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NJ Ruling Protects Insureds From Insolvent Carrier Gaps

By **Martin Bricketto**

Law360, New York (October 10, 2013, 7:50 PM ET) -- A recent New Jersey Supreme Court holding that insureds shouldn't be left holding the bag for an insolvent insurer's share of cleanup costs in long-running environmental contamination is a major win for policyholders and will be an important tool in settlement talks, attorneys say.

Attorneys for policyholders are cheering the Sept. 24 opinion in Farmers Mutual Fire Insurance Co. v. New Jersey Property-Liability Insurance Guaranty Association. The ruling means that, when an insolvent insurer is among those on the hook in continuous trigger cases, solvent insurers must pay up to their policy limits before the PLIGA steps in, and that policyholders shouldn't be responsible for the periods that an insolvent insurer covered, they say. The state guarantee association protects policyholders when a carrier goes belly up.

Carriers in the past have argued that a policyholder should eat an insolvent insurer's share of the cleanup costs, according to Christopher Loeber, a partner in Lowenstein Sandler LLP's insurance coverage practice group.

“What this does is really take away the insurers' ability to hold policyholders accountable for those time periods when they may have been insured by carriers who have gone insolvent,” Loeber said.

Farmers wanted the PLIGA to reimburse it for an insolvent insurer's share of cleanup expenses at two residential properties, based on Owens-Illinois Inc. v. United Insurance Co. That 1994 ruling treated progressive damage as an occurrence within each year of applicable policies and adopted a pro rata formula to spread responsibility among insurers, based on when their policies were in effect and the risks they incurred.

However, the high court found that the state Legislature has made the PLIGA a payor of last resort under such circumstances. A 2004 amendment to the New Jersey Property-Liability Insurance Guaranty Association Act exempts the PLIGA from the Owens-Illinois allocation scheme until the policy limits of all solvent insurers are used up, according to the opinion.

But attorneys also point to a paragraph of the ruling that shoots down arguments from amicus participant Zurich American Insurance Co. that a policyholder should be on the hook for the gaps that an insolvent carrier covered.

The court rejected the notion that, for the years in which the PLIGA stands in for an insolvent carrier, the insured and not a solvent carrier must make payments under the Owens-Illinois scheme before turning to the guaranty association for benefits.

That would “turn the PLIGA Act on its head,” according to the opinion, which highlighted the law's goal of minimizing the financial loss to policyholders from an insurer's insolvency.

“That aim would be defeated by making the insured bear the loss for the carrier’s insolvency before the insured received any statutory benefits from the Guaranty Association,” the opinion said.

While the ruling won't be the last word on the issue, the message is clear, according to Loeber.

“I think the court meant what it said and said what it meant: that when you have an insolvency, the first place you look is the solvent carrier,” he said. “What this has done is say, 'No, there's nothing unfair about holding solvent insurers liable up to the full amounts of their limits.'”

Calling the decision “huge,” Anderson Kill shareholder Robert D. Chesler said he is representing policyholders in two cases in which liquidated carriers are respectively tied to 50 percent and 40 percent of the coverages at issue. The opinion should help numerous policyholders in the state in such situations, he said.

“Over the past couple of decades, insurance companies have absolutely refused to take responsibility for those liquidated years, so you've got a big burden on the policyholder,” Chesler said. “This blows it out of the water and switches the duty to the insurance company.”

The decision also gels with a finding in Owens-Illinois that policyholders should participate in the allocation scheme when they forgo insurance coverage for certain time periods, according to Sherilyn Pastor, the practice group leader for McCarter & English LLP's insurance coverage group.

“The policyholder doesn't share in the allocation unless it goes bare,” Pastor said, adding later: “That's why policyholders pay premiums and purchase insurance — to protect themselves from losses, and there's nothing unfair about that.”

Claims tied to long-tail environmental contamination often settle before trial, and the Farmers Mutual ruling could prove useful for policyholders in those negotiations, according to Pastor.

“I think it will be effective in the sense that insurers sometimes look to reduce the amounts that they owe by arguing that a policyholder is somehow responsible or should be contributing and the decision provides powerful support that insurers pick up the loss,” she said.

However, James W. Carbin, a partner with Duane Morris LLP, questioned whether policyholders received any direct benefit from the decision, adding that he was surprised the case made it all the way to the state supreme court.

“I think as a general proposition guarantee funds are the last to be applied to and the structure of most guarantee funds doesn't permit them to respond until all private insurance is exhausted,” he said.

The lesson here is that the PLIGA isn't going to pay unless it's the last man standing, according to Carbin.

“I think it reinforces that in a settlement, the solution has to be approached independent of the guarantee fund except in those instances where it becomes clear that whatever available coverage there is won't be adequate,” he said.

--Editing by John Quinn and Richard McVay.