

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

AMERICAN & FOREIGN INSURANCE CO., and : CIVIL ACTION  
ROYAL INSURANCE COMPANY OF AMERICA, INC. :  
v. :  
PHOENIX PETROLEUM CO. : No. 97-3349

Norma L. Shapiro, J.

June 23, 1998

**Findings of Fact and Conclusions of Law**

American & Foreign Insurance Co. ("American") and Royal Insurance Co. ("Royal") seek a declaratory judgment that Phoenix Petroleum Co.'s ("Phoenix") activities in a joint venture were not covered by the insurance policies, and there is not duty to defend or indemnify. The Court granted American's motion for summary judgment, and held a non-jury trial on Royal's claims. In accordance with Federal Rule of Civil Procedure 52(a), the court enters the following findings of fact and conclusions of law.

**Findings of Fact**

1. Phoenix is a Pennsylvania Corporation engaged in the sale and marketing of refined petroleum products
2. American is a Delaware company with its principal place of business in North Carolina.
3. Royal Insurance Company of America is an Illinois company with its principal place of business in North Carolina.
4. In 1996, Phoenix purchased insurance from both American and Royal for the period of 1996 to 1997.

5. American issued a commercial general liability policy ("primary policy").
6. Royal issued a commercial catastrophe liability insurance policy ("umbrella policy").
7. Phoenix purchased the insurance contracts through its agent, Wharton/Lyon & Lyon, a retail insurance broker.
8. American and Royal sold the contracts through its agent, Tri-City Insurance Brokers, Inc., a wholesale insurance broker.
9. The insurance contracts were accepted by Phoenix at its principal place of business in Wayne, Pennsylvania.
10. The section of the primary policy regarding "Who is and Insured" provided that:

No person or organization is an insured with respect to the conduct of any current or past partnership, joint venture or limited liability company that is not shown as a Named Insured in the Declarations.

(Pl. Ex. 3, Section II, p. 7).

11. The primary policy stated Phoenix was a corporation.
12. Phoenix Petroleum is the only Named Insured in the primary policy declarations; no joint venture is mentioned.
13. The umbrella policy provided excess coverage for any claims against any insured "in any of the policies listed in Item VI Schedule of Underlying Insurance." (Pl. Ex. 4, endorsement 1).
14. Item VI, Schedule of Underlying Insurance, lists three policies: the primary policy, an automotive liability policy issued by "Royal", and a workers compensation and employers liability policy issued by "Selective." (Pl. Ex. 4, p. 2) .

15. The umbrella policy stated that Phoenix was a corporation.

16. In the insurance application, the box for corporation was checked; there was a box for joint venture, but it was not checked.

17. The form umbrella policy defined insured parties under Section III, and did not limit coverage to parties covered under the primary policy.

18. Section III of the umbrella policy was deleted and replaced with an endorsement issued concurrently with the policy.

19. That endorsement stated:

If you are designated as an insured in [the primary policy, the automotive liability policy, or the workers compensation and employers liability policy] you are also an insured under this policy.

If you are not an Insured in any of the[se] policies . . . you are not an Insured under this policy.

20. The umbrella policy provides coverage for property damage, which is defined as:

physical injury to tangible property, including all resulting loss of use of that property, or [] loss of use of tangible property that is not physically injured.

21. The umbrella policy excludes coverage for:

"Property Damage" to "Impaired Property" or property that has not been physically injured, arising out of:

(a) A defect, deficiency, inadequacy or dangerous condition in "Your Product" or "Your Work"; or

(b) A delay or failure by you or anyone acting on your behalf to perform a contract or agreement in accordance with its terms,

This exclusion does not apply to the loss of use of other property arising out of sudden and accidental

physical injury to "Your Product" or "Your Work" after it has been put to its intended use.

22. "Impaired Property" is defined in the umbrella policy as:

tangible property, other than "Your Product" or "Your Work" that cannot be used or is less useful because:

(a) it incorporates "Your Product" or "Your Work" that is known or thought to be defective, deficient, inadequate, or dangerous; or

(b) You have failed to fulfill the terms of a contract or agreement;

if such property can be restored to use by:

(a) The repair, replacement, adjustment or removal of "Your Product" or "Your Work"; or

(b) Your fulfilling the terms of such contract or agreement.

23. The parties provided the court with the umbrella policy and the primary policy, but did not provide the court with the automotive liability policy, or the workers compensation and employers liability policy for the policy year at issue.

24. In 1992, Phoenix and International Petroleum Company ("International") entered into a joint venture ("the joint venture") to manufacture and market lubricating oils.

25. In the context of the joint venture, Phoenix purchased base lubricating oil which it blended and compounded into finished lubricating oils.

26. Phoenix held title to the lubricating oils sold, invoiced and collected on the sales of the joint venture, paid expenses, carried income and expenses on its books and paid taxes.

27. The lubricating oils were sold by the joint venture under invoices bearing both companies' names.

28. Phoenix and International divided the profits from the joint venture equally.

29. The joint venture was not incorporated, did not have a tax identification number, did not have any employees, and did not have separate premises.

30. The joint venture entered into an agreement with a refining company, whereby the refining company would blend the oils for the joint venture, and would receive half the profits from the sale; the joint venture would receive the other half, to be divided equally between Phoenix and International.

31. In July 1996, the joint venture sold some of these blended lubricating oils to Horn Brothers Oil Company, Inc. ("Horn Brothers").

32. Horn Brothers resold the product to their customers.

33. Horn Brothers refused to pay amounts allegedly due.

34. When the joint venture brought suit to collect amounts owed, Horn Brothers, alleging that the oils were defective, counterclaimed for "an amount which exceeds \$400,000."

35. In their counterclaim, Horn Brothers sought damages for: direct and indirect loss of profits, damage to equipment, loss of use of equipment, economic damages including costs associated with recovering, replacing, storing and disposing of the defective oils; and repair and restitution for its customers damages.

36. The basis for the Horn Brothers claim was that the oils allegedly contained an excessive amount of particulates making them unsuitable as lubricants.

37. Horn Brothers was exclusively a customer of the joint venture, it did not purchase products from Phoenix Petroleum acting outside the joint venture.

38. Phoenix notified American and Royal of their duty to defend and indemnify.

39. American and Royal disclaimed coverage on the ground that the joint venture was not covered by Phoenix's primary policy or umbrella policy, respectively.

40. In its complaint, Phoenix stated that it did not challenge declination of coverage under the Primary Policy; it sought coverage under the umbrella policy.

41. The court granted summary judgment on behalf of American; the joint venture is not covered by the primary policy.

42. The court denied summary judgment on behalf of Royal because the "motion . . . turn[ed], in part, on whether the joint venture enjoys legal status independent from that of Phoenix, and could be independently insured." (Order, April 29, 1998, ¶ 3).

#### **Discussion**

Under Pennsylvania law when the facts are not in dispute the court interprets an insurance policy as a matter of law. See Pacific Indem. Co. v. Linn, 766 F.2d 754, 760 (3d Cir. 1985). The terms of a policy are construed according to their plain meaning. See Atlantic Mut. Ins. Co. v. Brotech Corp., 857

F. Supp. 423, 427 (E.D. Pa. 1994), aff'd, 60 F.3d 813 (3d Cir. 1995). If the plain meaning is clear, it must be given effect. McMillan v. State Mutual Life Assur. Co. of America, 922 F.2d 1073, 1075 (3d Cir. 1990). If the language is ambiguous, all doubts as to its meaning should be resolved in favor of the insured. St. Paul Fire & Marine Ins. Co. v. Lewis, 935 F.2d 1428, 1431 (3d Cir. 1991); Mohn v. American Casualty Co of Reading, 326 A.2d 346, 351 (Pa. 1974). A provision of an insurance policy is ambiguous if, on considering it in the context of the entire policy, reasonably intelligent people would honestly differ as to its meaning. Britamco Underwriters, Inc. v. C.J.H., Inc., 845 F. Supp. 1090, 1093 (E.D. Pa.), aff'd, 37 F.3d 1485 (3d Cir. 1994). "The language of the policy may not be tortured ... to create ambiguities where none exist." Pacific Indem. Co. v. Linn, 766 F.2d 754, 761 (3d Cir. 1985).

The umbrella policy limited coverage to insureds under any of the listed policies, one of which was the primary policy. The primary policy limited "Who was an Insured" to organizations designated in the declarations. Phoenix Petroleum Corporation is the only named insured designated in the declarations. However, "Who is an Insured" specifically narrowed the possible activities by stating that "[n]o person or organization is an insured with respect to the conduct of any . . . joint venture." (Pl. Ex. 3, p. 7). Phoenix was not considered an insured under the primary policy for activities in the joint venture.

However, the umbrella policy does not limit coverage to activities under the primary policy; nor does it limit coverage only to those insured under the primary policy. The umbrella policy extends coverage to an insured under any of the underlying policies. If an individual or entity is insured under the automotive liability policy, it is also insured under the umbrella policy. The insurance under the umbrella policy is not limited to the activities covered under the respective underlying policies. If an organization is insured for any limited claim under any underlying policy, it is an insured for the purposes of the umbrella policy, and the umbrella insurance is not limited to the claims allowed in that particular underlying policy. The fact that Phoenix's joint venture activities were excluded under the primary policy does not mean that they were excluded under the other policies. Royal objected to the introduction of the other policies, so there is no evidence of record that all the other policies limited insureds in the same manner as the primary policy.

The second clause of the endorsement is the negative corollary of the first. If an organization is not listed as "an Insured in any of the [underlying policies, it is] not an Insured under [the umbrella] policy." (Pl. Ex. 4, p. 3) (emphasis added). In order to be covered by the umbrella, an organization must merely be an insured under any of the underlying policies. Royal has conclusively shown that Phoenix's joint venture activities were not covered by the primary policy. This does not

establish that the joint venture's actions were not covered by any of the underlying policies.

The language is clear, and the court will not torture the language to create an ambiguity where none exists. Pacific Indem. Co. v. Linn, 766 F.2d 754, 761 (3d Cir. 1985). Even if the second clause can possibly be read that the umbrella policy limits coverage to those insured under the appropriate correlative underlying policy, the language would be ambiguous at best. The court must read the alleged ambiguity to the benefit of the insured. St. Paul Fire & Marine Ins. Co. v. Lewis, 935 F.2d 1428, 1431 (3d Cir. 1991).

The court is required to read the endorsement to cover any insured under any underlying policy. Phoenix has failed to demonstrate that the joint venture was not an insured under any underlying policy. The court agrees that it was not an insured under the primary policy, but since the umbrella policy does not limit coverage to the terms of the relevant underlying policy, Royal has failed to carry its burden, and the court cannot grant judgment in its favor.

Under Pennsylvania law, an insurer has a duty to defend the insured whenever the complaint filed against the injured "may potentially come within the policy's coverage." Twin City Fire Insurance Co. v. Home Indemnity Co., 650 F. Supp. 785, 789 (E.D. Pa. 1986) (quoting Pacific Indemnity Co., 766 F.2d at 760). The claim against the joint venture potentially comes within the umbrella policy's coverage, because it involves actions by the

joint venture which may be covered by one of the underlying policies.

The duty to indemnify is narrower than the duty to defend; it encompasses only claims actually covered, rather than those potentially covered. See Erie Insurance Co. v. Claypoole, 673 A.2d 348, 355 (Pa. 1996). At this point, it is not clear to the court whether claims made by Horn Brothers may be covered by the umbrella policy.

Several claims made by Horn Brothers are not covered by the umbrella policy, and Royal has no duty to indemnify to the extent any recovery by Horn Brothers is based on them. Horn Brothers claims "loss of profits, loss of opportunities and loss or damage to business reputation." (Pl. Ex. 9, p. 5, ¶ 10). Loss of good will and reputation constitutes economic loss, not property damage, and is not covered by the umbrella policy; Royal need not indemnify Phoenix for claims of economic loss.

International Ins. Co. v. St. Paul Fire & Marine Ins. Co., 1988 WL 113360, at \*5 (E.D. Pa. Oct. 25, 1988).

Horn Brothers also seeks to recover "costs associated with recovering, replacing, storing, and disposing of the defective oil." (Pl. Ex. 9, p. 5, ¶ 9). These costs are not covered by the umbrella policy, which is limited to "Bodily Injury," "Property Damage," "Personal Injury" and "Advertising Injury," (Pl. Ex. 4, p. 1); Royal is not obligated to indemnify Phoenix against these Horn Brothers' claims. Standard Venetian Blind Co. v. American Empire Ins. Co., 469 A.2d 563 (Pa. 1983).

Horn Brothers also seeks to recover for loss of use of storage tanks during the period they contained Phoenix's allegedly defective product. (Pl. Ex. 9, p. 4, ¶ 7). The umbrella policy excludes damages for loss of use of tangible property, if the property can be restored to use by removal of the insured's product. Horn Brothers's storage tanks could be restored to use by removing the joint venture's lubricating oil. Its claim for loss of use of storage tanks is excluded by the umbrella policy, and Royal has no obligation to indemnify Phoenix for that claim if successful on the merits. Since there is no actual coverage for these claims, there is no possible coverage, and if all other claims are resolved, Royal need not defend Phoenix on those claims.

In order to find that other claims are actually covered, the court must find that Royal knew of the risk it was insuring, and undertook to cover it. See New York Life Ins. Co. v. Johnson, 923 F.2d 279, 283 (3d Cir. 1991) (citing Mutual Benefits Life Insurance Co. v. JMR Electronics Corp., 848 F.2d 30 (2d Cir. 1988)) ("If a fact is material to the risk, the insurer may avoid liability under a policy if that fact was misrepresented in an application for that policy whether or not the parties might have agreed to some other contractual arrangement had the critical fact been disclosed.").

Wharton/Lyon & Lyon, acting as Phoenix's agent, represented that Phoenix was engaged only in the sale but distribution of petroleum products; the joint venture

manufactured lubricating oils.<sup>1</sup> Royal based its insurance premiums on the representation that the oil Phoenix sold was distributed by insured contract carriers so that Phoenix "never touch[ed] the product." (Pl. Ex. 1, p. 2). Royal has argued that the risk significantly increases if the umbrella policy covers not merely sale and distribution but also manufacture of lubricating oils. When Wharton/Lyon & Lyon was contacted by another insurance company about whether Phoenix manufactured lubricating oils, or worked with other companies in that regard, (Def. Ex. 11, p. 2), Wharton/Lyon&Lyon, Phoenix's agent, responded that "Phoenix **does not** do any manufacturing," and neglected to mention its numerous joint venture arrangements of which Wharton/Lyon & Lyon had knowledge. (Def. Ex. 12, p. 2) (emphasis in original). Royal allegedly did not base its premium on the higher risk because that risk was not ever mentioned.

Whether Royal knew of the risk and whether other claims against the joint venture for allegedly defective lubricating oil are covered by the umbrella policy must be considered after disposition of the West Virginia action. A court can consider whether the claims on which Horn Brothers actually prevails were covered by the umbrella policy's duty to indemnify Phoenix. The action before this court is a request for a declaratory judgment

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<sup>1</sup> Phoenix's President, Stephen Wang, admitted that Wharton/Lyon & Lyon, the insurance broker, was its agent. Even if he had not admitted it, the court would have reached the same conclusion. See, e.g. Rich Maid Kitchens, Inc. v. Pennsylvania Lumbermens Mutual Ins. Co., 641 F. Supp. 297, 303 (E.D. Pa. 1986) (citing Taylor v. Crowe, 282 A.2d 682, 683 (Pa. 1971)).

to determine the scope of Royal's duty to defend and indemnify. It is premature to determine the precise scope of its duty to indemnify. Royal may be entitled to rescind the umbrella policy, New York Life Ins. Co. v. Johnson, 923 F.2d 279, 283 (3d Cir. 1991), or may have a claim against Wharton/Lyon & Lyon for fraud, but the court expresses no opinion about a claim for rescission or for fraud.

Phoenix is seeking attorney fees in this action. Under Pennsylvania law, Phoenix is entitled to attorney fees only if Royal acted in bad faith in disclaiming coverage and refusing to defend. Kelmo Enterprises v. Commercial Union Ins. Co., 426 A.2d 680, 685 (Pa. Super. 1981); accord F.B. Washburn Candy Corp. v. Fireman's Fund, 541 A.2d 771 (Pa. Super. 1988). Phoenix has not alleged or shown that Royal acted in bad faith. United States Fire Insurance Co. v. Royal Insurance Co., 759 F.2d 306, 309 (3d Cir. 1985), American Franklin Life Ins. Co. v. Galati, 776 F. Supp. 1054, 1064 (E.D. Pa. 1991). Phoenix's request for attorney fees is denied.

Any facts in the Discussion section not found in the Facts section are incorporated by reference therein.

#### Conclusions of Law

1. The court has jurisdiction over this action under 28 U.S.C. § 1332, and 28 U.S.C. § 2201.
2. Phoenix purchased the umbrella policy through its agent, Wharton/Lyon & Lyon.

3. Royal sold the insurance through its agent, Tri-City Insurance Brokers, Inc.
4. Phoenix was insured under the umbrella policy.
5. The joint venture was not a separate legal entity. Beavers v. West Penn Power Co., 436 F.2d 869 (3d Cir. 1971).
6. Phoenix's activities in the joint venture may be covered by the umbrella policy.
7. Royal has the duty to defend Phoenix for actions of the joint venture in the counterclaim brought by Horn Brothers in West Virginia so long as there remain claims as to which there may be a duty to indemnify.
8. Royal has no duty to indemnify Phoenix for any claims by Horn Brothers for "loss of profits, loss of opportunities and loss or damage to business reputation," "costs associated with recovering, replacing, storing, and disposing of the defective oil," or for loss of use of storage tanks during the period when they contained Phoenix's allegedly defective product.
9. Royal did not act in bad faith in disclaiming coverage for the claims asserted against Phoenix in the underlying action.
10. Phoenix is not entitled to attorneys fees for its defense of this declaratory judgment action.
11. The court will direct judgment as to the duty to defend; as to the duty to indemnify, the court will place this claim in administrative suspense, pending resolution of Horn Brothers' counterclaim in Phoenix Petroleum Co. and International Petroleum

Co. v. Horn Brothers Oil Company, Inc., Civil Action No. 97-C-2,  
Circuit Court of Pleasants County, W. Va.

IN THE UNITED STATES DISTRICT COURT  
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AMERICAN & FOREIGN INSURANCE CO., and : CIVIL ACTION  
ROYAL INSURANCE COMPANY OF AMERICA, INC.:  
v. :  
PHOENIX PETROLEUM CO. : No. 97-3349

ORDER

AND NOW, this 23rd day of June, 1998, following a non-jury trial on June 22, 1998, it is **ORDERED** that:

1. Plaintiff's request for a declaratory judgment is **GRANTED** in part; defendant's request for a declaratory judgment is **GRANTED** in part.

2. As to the duty to defend, the court declares that:

a. Royal Insurance Company of America has the duty to defend Phoenix Petroleum Co. in the counterclaim brought by Horn Brothers in Phoenix Petroleum Co. and International Petroleum Co. v. Horn Brothers Oil Company, Inc., Civil Action No. 97-C-2, Circuit Court of Pleasants County, W. Va.

b. The court having adjudicated fewer than all claims for relief, the court directs entry of final judgment as to the duty to defend pursuant to Fed. R. Civ. P. 54(b) because it finds that there is no just reason for delay.

3. As to the duty to indemnify, the court declares that:

a. Royal has no duty to indemnify Phoenix for claims by Horn Brothers for loss of profits, loss of opportunities and loss or damage to business reputation, costs associated with recovering, replacing, storing, and disposing of the defective oil, or for loss of use of storage tanks during the period when they contained Phoenix's allegedly defective product.

b. Royal may have a duty to indemnify other claims; as to those claims, the action is placed in administrative suspense pending the outcome of Horn Brothers' counterclaim in Phoenix Petroleum Co. and International Petroleum Co. v. Horn

Brothers Oil Company, Inc., Civil Action No. 97-C-  
2, Circuit Court of Pleasants County, W. Va.

4. Phoenix's request for attorney fees in this action is

**DENIED.**

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J.