

Legal Opinion: GCH-0046

Index: 2.265

Subject: Liability Insurance for Lead-Based Paint Exposures

February 25, 1992

MEMORANDUM FOR: Michael B. Janis, General Deputy Assistant  
Secretary, PD

FROM: Robert S. Kenison, Associate General Counsel  
Office of Assisted Housing and Community Development, GC

SUBJECT: Liability Insurance for Lead-based Paint Exposures

This is in response to your memorandum of August 22, 1991 to me. Please excuse the delay in responding to your memorandum. You requested our review of the attached Lead-Based Paint Abatement Pollution Liability Insurance Policy (the "Policy"), issued by American Empire Surplus Lines Insurance Company. You also requested our opinion and interpretation regarding exposures under this insurance and methods of dealing with them and our analysis of coverage regarding four scenarios. We will first present our section-by-section review of the Policy highlighting your issues and potential exposures and then respond to the scenarios and recommendations for dealing with the exposures.

Endorsement No. 01 - Lead-Based Paint Abatement Pollution  
Liability Insurance Coverage:

Although this section fails to describe what is considered "abatement/removal or the testing for the presence of lead-based paint" (an issue raised by the Office of Inspector General's Review of Master Liability Insurance Policy for Testing and Abatement of Lead-Based Paint in Public Housing, dated September 24, 1991, No. 91-TS-108-0016 (the "IG Review") at page 19), the Amendatory Condition-Warranty provision (Endorsement No. 06) indicates that "the named insured and the additional named insureds hereby warrant that they will comply with the most current lead-based hazard elimination regulations the "Regulations" and the recommendations outlined in the document entitled, "Lead-Based Paint Hazard Identification and Abatement in Public and Indian Housing" the "Guidelines" dated April 1, 1990 (as amended, revised or updated)." We suggest that the best interpretation of the Policy is that it covers all units which were the subject of abatement or testing of lead-based paint in conformity with the Regulations and Guidelines.

Units which were part of a random sample test (those physically tested as well as those which were part of the test group, e.g., units counted in determining the size of the random sample) are covered by the Policy. The Guidelines permit two

methods for selecting the statistical sample for testing purposes (i.e., systematic sampling plan and random number procedure). The Policy would permit use of either method. The IG Review also discusses this issue of unit coverage on pages 20-22. To the extent that the PHA made reasonable statistical projections or used random number procedures properly, it should be able to withstand legal challenge. If HUD revises the Guidelines to limit the sampling to a pure random procedure, as PD&R suggests in the IG Review (on page 22 of the IG Review), the Policy would also limit PHAs to that procedure.

Only units actually abated pursuant to the Regulations and Guidelines are covered by the Policy. In addition, any other site which was involved in the abatement/removal or testing are also covered by the Policy (e.g., handling, storage, disposal, processing or treatment sites). See Paragraphs (ii), (iii), and (iv) of Pollution Coverage, Endorsement No. 1. This Policy does not cover any other units (not involved in the abatement/removal or testing of lead-based paint). Such remaining units may be covered by PHAs' general liability policy.

Your memorandum concludes that Endorsement No. 1 restricts coverage so that it applies only to an occurrence taking place during the testing or abatement/removal process. Although it could be interpreted that the Policy requires both the occurrence and the bodily injury or property damage to occur during the policy period and thereby exclude pre- or post-abatement injuries (as concluded by Anderson Kill Olick & Oshinsky, in their September 16, 1991 opinion, which was procured by the Inspector General and is attached as Appendix 6 to the IG Review, "the AKOO opinion"), it could be argued that the coverage is much broader and not ambiguous. This Policy applies to "an occurrence arising out of the actual, alleged or threatened discharge, dispersal, release, escape, ingestion or presence of lead-based paint during its abatement/removal or testing for the presence of lead-based paint". Section I.1.b.(2) of the Commercial General Liability Coverage Form (the "CGLC form") additionally states that the insurance only applies to bodily injury caused by an occurrence that takes place in the coverage territory and occurs during the policy period. For example, an occurrence could arise out of the release of lead-based paint during abatement, but the injury may not ensue until months later (but still within the policy period) when a child comes in contact with the lead-based abatement residue. This arguably narrows the coverage of post-abatement injuries and eliminates pre-abatement coverage.

Another relevant consideration in determining the extent of coverage is the issue of when the injury occurs. We have reviewed the AKOO opinion regarding trigger of coverage and agree with its analysis and recommendations, except as noted in this opinion.

As a general rule, the language of an insurance policy will be given its plain meaning and there will be no resort to rules of construction unless an ambiguity exists. *National Fidelity Life Insurance Company v. Karaganis*, 811 F.2d 357, 361 (7th Cir. 1987). Whenever there is any question of interpretation of a written contract, the court will seek to determine "the intention of the parties as derived from the language employed." 4 *Williston, Contracts* 600, at 280 (3d ed. 1961). The determination of whether a provision in an insurance policy is ambiguous, and whether extrinsic evidence of intent is therefore admissible, "is a threshold question of law for the court." *Garza v. Marine Transport Lines, Inc.*, 861 F.2d 23, 26-27 (2d Cir. 1988). If the intent of the contracting parties cannot be ascertained after the trier of fact considers extrinsic evidence about the meaning of an ambiguous policy term, other rules of construction may then be applied only as a last resort. *Alfin, Inc. v. Pacific Ins. Co.*, 735 F. Supp. 115 (S.D.N.Y. 1990). The general rule of construction applicable to insurance contracts is that ambiguities are construed in favor of the insured and against the insurer. *Thomas J. Lipton, Inc. v. Liberty Mut. Ins. Co.*, 34 N.Y.2d 356, 361, 314 N.E.2d 37, 39, 357 N.Y.S.2d 705, 708 (1974). Although a good argument can be made for interpreting the Policy covers all units which were the subject of abatement or testing of lead-based paint in conformity with the Regulations and Guidelines, we suggest that based on our review, it would be desirable to revise the language of the Policy rather than risk an undesirable result through judicial proceedings.

Your memorandum states that there is no coverage for the existence hazard. It should be noted that any unit which was the subject of testing and/or abatement pursuant to the Regulations or Guidelines, is covered by the Policy, regardless of whether it had or continues to have a lead-based paint hazard.

Your memorandum also states that there would be no coverage under the PHA's general liability policy due to exclusion f (we believe that you intended to reference Section I.2.f. of the CGLC Form, incorporated except as amended by endorsements to the Policy). Exclusion f is modified by the endorsements and is of no effect with respect to the PHA's general liability policy. The coverage of lead-based paint claims under a PHA's general liability policy is subject to the interpretation of that individual policy by the State and its courts. The issue of primary and excess insurance (i.e., situations where a PHA has more than one insurance covering an injury; e.g., general liability and pollution liability insurance for lead-based paint related injury) is covered in Section IV.4 of the CGLC Form. Endorsement No. 04 to this Policy deletes Section IV.4 and provides that if the PHA has other insurance (e.g., general liability, workers compensation, lead-based paint pollution insurance) to cover the injury, the Policy is null and void.

In addition to those listed in the endorsement, we would suggest that HUD should have also been named because of its interest in the project as evidenced by the Declaration of Trust.

Endorsement No. 03 - Architects and Engineers Professional Liability Coverage Endorsement

We do not have any comments regarding this endorsement.

Endorsement No. 04 - Amended Condition-Other Insurance

This amendment revokes the payment of a claim under this Policy if insurance is available from another policy (e.g., PHA general liability policy or contractor's insurance). Neither this endorsement nor any of the exclusions limits the coverage under the PHA's general liability policy as suggested by your memorandum's reference to exclusion f. This endorsement prevents double coverage or expanded coverage limits, but it does not appear to void coverage as to the remaining insureds under the Policy (it only voids coverage as to the insureds that are covered by other insurance).

Endorsement No. 05 - Amended Condition-Cancellation

Paragraph 2 allows a PHA/IHA to unilaterally cancel this Policy. We would suggest that this action be taken after notice to HUD and after procurement of alternative coverage. We are unaware whether HUD is requiring this additional lead-based paint insurance or if certain PHAs have reviewed their existing policies with counsel and their insurance companies regarding pollution coverage.

Endorsement No. 06 - Amendatory Condition-Warranty

The insured warrants that it will comply with the most current Regulations and Guidelines. Although this endorsement makes the Guidelines mandatory, the Guidelines state that they are not mandatory (except where the Guideline is based on statute or regulation). HUD could make the Guidelines mandatory through rulemaking; however, this endorsement effectively makes the Guidelines mandatory for purposes of lead-based paint testing and abatement covered by the Policy.

Additionally, the endorsement does not define a "specific warranty violation." There should be guidance regarding major

5

vs. minor violations of the Guidelines.

By styling the endorsement as a warranty, the insurer may allege that the insured's failure to follow the Guidelines results in forfeiture of coverage (i.e., Exclusion 2.a of the CGLC Form excludes liability for bodily injury or property damage expected or intended from the standpoint of the insured). It may be argued that the insurer has shifted the risk of the contractor's improper conduct from the insurer to the insured,

leaving limited coverage for the kind of conduct the insurance was designed to provide. This may not be fatal, but it deserves additional clarification. The endorsement also does not provide for an effective cancellation date.

Endorsement No. 07 - Amendatory Condition-Claim Reports

We do not have any comments regarding this endorsement.

Endorsement No. 08 - General Amendatory Conditions

Paragraph 4 provides that expenses incurred by the insurer in the settlement or adjustment of any claim are payable in addition to the limit of insurance. The Supplementary Payments in the CGLC Form requires the insurer to defend the insured and pay all expenses associated with defense in addition to the limits of liability. There is a potential conflict between Paragraph 4 and the Supplementary Payments clause. It could be interpreted that Paragraph 4 nullifies the Supplementary Payments clause.

Paragraph 6 states that the limit of insurance (\$1,000,000 each occurrence) is not affected by the number of insureds, claims or person making claims. Paragraph 7 states that each incident of "Advertising Injury" or "Personal Injury" shall be deemed an "occurrence" for the purposes of the Policy. Further, claims arising out of the same incident or a series of interrelated incidents shall be treated as a single occurrence. These paragraphs and the definition in Section V.9. of the CGLC Form could be interpreted to limit the insurance to one occurrence per insured (maximum of \$1 million per insured). However, it could also be argued that Paragraph 7 is limited to coverage for "Advertising Injury" or "Personal Injury" which is separate from liability coverage for bodily injury or property damage. It is also significant that the Policy does not contain an aggregate or annual aggregate, which may suggest that the coverage is not limited as may have been suggested by the AKOO opinion. Additionally, PIH 91-3, Insurance Requirements for the Testing, Abatement, Clean-up and Disposal of Lead-Based Paint in Public and Indian Housing states in paragraph 3(b) of the Minimum Requirements that the "minimum limit of liability shall be

6

\$1,000,000 per occurrence combined single limit for bodily injury and property damage without an annual aggregate. The PHA shall determine whether this limit is adequate based on the circumstances existing."

As written, the extent of coverage is subject to varying interpretations. The insurer would probably argue that multiple claims resulting from testing or abatement in a public housing project (consisting of all buildings covered by the testing or abatement work contract) constitutes one occurrence and only \$1 million would be available for the claims. The insured should argue that testing or abatement in each unit constitutes an occurrence and the \$1 million limit of insurance would apply to

each claim. The term "occurrence" should be defined more precisely in order to provide for more claim coverage. Claims arising out of the same testing or abatement activities should be discussed in a way to avoid the limitation of one claim per insurance contract or one claim for each contract for testing and abatement.

#### Endorsement No. 09 - Additional Amendatory Condition

We do not have any comments regarding this endorsement.

#### Scenarios

- I. A random number of units are tested and all are found free of lead-based paint. Therefore, no abatement is needed. Later on, a claim arises from a tenant in a unit that was "not tested" and that unit is discovered to have lead-based paint.

Your memorandum states that you have been informed by the insurance company that there would be no coverage under the Policy since this particular unit was "not tested." It is our opinion that the unit "not tested" would be covered by the Policy only if it was part of the units counted in determining the size of the random sample, and the insured followed the Guidelines and Regulations. See our opinion regarding Endorsement No. 01 for a complete discussion of this situation.

- II. If a unit that was tested and was found to be lead-free is checked again, and it is found that this unit, in fact, did contain lead-based paint and the testing was improperly done, would the tenant in the contaminated unit have a valid claim?

As long as this bodily injury was not expected or intended by the insured, the insured would probably have a valid claim

7

under the Policy. This sounds like a question which would turn on the surrounding facts (e.g., the negligence of the insured or its contractors, major vs minor violations of the Regulations or Guidelines, possible cancellation of the policy, and the intentions of the insured). However, see our opinion regarding Endorsement No. 06 for a complete discussion of problems related to the warranty condition and our opinion regarding Endorsement No. 01 regarding trigger of coverage (issue relating to the Policy's requirement that both the occurrence and the bodily injury must occur during the policy period).

- III. Similar to scenario II above, but in this case, the claim is made by a tenant in an untested unit and the untested unit is found uncontaminated.
- III. Similar to scenario II above, but in this case, the claim is made by a tenant in an untested unit and the untested unit is found uncontaminated.

Your memorandum suggests that there would be no coverage, but on the other hand liability would be questionable. We agree that this claim would not be covered by the Policy unless the untested unit was part of the units counted in determining the size of the random test. If the unit was part of the units counted in determining the size of the random test, the Policy should cover defense costs. However, see our concerns regarding Paragraph 4 of Endorsement No. 08 (potential conflict between Paragraph 4 and the Supplementary Payments clause regarding duty to defend). If this claim was not covered by the Policy, the PHA should determine whether this claim is covered by any other policy (e.g., general liability policy), and if not, the PHA would have to defend this case by showing the validity of the test results and presenting any additional evidence regarding other sources of lead poisoning unrelated to the unit.

IV. A claim is made by a tenant in a unit that was  
physically tested and found uncontaminated.  
IV. A claim is made by a tenant in a unit that was  
physically tested and found uncontaminated.

Your memorandum concludes that there would be coverage and the insurance company would have to defend the suit. However, you suggest whether or not the claim would be paid would depend upon a re-test to confirm the original test was correct. As indicated in our responses to Scenarios II and III above, this claim should probably be covered (except for problems related to Endorsements Nos. 1 and 8). It would be an evidentiary question regarding the validity of the test.

#### Recommendations on Methods of Dealing with Exposures

We are available to discuss the options related to insurance and the improvement of the Policy. As pointed out by the IG Review and the AKOO opinion, there are alternatives to insurance such as statutory exclusions or indemnification, which you may

8

want to explore further. We can also assist you in following up on any of the IG Review's recommendations.

Attachments