

IN THE UNITED STATES DISTRICT COURT
FOR THE EASTERN DISTRICT OF PENNSYLVANIA

SCRANTON DUNLOP, INC., DBA : CIVIL ACTION
SANDONE TIRE AND BATTERY :
 :
v. :
 :
ST. PAUL FIRE AND MARINE :
INSURANCE COMPANY, et al. : No. 00-2138

MEMORANDUM

Ludwig, J.

August 4, 2000

Defendants St. Paul Fire and Marine Insurance Company (St. Paul) and the United States Fidelity and Guaranty Company (USF&G) move to dismiss the complaint for failure to state a claim. Fed. R. Civ. P. 12(b)(6).¹ Jurisdiction is diversity. 28 U.S.C. § 1332.

This is a breach of contract action involving a liability insurance policy issued by USF&G to plaintiff Scranton Dunlop, Inc., dba Sandone Tire and Battery.² On June 5, 1994, a fire broke out on a property once used for the storage and disposal of scrap tires – a property previously owned by plaintiff. On June 5, 1996, the then current owner, Sally Shair Weiss, sued plaintiff for the resulting damage and clean-up costs. Weiss v. Johnson et al., Civ. No. 96-1012 (M.D. Pa., 1996). On August 4, 1994, plaintiff gave notice of the claim to USF&G,

¹ Under Rule 12(b)(6), the allegations of the complaint are accepted as true, and all reasonable inferences are drawn in the light most favorable to the plaintiff, and dismissal is appropriate only if it appears that plaintiff would prove no set of facts that would entitle her to relief. See United States v. Occidental Chem. Corp., Civ. No. 99-3084, 1999 WL 1268110 at *2 (3d Cir. Dec. 28, 1999).

² St. Paul is the successor to USF&G. Prior to the acquisition, USF&G and plaintiff entered into the insurance contract in dispute.

which, despite several requests, took no steps to provide a defense. On June 30, 1998, plaintiff contacted St. Paul, which had acquired USF&G, and on September 9, 1998, St. Paul denied coverage, citing the insurance policy's pollution exclusion.³

³ Section f. expressly excludes coverage for

- (1) "Bodily injury" or "property damage" arising out of the actual, alleged or threatened discharge, dispersal, seepage, migration, release or escape of pollutants:
 - (a) At or from any premises, site or location which is or was at any time owned or occupied by, or rented or loaned to, any insured;
 - (b) At or from any premises, site or location which is or was at any time used by or for any insured or others for the handling, storage, disposal, processing or treatment of waste;
 - (c) Which are or were at any time transported, handled, stored, treated, disposed of, or processed as waste by or for any insured or any person or organization for whom you may be legally responsible; or
 - (d) At or from any premises, site or location on which any insured or any contractors or subcontractors working directly or indirectly on any insured's behalf are performing operations:
 - (i) if the pollutants are brought on or to the premises, site or location in connection with such operations by such insured, contractor or subcontractor; or
 - (ii) if the operations are to test for, monitor, clean up, remove, contain, treat, detoxify or neutralize, or in any way respond to, or assess the effects of pollutants.

Subparagraphs (a) and (d)(i) do not apply to "bodily injury" or "property damage" arising out of heat, smoke or fumes from a hostile fire.

As used in this exclusion, a hostile fire means one which becomes uncontrollable or breaks out from where it was intended to be.

(continued...)

Following St. Paul's denial of coverage, plaintiff defended the claim itself, and on October 13, 1999, the action was dismissed on a Rule 12(b)(6) motion – an appeal is pending.

In the present action, it is alleged that the disclaimer of coverage violated the liability insurance contract and amounted, in these circumstances, to bad faith. The insurers contend that the pollution exclusion applies to the underlying damage claim and, accordingly, the decision to deny coverage did not involve bad faith.

I. Duty to Defend

Under the insurance policy, the insurer is required to defend the insured against covered claims. The duty to defend is broad and is operative if recovery is conceivably possible. See Frog, Switch & Mfg. Co. v. Travelers Ins. Co., 193 F.3d 742, 746 (3d Cir. 1999).

³(...continued)

- (2) Any loss, cost or expense arising out of any:
- (a) Request, demand or order that any insured or others test for, monitor, clean up, remove, contain, treat, detoxify or neutralize or in any way respond to, or assess the effects of pollutants; or
 - (b) Claim or suit by or on behalf of a governmental authority for damages because of testing for, monitoring, cleaning up, removing, containing, treating, detoxifying or neutralizing, or in any way responding to, or assessing the effects on pollutants.

Pollutants means any solid, liquid, gaseous or thermal irritant or contaminant, including smoke, vapor, soot, fumes, acids, alkalis, chemicals and waste. Waste includes materials to be recycled, reconditioned or reclaimed.

Pennsylvania law governs the insurance policy, which must be interpreted "according to its plain meaning." Id. at 745-46. If unambiguous, the plain meaning of the language may not be altered, see Lobaugh v. Lobaugh, 753 A.2d 834, 836 (Pa. Super. Ct. 2000); and "a provision is ambiguous only if reasonable people could, in the context of the entire policy, fairly ascribe differing meanings to it." Frog, Switch & Mfg. Co., 193 F.3d at 746. If ambiguous, extrinsic evidence may be considered to ascertain the parties' intent. See Seven Springs Farm, Inc. v. Croker, 748 A.2d 740, 744 (Pa. Super. Ct. 2000). Ambiguities that cannot be reconciled are to be resolved "in favor of the insured because the insurer writes the contract." Frog, Switch & Mfg. Co., 193 F.3d at 746.

This issue of whether there is coverage under the policy turns on whether the pollution exclusion or its hostile fire exception is applicable to the facts of this case. Since this is a matter of state law that has not been decided by the Pennsylvania Supreme Court, a prediction must be made as to how that court would rule if confronted with the same facts. See Polselli v. Nationwide Mutual Fire Ins., 126 F.3d 524, 528 (3d Cir. 1997).⁴

According to defendants, the hostile fire exception refers only to sections f(1)(a) and f(1)(d)(I) of the exclusion, and, as a result, the other exclusion provisions act independently and form a separate basis for the denial of coverage. Under this view, the effect of the hostile fire exception need not be considered.

⁴ There appear to be no reported Pennsylvania decisions on point.

Plaintiff's counter-argument is that the separate exclusion provisions are interdependent and exclude coverage for all damage caused by pollution, unless the damage is caused by a hostile fire. Given this analysis, the hostile fire exception is an affirmative grant of coverage for situations in which coverage might otherwise be excluded.

Pollution exclusions in this type of policy have been construed both ways. In Mid-Continent Casualty Co. v. Safe Tire Disposal Corp., 16 S.W.3d 418 (Tex. App. 2000), the separate provisions were considered to be independent – so that as long as a claim falls within one of the sub-sections that is not subject to the hostile fire exception, coverage is excluded regardless of the exception's applicability to another sub-section. Id. at 421-24. However, the separate provisions have also been treated as a single exclusion, modified in their entirety by the hostile fire exception. See American Star Ins. Co. v. Grice, 854 P.2d 622, 625 (Wash. 1993). What is more, it has been said "that the language of the pollution exclusion when read with the hostile fire exception thereto is fairly susceptible to differing reasonable interpretations by an average person." Id.

Since two potential constructions exist, the use of extrinsic evidence may have to be explored, making the motion premature and requiring it to be denied.

II. Bad Faith

Bad faith necessitates clear and convincing evidence that the insurer unreasonably declined to carry out the terms of the policy or recklessly disregarded the basis of the underlying claim. See Adamski v. Allstate Ins. Co., 738 A.2d 1033, 1036 (Pa. Super. Ct. 1999). A reasonable but incorrect interpretation of an insurance provision does not rise to bad faith. See Bostick v. ITT Hartford Group, Inc., 56 F. Supp.2d 580, 587 (E.D. Pa. 1999). Defendants' reading of the pollution exclusion appears to be facially reasonable in that it has decisional support, but facts may be developed as to the parties' contractual intent that could lead to a different conclusion. For this reason, this portion of defendants' motion must also be denied.

Edmund V. Ludwig, J.

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ORDER

AND NOW, this 4th day of August, 2000, the motion of defendants St. Paul Fire and Marine Insurance Company and the United States Fidelity and Guaranty Company to dismiss the action is denied.

Edmund V. Ludwig, J.