] One recent study attempted to provide some methodology for balancing potential risks from various substances. It noted, for example, that of 35 wells shut down in Santa Clara Valley because of supposed pollution hazard only two appear to have human exposure dose/rodent potential dose (HERPs) higher than that of ordinary chlorinated tap water. The study also reported that even water from the most contaminated of the wells was several orders of magnitude less for its HERPs value than beer or wine.[15]

Uncertainty also is reflected in perceptions of the relationship between natural and manmade substances and their harmfulness. It is only recently apparent that this dichotomy is misleading as to the characteristics of the substances and as to their harmful potential.[16]

Courts as well as scientists are rountinely grappling with the problems of harmfulness and causation. A disturbing trend from the point of view of those who might be looking toward providing insurance is the increased use of various forms of marginal science to overcome difficulties in proving causation. "Clinical ecology" is a "science" offering broad support for causation in

bodily injury cases, but the science has been repudiated by many in the medical establishmentand cited as an example of poor science flourishing in the courtroom. [17]

The problems confronted by an underwriter that provides coverage for environmental exposures for bodily injury or clean-up arise whether or not the science is valid. The existence of the potential for what is sometimes called "junk science" or the use of medically suspect experts is only one aspect of the problem. An underwriter providing insurance for a producer of a substance is never going to have more knowledge than the best scientific evidence available at the time that the product is underwritten. If there is a change in the state of science or a discovery with regard to toxicity occurring after the date of underwriting, the underwriter will be bound if there is no state-of-the-art defense. It is unreasonable to expect an underwriter to have even that degree of knowledge for all potentially harmful products that exist in the United States even if there were not a substantial degree of scientific controversy.

The underwriter is faced with two extremely difficult problems: the continuing development of the state of scientific knowledge and the possibility that large bodily injury rewards may be based upon what is either minority or junk scientific evidence. The state of science that determines the harmfulless of products is a fundamental variable for which there is little stability.

Another scientific variable in the environmental area is how one accomplishes clean-up. The disputes over how to accomplish clean-ups occupied volumes of debate in the Superfund reauthorization process of 1984, 1985, and 1986. It is known as the "how clean is clean" issue. The difference in estimates on how clean-up might be accomplished and how much it may cost reflected in the EPA's estimate of $16 to $22 billion versus the Office of Technologic Assessment's estimate of $100 billion.[18] These assessments both were made before the completion of the Superfund Amendments and Reauthorization Act of 1986 (SARA); various estimates indicate that the cost of clean-up after SARA may be three to five times the preamendment estimate.[19]

LEGAL ASPECTS OF THE PROBLEM

While the characteristics of environmental exposures enumerated above would certainly seem daunting, there was a relatively modest and experimental insurance market for a brief period of time following development of RCRA's* insurance requirements. This market was predicated, in part, on a generalized perception that CERCLA would not be as Draconian as it proved to be. Even in the Environmental Protection Agency some, conceded that in the early days the exact nature of the Superfund liability system was

* Resource Conservation and Recovery Act 1976

unclear.[20] The development of case law under Superfund in the 1980s dispelled any illusions as to its insurability. The scientific and technical difficulties involved in estimating the potential for liability--the major impediment to the development of an insurance market--haunt the liability system developed under CERCLA, together with some additional legal problems involving insurance coverage and bodily-injury cases.

As a liability system developed to provide funding for past clean-ups on a highly punitive basis and without regard to fault, insurers became unable to categorize or assess the risks they might be bearing. Unable to underwrite, they were unable to provide a insurance market. Traditional insurance policies do not distinguish between the types of damages underwritten. A policy that might provide coverage for bodily injury might also be subjected to liability systems intended to provide clean-up costs.

The business of insurance is a collective risk transfer or risk-funding mechanism which, when done through the commercial industry, requires assessment of each individual risk and of the total risk. For most situations involving toxic exposures, it is impossible to develop proper individual or collective risk assessment because the variables are too great and the opportunities to isolate the individual insured no longer exist. The scientific problems discussed before remain a major variable. The most awesome prospect, however, is entering into field that

features retroactive, joint and several, and strict liability and compounding them with insurance coverage interpretation problems.

Joint liability is the first impediment to individual risk assessment because an individual insured with limited responsibility and no wrongdoing may be selected to bear enormous liabilities, wholly out of proportion with the conduct of the insured. A risk assessor who has reviewed the activities and conduct of a particular insured and found them to be exemplary cannot develop a premium reflecting that fact because the insured may become entangled in litigation involving actors whose conduct may be less desirable, but whose financial status is insufficient to bear the liability burdens that confront them.

Jeffrey Matz, lead counsel for the plaintiffs in the McColl dump site bodily-injury and property damage litigation, offers an example of the operation of joint and several liability.

> "One example from McColl involves not only the question of joint and several liability, but the question of good faith settlement as well. The State of California originally offered $25,000 to extricate itself from the case. The only possible theory of liability against the state involved a 1954 letter to the California Water Resources Board, which remotely referred to the presence of the McColl dump site. There was no evidence that the state had ever authorized the dumping or that they participated in the operation of the

dump site or the approval, design, construction or sale of the homes to the plaintiffs. Besides the weak theory of liability, we also seem to be stuck in the quagmire of governmental immunities. So the plaintiffs were satisfied with $25,000 in full and final settlement with the state. But when the state moved for a finding that the settlement was entered in good faith, the court denied the motion because the sum was inadequate. Ultimately, California paid $300,000, the motion for good faith settlement was approved and the case against the state was settled."[21]

Statutory liability under Superfund most clearly exemplifies the difficulty in providing insurance for toxic exposures. It is here that the courts have crafted a retroactive[22] system of joint and several [23] and strict liability.[24] There is also a punitive aspect associated with these pollution exposures. At the conclusion of the trial court portion of the longest-running civil liability trial in United States history, a jury awarded $1 to each claimant for compensatory damages against Monsanto Corporation and went a step further by awarding over $16 million in punitive damages. [25] A trial court dealing with a small-garage owner, who had a limited understanding of legal procedures, and who had been illegally depositing used oils in a hole in the back of his yard, decided appropriate punishment constituted a $37 million fine! [26] That should teach him a lesson.

Carrying retroactive liability to the extreme, the Justice Department has initiated litigation against the Pennsylvania Railroad, which was discharged from its bankruptcy in 1978, for environmental disposal practices prior to that date. These liabilities are to be imposed under Superfund and according to the Justice Department the intent of Congress was that clean-up shall take precedence over the pre-CERCLA settlements arrived at by bankruptcy procedures. [27] In a case involving dioxin exposure, a court has decided that a discovery rule will apply, allowing suit brought in 1985 for a decedant's death from a kidney cancer in 1976.[28] One wonders if causes of action for all of the potential toxic exposures yet to be discovered, but which caused deaths at any time within this century, will follow this ruling.

There are advocates of procedural modifications to deal with the difficulties plaintiffs face in proving individual causation. Thus, the creative use of class actions coupled with "probability of causation" as a method of distributing injury costs are gaining support among some in the academic community.[29] Even the nature of damages for toxic exposures threatens to undergo considerable expansion, so that bodily injury cases may include recoveries for the fear created by exposure to substances.[30]

Insurers are undoubtedly aware that as in the statutory program for clean-up liability, there remains the possibility that a federal cause of action for bodily injuries also might be established by Congress, subject to the same retroactive joint and

strict liability regime that characterizes the Superfund. In the Second Session of the 98th Congress, Representative Florio introduced a bill which would have created precisely such a scheme. It would have required that a plaintiff show that there was an injury, even including fear, that there was exposure to a hazardous substance, and that the defendant was responsible for the presence of the hazardous substance. The defendant then would be allowed to demonstrate that the injuries were not the result of that exposure. This legislation was narrowly defeated in the House of Representatives and never advanced to the Senate. Nevertheless, it stands as a daunting scenario for any insurer that becomes involved with toxic exposures. [31]

JUDICIAL CONSTRUCTION OF INSURANCE POLICIES

The final hurdle insurers confront is the difficulties that arises in determinating the meaning of insurance policy language. The courts have taken a seemingly schizophrenic approach to the resolution of disputes between insurers and insureds. [32]

The most dangerous exposure for insurers is a public policy-based interpretation of the insurance contract. This is most clearly exemplified in the Summit vs. Liberty Mutual Insurance Company case. In that case, a trial court construing the "owned property exclusion" determined that even though the policy language was clear, unambiguous, and applied to the facts, the court would find coverage for the insured because of a public

policy in the State of New Jersey in favor of cleaning up the environment. The court reasoned further that if clean-up costs were not borne by insurers, then they would fall upon taxpayers. The New Jersey Appellate Division reversed this portion of the trial courts ruling saying "while public policy as expressed in our statutes may have set the stage for Summit's claim, it cannot alter clear provisions of a contract between the parties".[33] Although reversed the trial court's reasoning represents a theoretical approach to determinating insurance contract interpretation that can chill future insurance activity.

It is worth noting that the cost of determining insurance coverage through litigation in and of itself constitutes a major expenditure. The trial of the Shell Oil Company coverage dispute with its numerous insurers is but a single example. Not only has that case involved the use of some 120 lawyers from major law firms and expenses for computer usage, but the number of exhibits and similar trappings of mega-litigation are on a comparable scale.[34]

The stakes behind such litigation are monumental. The publicity of these mega-suits is, in part, responsible for the SEC consideration of whether such liabilities should appear in corporate annual filings. The Wall Street Journal discussed the relationship between these exposures and SEC disclosure in an article titled "Can $100 billion have no material affect on balance sheets?".[35]

The judicial interpretation of insurance policies applicable to toxic and pollution exposures is fraught with uncertainty. Cases readily can be found to support whatever proposition a party may desire. The subject of the litigation involves construction of numerous important contract clauses; the most uncertain involve pollution damage. There is a similar field of litigation covering toxic exposures for products such as asbestos.

The primary dispute is whether there is coverage under general liability policies at all. The secondary area of dispute is if there is such coverage, then how much. The major litigation experience has been concerned with the general liability policy's "pollution exclusion." With slight variations, this clause generally reads as follows:

> "This insurance does not apply...(f) to bodily injury or property damage arising out of the discharge, dispersal, release, or escape of smoke, vapors, soot, fumes, acids, alkalis, toxic chemicals, liquids or gases, waste materials or other irritants, contaminants or pollutants into or upon land, the atmosphere, or any water course or body of water; but this exclusion does not apply if such discharge, dispersal, release or escape is sudden and accidental."

It is on the meaning of "sudden" that the courts have had contrary results.

One line of reasoning is that "sudden" is a word meaning unexpected. If "sudden" means unexpected, then the entire inquiry as to whether coverage exists comes down to the question of whether the event was unexpected. Courts are not bound by temporal considerations such as the length of time during which ground may have been permeated. [36] The opposite line of reasoning is well exemplified in Claussen vs. Aetna Casualty & Insurance Company. The court construed the word "sudden" to have a temporal meaning and refused coverage for an event occurred over a substantial period of time. The court said, "Only in the minds of hypercreative lawyers could the word [sudden] be stripped of its essential temporal attributes." In discussing supporting authorities for the non-temporal interpretations, the court said, "It is sometimes appropriate to point out that the emperor has no clothes." [37]

In the Shell Oil coverage case, Judge Lanum reached several important conclusions in April of this year.[38] He held that traditional rules of insurance policy interpretation, which arose from the apparent unequal bargaining power favoring insurers and requiring construction of ambiguities in favor of insureds, were inappropriate for Shell. The court in passing did level some critisism at the Superfund noting that CERCLA "is an inartfully drawn and ill conceived piece of Federal legislation with many provisions of questionable constitutional validity." Judge Lanum

found that clean-up costs could constitute insured damages. In the same court before Judge John J. Bible insurers meet with a better result on this issue when in the Aerojet decision Judge Bible ruled for insurers that such costs were not damages within the meaning of the insurance policy.[39]

The second fundamental coverage issue is whether covered damage has occurred. The most important area of litigation arises in the Superfund context. The question is whether environmental clean-up costs which are sought by an agency through equity actions for enforcement of administrative orders constitute "damages," as required under an insurance policy. The courts differ on whether damages must be monetary. If insurers are successful in sustaining the position that "damages " do not include clean-up costs then they will be able to avoid substantial exposure under Superfund. This may last only until such time as the government chooses to restructure the form in which it makes its claims for these costs. The case law on this is very recent and is sharply divided. The position taken in Maryland Casualty Co. v. Armco, Inc. and in Continental Insurance Companies v. NEPACCO support the proposition that there is no covered damage, whereas New Castle County v Hartford Accident & Indemnity in New Jersey and U.S. Aviex Co. v. Travelers Insurance Co. in Michigan arrive at the opposite conclusion.[40]

Insurers' optimism after their victories is reflected in a statement by the American Insurance Association President, who said:

> "Insurance companies did not agree to accept hazardous waste generators' burdens of complying with environmental requirements, did not charge premiums for that risk, and entered into contracts that clearly did not cover this kind of expense. Two federal appeals courts have confirmed those conclusions. We believe the issue should now properly be regarded as settled." [41]

Most insurers are probably not as sanguine as this statement would indicate. They may be fearful of the contrary line of state cases.

The other remaining issue of major impact in practically every environmental exposure case is the question of what an occurrence is and when it happens. Generally speaking, insurance policies provide coverage for damages that result from an occurrence during the policy period. An occurrence is usually defined along the following lines:

> "Occurrence - an accident including continuous or repeated exposure to conditions which result in bodily injury or property damage neither expected nor intended from the standpoint of the insured."

The issue in latent injury cases becomes which insurance policy will provide coverage for events that fall within the definition of damages under the policy. This has arisen in several contexts the most thoroughly litigated of which were the asbestos cases.

These cases divided insurers as they sought to locate coverage within policy periods provided by other carriers. The theoretical periods of time during which coverage might have been afforded to an insured were those periods during which the injured party was exposed to asbestos fibers ("exposure"); those periods during which the injured party had fibers located in the lung tissue ("residence"); and that period of time at which asbestos injury became diagnosable ("manifestation"). Chronological decisions by the Courts adopted positions which generally expanded coverage. The most recent cases have shown an inclination to establish a triple trigger of coverage. This means that coverage will apply under a policy held by the insured during any period of time during which there was either exposure or fibers in residence or manifestation of injury.[42] One case adopted a triple-trigger approach to asbestos property damage cases.[43] An asbestos defendant sued by a building owner could receive coverage under all policies held during the time when there was asbestos in the building.

A similar question arises where recovery is sought for environmental pollution. As in the asbestos cases, where the courts forged an ever-broadening theory of coverage, the courts started

out granting coverage for all periods during which permeation from the site occurred.[44] However, in 1986, with Abex v. Maryland Casualty [45] and again in Mraz v. Canadian Universal Insurance Co.[46] new rules were promulgated for these kinds of environmental exposures. In the Abex case, which dealt with bodily injury from landfill exposure, the court adopted an "injury in fact" theory. In the Mraz case, the court adopted a theory for property damages akin to a manifestation theory. There the court held that leakage that occurred in 1969, but was not discovered until 1981, would not be covered by any policy but a 1981 policy. This decision, if followed elsewhere, would significantly reduce losses for insurers since later policies tend to more explicitly exclude environmental clean-up and pollution exposures. Therefore, if the damage or leaking becomes manifest during a period when the exclusion is more clearly worded, the court may enforce the exclusion and deny coverage.

FUTURE PROSPECTS FOR INSURED - INSURER ACTIVITY

Unfortunately, the future prospects for participation by commercial insurers in the area of toxic exposures remains limited. The uncertainties associated with the development of toxic tort liability as to the time, nature of exposure, and the amount of liability make it generally more attractive for insurers to place their capacity in other lines and at the disposal of other liabilities. In addition, concern by commercial insurers because of past exposures, particularly under Superfund, gives some

wariness about the state of their surplus and, therefore, their ability to provide insurance. There does appear to be a newly competitive insurance market, however, as insurers have repaired their capacity, and it is possible that the future will see some return of coverage for toxics.

The opportunity remains for generating enormous premium. If circumstances of stability are created or found, the market may well return. Some insurers, limited in number, have shown a willingness to participate in the market today. Their underwriting is careful and the coverage tends to be fairly limited. Nevertheless, they are demonstrating the kind of imagination that provides customers with the coverage they need. These insurers are in the process of creating new products designed to meet today's needs.[47]

There are a number of developments in self-insurance pools, trusts, and individual captives with some external risk-sharing. Risk- funding is becoming very important in the environmental area. The development of either risk-transfer or funding depends upon a number of imaginative efforts by risk managers and insurance people, as well as the managements of the protected entities.

One of the threshold issues that must be addressed by any program of insurance or self-insurance is the stability of the terms of policy coverage. It may be said that the uncertainty in judicial

policy interpretation benefits neither insurers nor insureds in the long run. The interpretation of policy language will always involve the inherent limitations of linquistic precision and the incentives for courts to make determinations that maximize coverage.

There is reason to believe, however, that as a body of law is developed that establishes specific consensus meanings for policy terms that apply to toxic exposures, it may be possible to use the varied decisions to develop a more stable and certain contract. In addition, the opportunity for participants in pools to develop their own language is significant and is by its very nature less susceptible to claims of "contract of adhesion." If the people insured are the same people who have developed the policy language, then it seems less likely that courts will construe the language in favor of individual insureds rather than for the benefit the group. There are also proposals surfacing by insurers to resolve past liabilities, which would in turn ease future insurability.[48]

One of the major impediments to insurance for toxics is the existence of joint and several liability. This means that the assessment of individual risk characteristics of a potential insured are only of limited value because of the possibility that the insured may interact with numerous other entities whose activities are beyond the knowledge of the insurer. There are, however, circumstances in which the operations of an individual

insured may make it possible to avoid this dilemma. Where a firm's activities are entirely controlled by the firm and there is no interaction with another, integrated waste management and pollution control, and insurance may be possible. The firm would be subject to principles of joint and several liability, but if there is no interaction with others, then the activities are, in effect, several and not joint.

A key to such insurance and to operations of any firms with toxic exposures in the future will include heightened environmental awareness, the increased use of environmental audits, and risk assessments. Also, as greater regulation comes into play and as greater knowledge is developed, stability on the scientific side may well also enhance the possibility of risk transfer. The key to taking advantage of these opportunities will be a substantial knowledge of the law, science, and risk assessment. These factors, combined with sound underwriting, should make it possible and responsible for insurers to return to the market and for businesses to pool to insure their collective risks.[49]

Another insurance tool which may prove useful for allowing pools, or the commercial insurance industry to function, is the creative use of deductibles and tailoring of coverage to fit within certain economic perameters. A deductible may be crafted to compensate for residual or past exposures and to allow a risk transfer of future liability. A company might provide an insurance policy with no "drop down" provisions that would take

effect after the expenditure of an expected loss at a site where a known clean-up might be required.

In the case of an exposure with a pharmaceutical or similar product, such as vaccines, where there is an expected adverse consequence that public policy deems worth assuming, and where there is reasonable certainty as to the number of adverse events and their traditional costs within the tort system, it should be possible for an insurer to craft a workable deductible. This would leave with the insured the expected exposures as well as a buffer. The insurer could then provide coverage for an exceptional level of frequency or severity. If, for example, a product produces an expected 50 adverse events per year, an insurer might be comfortable with a buffer that would require the insured to respond to any events between 75 and 100. The insurer might also respond to any losses that exceed the expected average. If the expected average loss in such a circumstance were $1 million, the insurer might be comfortable with a buffer that would allow it to assume liability within the $1 million to $3 million range. It should also be possible for an insurer using such deductible safety zones to provide coverage in excess of certain aggregate losses, for example $100 million. These are some of the factors that went into the creation of certain markets for high excess limits during the recent hard market shortage of commercial insurance.

Another insurance opportunity may be the creative use of annuities. In toxic exposures, annuities may be useful in the payment of long-term exposures as well as the prefunding of certain varieties of anticipated losses. Some people are working on the use of structuresd settlements for payment of clean up costs. This approach offers great advantages for all parties.

Insurers should be on the lookout for circumstances in which specific liability types are limited as to time and cost. Special legislation may provide an opportunity to limit the exposure. In these circumstances, with favorable legislative guidance or judicial interpretation, it may be possible to insure specific distinct and discreet varieties of toxic liability exposure. Examples of such limited liability include provisions in the federal Superfund and some state laws limiting the exposure of remedial action contractors.[50] Expansion of the "innocent land owners defense" in the Superfund Amendments and Reauthorization Act[51] provides an opportunity for insurance to play a role for banks and other parties, where there may be innocent land-owning acquisitions.[52] Finally, it also may be possible to provide coverage for underground storage tanks under proposed regulations being promulgated by the Environmental Protection Agency. Unfortunately, smaller insureds may encounter extreme difficulties in obtaining coverage in this category.

From the public policy perspective, it is unfortunate that the system has become so unstable that insurers are no longer able to

provide their traditional service of risk-spreading and supplemental risk-avoidance. Special circumstances may facilitate the insurance industry's return to these markets. On the whole, however, until the legislative judicial revolution concerning toxic torts becomes more settled, it is unlikely that insurers will remain a major player in society's resolution of these issues.

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