7/6/92

DIAMOND SHAMROCK CHEMICALS COMPANY,

Plaintiff-Petitioner,

v.

AETNA CASUALTY & SURETY COMPANY, et al.,

Defendants-Respondents.

: SUPREME COURT OF NEW JERSEY
:
: DOCKET NO. 35,462
:
: Civil Action
:
: ON PETITION FOR CERTIFICATION
: FROM THE FINAL JUDGMENT OF
: NEW JERSEY SUPERIOR COURT,
: APPELLATE DIVISION
:
: Sat Below:
: Superior Court, Appellate
: Division
: Judges Baime, Antell and
: Long, J.A.D.

PETITION FOR CERTIFICATION OF DIAMOND SHAMROCK CHEMICALS COMPANY

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PETITION FOR CERTIFICATION AND APPENDIX

Plaintiff-Appellant-Cross-Appellee Diamond Shamrock Chemicals Company ("Diamond") hereby petitions for certification to this Court of the final judgment of the Appellate Division, Dkt. No. A-694-89T2 filed, following reargument, on June 4, 1992, with respect to those portions of the Appellate Division's judgment which denied Diamond's appeal and granted in part certain excess insurers' cross-appeals with respect to insurance coverage for (a) environmental damage claims and (b) Diamond's contribution to settlement of a product liability class action involving Agent Orange.

I. Statement of the Matters Involved

a) Denial of Coverage for Environmental Damage Claims

The Chancery Division denied Diamond coverage for its environmental liabilities principally on the basis of the "expected or intended" exclusion. The Court's factual findings with respect to the environmental damage in question (i.e., soil and groundwater contamination), however, do not establish any more than negligence or, arguably, gross negligence. The principal purpose of liability insurance is to protect insureds from negligence and gross negligence liability awards, and the case law construing the "expected or intended" exclusion accordingly sets a higher standard than negligence or gross negligence. The Appellate Division acknowledges in its opinion that the

"expected or intended" exclusion "has received uneven treatment and has yet to be authoritatively resolved by our Supreme Court" (slip op. at 50). Diamond submits that the exclusion requires actual expectation of or intent to cause the harm in question and that the better reasoned case law supports this. The question requires clarification by this Court.

The Appellate Division, apparently recognizing the inadequacy of the Chancery Court's factual findings but agreeing with the result, substituted its own new and different findings (slip op. at 51-54) for those of the Chancery Division. The Appellate Division, however, was not present at the trial, could not assess the credibility of the witnesses and should have reversed and/or remanded for further findings by the Chancery Division.

The Appellate Division's ruling, if upheld, threatens the ability of New Jersey businesses, municipalities and utilities to respond to the many pressing environmental problems in this State. Prompt and effective funding is an urgent requirement for remediation of the many of the environmental sites which the NJ DEP has found to be a threat to the health and welfare of the citizens of New Jersey. An indispensable source for that funding is the comprehensive general liability insurance that businesses, public utilities and

municipalities historically purchased to protect themselves and the public from unanticipated liabilities of this kind.[1]

Moreover, the Appellate Division has set a very dangerous precedent. By taking out of context a few isolated incidents from the trial record and using these to condemn the entirety of an eighteen year course of conduct at a multi-faceted operation, the Appellate Division has sent an unfortunate message to all insurers with respect to New Jersey pollution sites. If insurers attack their insureds hard and long enough, they may be able to escape their obligations to cover their insureds' liabilities for clean up of New Jersey pollution. Insurance companies will be encouraged to engage in years and years of very expensive discovery in hopes of uncovering some disgruntled former employee or some scrap of paper upon which to base their expected or intended defense. In the interim, necessary cleanup will be hampered.

b) Denial of Coverage for
Agent Orange Products Liability Claims

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1 Diamond respectfully refers the Court to the amicus brief filed in the Appellate Division on behalf of the New Jersey League of Municipalities and the New Jersey Institute of Municipal Attorneys. Since that brief was filed, the United States Court of Appeals for the Second Circuit in B.F. Goodrich Co. v. Murtha, 958 F.2d 1192 (2d Cir. 1992), held that municipalities may be subject to liability under the Comprehensive Environmental Response, Compensation, and Liability Act of 1980 for the disposal of municipal waste which contains hazardous material (958 F.2d at 1199).

Diamond paid $23.4 million in settlement of product liability claims against it arising out of Agent Orange and sought coverage from its insurers. Diamond's primary insurer, Aetna, admitted coverage in the amount of $7.8 million, and its excess carriers denied coverage, purported to "reserve their rights" or ignored the notice of claim. Diamond filed the instant suit seeking full coverage.

The court which handled the underlying Agent Orange claims (the United States District Court for the Eastern District of New York, Hon. Jack B. Weinstein) in an unrelated coverage action by Uniroyal found that the war risk exclusion did not apply to Agent Orange product liability claims and awarded Uniroyal full coverage for its Agent Orange liabilities under policies essentially the same as Diamond's. The Chancery Division found that New York law applied and that Diamond was covered by its policies, applying the law similarly to Judge Weinstein in Uniroyal, Inc. v. Home Insurance Co., 707 F. Supp. 1368 (E.D.N.Y. 1988). Nonetheless, the Chancery Division then awarded Diamond only partial coverage because it applied the arbitrary loss allocation formula employed by Judge Weinstein in the Uniroyal case. That formula, however, depends on facts presented to the Uniroyal court (including by stipulation) which were not presented to the Chancery Division and resulted in full coverage to Uniroyal. Diamond appealed on the basis that it was improper to adopt an arbitrary allocation formula from some other case without a factual

predicate in the record, especially where the result is to undermine to a significant degree the finding of coverage.

The Appellate Division denied every aspect of Diamond's appeal with respect to coverage for its Agent Orange products liability claims, while it chose to grant several grounds of certain excess insurers' cross-appeals. The result is to reduce the significant partial recovery granted by the Chancery Division to virtually nothing. Specifically, the Appellate Division, after finding that New York law applies, flatly rejected Judge Weinstein's interpretation of New York law in Uniroyal, the only case on point, and held that the war risk exclusion (which appears in most of Diamond's excess policies) applies. On the other hand, the Appellate Division affirmed the application of Judge Weinstein's arbitrary allocation formula despite acknowledging the complete absence of any factual predicate in this case. Thus, in applying New York law, the Appellate Division chose not to follow New York legal precedent in Uniroyal but chose to adopt the factual findings of that Court. As noted, those factual findings led to full recovery by Uniroyal, whereas the effect here is to drastically reduce what little recovery Diamond could obtain under its policies which do not have war risk exclusions.

To support its reversal of the Chancery Division on the war risk exclusion, the Appellate Division not only disregarded Judge Weinstein's view of New York law but engaged in more de novo

fact-finding. Specifically, the Appellate Division hinged its decision on its finding that "Agent Orange was not a commercial product. . . . The record fairly shrieks of evidence that Agent Orange was a 'novel weapon of war'. . ." (slip op. at 90). This finding, however, ignores the evidence that Diamond's alleged liability was predicated on the dioxin contamination which occurred in the manufacture of the 2,4,5-T component of Agent Orange, which was the same 2,4,5-T that was used in many commercial products (slip op. at 11). Thus, Diamond's liability was garden variety product liability arising out of an impurity created in a manufacturing process that was used for civilian and military products alike and was not based on some peculiar aspect of Agent Orange. This illustrates the danger of de novo fact-finding at the appellate level.

The Appellate Division then went on, ignoring or misapplying a long line of precedents in this Court and other decisions of the Appellate Division, to reverse the Chancery Division's allowance of prejudgment interest, although Diamond has actually been out of pocket $23.4 million since January 1985.

The above rulings threaten to create a severe disarray in the lower courts of this State both as to the procedure for making findings of fact and as to the substantive law as to the "expected or intended" exclusion, and the timing and number of occurrences, and

call upon this Court to exercise its supervisory powers to prevent a breakdown of the rule of law in favor of ad hoc result-oriented determinations.

On April 16, 1992 Diamond filed a timely motion for reconsideration of the Appellate Division's decision with respect to coverage for Diamond's Agent Orange settlement, which the Appellate Division erroneously believed was completely disposed of by its war risk ruling. On May 7, 1992, the Appellate Division granted reconsideration, and, after further oral argument on May 19, 1992, the Appellate Division filed its decision on all issues on June 4, 1992. Diamond filed its notice of petition for certification on June 22, 1992.

II. Questions Presented

A. Environmental Damage Claims.

1. In an environmental insurance coverage action where intention of the insured is a critical issue to be decided, was it proper for the Appellate Division to equate the standard for determining intent in an environmental insurance case involving non-assaultive business behavior with the standard used in child molestation cases?

2. Where the Appellate Division apparently found the factual findings made by the Chancery Division after full trial to be inadequate, was it proper for the Appellate Division to make its own factual findings on the basis of a cold appellate record, rather than

reversing and remanding with a direction that the Chancery Division make proper findings?

B. Agent Orange Product Liability Claims.

3. Did the Appellate Division abuse its discretion in applying an ad hoc waiver of the requirement that there exist some evidence in the trial court to support acceptance of stipulations and evidentiary findings made by another court in an unrelated case, particularly where that waiver applies only in favor of insurers and not insureds?

4. Did the Appellate Division improperly refuse to apply binding precedent with respect to the propriety of awarding prejudgment interest on liquidated amounts on the basis of its unprecedented interpretation of a standard clause in excess liability policies?

5. Did the Appellate Division abuse its discretion in making de novo factual findings in order to support its reversal of the Chancery Division's holding that a war risk exclusion in certain excess insurance policies did not apply, rather than reversing and remanding to the Chancery Division with a direction that it make appropriate factual findings?

III. Reasons Why Certification Should Be Granted

Certification should be granted here because (1) the appeal presents significant substantive issues which are unsettled and should be resolved by this Court; (2) certain of these issues are presently pending before this Court in another case; (3) certain of these issues are subject to conflicting decisions in the Appellate Division; and (4) the appeal also presents issues with respect to de novo fact finding by the Appellate Division.

1. This appeal presents issues of general public importance that have not been decided but should be settled by this Court.

Certification is appropriate in this case because the appeal presents questions of general public importance which have not yet been but should be settled by this Court: (a) with respect to coverage for environmental claims, determination of the proper test for applying the "expected or intended" exclusion and, in particular, the standard of proof necessary in order to satisfy the insurers' burden with respect to this exclusion, and (b) in terms of coverage for product liability claims, determination of the propriety of wholesale adoption factual findings and stipulations from the record of an entirely unrelated case in order to support an admittedly arbitrary allocation scheme, while refusing to apply the holding of coverage in that case, and the denial of prejudgment interest where the insured had been out of pocket $23.4 million for 4 1/2 years before judgment was entered.

a) Environmental Damage Claims

The Appellate Division in Prudential Property & Casualty Insurance Co. v. Karlinski, 251 N.J. Super. 457 (App.Div. 1991), concluded based on its review of New Jersey authorities that "it is difficult to ascertain a clear weight of authority on the subject of liability insurance coverage for unintended results on intentional acts" (251 N.J. Super. at 464). The Court reviewed the numerous Appellate Division decisions since this Court wrote on the subject in Ambassador Insurance Co. v. Montes, 76 N.J. 477 (1978), including: Allstate Insurance Co. v. Schmitt, 238 N.J. Super. 619 (App.Div.), certif. denied, 122 N.J. 395 (1990); Atlantic Employers Insurance Co. v. Tots & Toddlers Pre-School Day Care Center, Inc., 239 N.J. Super. 276 (App.Div.), certif. denied, 122 N.J. 147 (1990); SL Industries v. American Motorists Insurance Co., 248 N.J. Super. 458 (App.Div.), aff'd as mod., slip op. (June 17, 1992); Morton International, Inc. v. General Accident Insurance Co., Dkt. No. A-895-89T1, Slip Op. (App.Div. October 2, 1991), certif. granted, 127 N.J. 563 (March 2, 1992). Because all of the above decisions, as well as the instant one, involve construction of standard form insurance policy language found in literally hundreds of thousands of insurance policies purchased by insureds in this State, it is vital that this Court give a clear statement of the law of New Jersey with respect thereto in the context of insurance coverage for environmental liability.

b) Agent Orange Product Liability Claims

Diamond is not aware of any decision by this Court which addresses the Appellate Division's rulings with respect to either (1) its ad hoc waiver of the requirement that there be evidence in the record to support the liability allocation scheme adopted by the Chancery Division from an unrelated litigation, particularly where the Appellate Division's ruling, by its terms, applies only in favor of the insurers and not to an insured (slip op. at 66), or (2) its construction of a standard clause in certain excess insurance policies as precluding an award of prejudgment interest, despite the fact the insured has been out of pocket the amount determined by the judgement to be payable under these excess policies for 4 1/2 years. These are both matters which are appropriate for this Court's exercise of its supervisory jurisdiction over the Appellate Division.

2. This appeal presents questions similar to ones presented by another appeal now before this Court.

Environmental Damage Claims

An appeal pending before this Court presents similar questions, i.e., Morton International Inc. v. General Accident Insurance Co., No. 34,341, which involved construction by the Appellate Division of the "expected or intended" exclusion in the context of environmental damage claims. That case, however, involved a ruling on a motion

for summary judgment. The instant appeal involves a decision rendered by the Chancery Division after a full trial on the merits. Therefore, in order to provide a complete resolution of this critical issue, we submit that it is appropriate to grant certification in order to permit consideration of this issue in all of the contexts in which it is presented in the lower courts of this State.

3. The Appellate Division's decision is in direct conflict with decisions of this Court and of other panels of the Appellate Division.

a) Environmental Damage Claims

The decision of the Appellate Division below is in direct conflict with the decisions of the Appellate Division in Prudential Property & Casualty Insurance Co. v. Karlinski, supra, Morton International, Inc. v. General Accident Insurance Co., supra, and the recent decision of this Court in SL Industries v. American Motorists Insurance Co., supra. In Karlinski, the Court, having reviewed all the relevant authorities in detail, held that "where the intentional act does not have an inherent probability of causing the degree of injury actually inflicted, a factual inquiry into actual intent of the actor to cause that injury is necessary" (251 N.J. Super at 464). In Morton International, the Court adopted the following formulation: "Coverage will exist for the unintended adverse results of intentional acts except where the Court determines that the harm involved was so certainly foreseeable to the insured as to have been constructively

intentional" (slip op. at 38-39). Finally, in SL Industries, this Court, stating that "the Karlinski test presents the most reasonable approach", formulated the test as follows:

> "Assuming the wrongdoer subjectively intends or expects to cause some sort of injury, that intent will generally preclude coverage. If there is evidence that the extent of the injuries was improbable, however, then the Court must inquire as to whether the insured subjectively intended or expected to cause that injury. Lacking that intent, the injury was 'accidental' and coverage will be provided" (slip op. at 12).

This Court has yet to resolve the proper test to be applied in the area of coverage for environmental damage. The Appellate Division here acknowledged that the expected or intended exclusion issue "has received uneven treatment and has yet to be authoritatively resolved by our Supreme Court" (slip op. at 50).

This Court should resolve the conflict in the Appellate Division and provide guidance for all the courts of New Jersey with respect to the appropriate construction of the standard form "expected or intended" exclusion in environmental coverage cases. This Court should also reverse the Appellate Division's judgment with respect to its de novo factual findings based on a cold appellate record.

b) Agent Orange Product Liability Claims

The Appellate Division's ruling denying prejudgment interest is directly contrary to the holding of the Appellate Division in Ellmex Construction Co. v. Republic Insurance Co., 202 N.J. Super. 195, 212-213 (App.Div. 1985), certif. denied, 103 N.J. 453 (1986):

> "The equitable purpose of an award of prejudgment interest is compensatory, 'to indemnify the claimant for the loss of what the monies due him would presumably have earned if the payment had not been delayed . . . . The fact remains that . . . the defendant has had the use, and the plaintiff has not, of monies which the judgment finds was the damage plaintiff suffered.'"

As this Court noted in affirming an Appellate Division reversal of a trial court's denial of prejudgment interest in Meshinsky v. Nichols Yacht Sales, Inc., 110 N.J. 464, 478 (1988):

> "As the Appellate Division noted, '[o]nce the trial judge concluded that plaintiff's rescission of the contract * * * was proper * * *, the damages awarded were "capable of ascertainment by mere computation"' . . . . We are in accord with the Appellate Division's conclusion that under the circumstances the denial of prejudgment interest was an abuse of discretion."

While the Appellate Division acknowledged these decisions, it found them overridden by a provision of the excess insurance policies which provides that "[l]iability under this Policy with respect to an occurrence shall not attach and unless and until the Assured, or the Assured's underlying Insurers, shall have paid or have been liable to pay the amount of underlying limits on account of such occurrence" (slip op. at 102). This wording is a standard clause

found in virtually every commercial excess liability policy and, thus, the Appellate Division has created an exception that threatens to swallow the rule. In the absence of a clear provision excluding prejudgment interest (which the Appellate Division found did not exist), the Appellate Division's ruling is directly in conflict with the law of this State. See, e.g, Rova Farms Resort, Inc. v. Investors Insurance Co., 65 N.J. 474, 512 (1974), "the basic consideration is that the defendant has had the use, and the plaintiff has not, of the amount in question."

IV. This Appeal Calls For An Exercise Of The Supreme Court's Supervision Of The Appellate Courts

As noted with respect to both the denial of coverage for environmental damage claims and the elimination of most of the coverage for the Agent Orange product liability claims, the Appellate Division has engaged in de novo fact finding based on a cold appellate record. The Appellate Division did not have the opportunity to assess the credibility of witnesses or to put particular items of evidence into proper context. As this Court has stated on numerous occasions, appellate courts should exercise extremely sparingly the power to make factual findings based on a cold appellate record. State v. Whitaker, 79 N.J. 503 (1979); Leimgruber v. Claridge Associates, Ltd., 73 N.J. 450 (1977). Particularly where, as here, the appellate fact-finding results in severe prejudice to the party

against which the findings have been made, it is appropriate for this Court to exercise its supervisory powers to correct the Appellate Division's abuse of discretion.

V. Errors Complained of and Comments on the Appellate Division's Decision

a) Environmental Damage Claims

In reaching the decision it did, the Appellate Division appeared to give great weight to the findings made by the Chancery Division with respect to Diamond's alleged deliberate dumping of waste materials to the Passaic River, although it acknowledged that Diamond had not been asked to clean up the River and that its liability for environmental damage related to the soil and ground water at and adjacent to its former plant site (slip op. at 12). In doing so, the Appellate Division made reference to Evidence Rule 46 (id.). The applicability of this Rule was neither briefed nor argued by the parties in the Chancery Division or on the Appeal, and Diamond submits that the reliance on Evidence Rule 46 is entirely misplaced. Neither damage to nor cleanup of the Passaic River is at issue in this case.

Although the decision of the Appellate Division pays lip service to is the Karlinski decision (slip op. at 50), its recitation of the evidence fails to meet the test established in Karlinksi. The record does not support a finding that Diamond expected or intended

the environmental harm to the soil or groundwater for which it was found to be legally liable as a result of newly enacted laws and recent scientific detection techniques some 14 years after it ceased operations at the Lister Avenue plant, nor do the factual findings of the Chancery Division meet this standard.

While the Appellate Division purported to describe the evidence supporting its own finding that Diamond subjectively intended to harm the environment, its description makes clear that the record does not support that finding. It relied principally on the knowledge of Diamond with respect to the risk of chloracne, a severe industrial skin condition caused by concentrated workplace exposure to an impurity in certain herbicides produced at Diamond's plant (slip op. at 51-53). None of this evidence related to the alleged harm to the soil and groundwater for which Diamond was found liable 14 years after it stopped operating the plant. The rest of the recitation is based on evidence of Diamond's sloppy housekeeping and negligence with respect to the handling of certain valuable industrial chemicals (slip op. at 52-54), but again no evidence is pointed to -- there is none -- that Diamond "expected or intended" the contamination of soil and groundwater which was found in 1983. Although the Appellate Division "recognize[d] that we should not judge Diamond's conduct from the vantage point of twenty-twenty hindsight" (slip op. at 54), that is precisely what the Court did here. Neither the Chancery Division nor the Appellate Division had any basis to make the

critical findings necessary under Karlinski and the other cases cited above.

By failing to properly apply Karlinski, the Appellate Division has created a situation in which what was at most evidence of sloppy housekeeping and negligence with respect to the environmental consequences, to the limited extent known, of its day-to-day operations, became grounds for effectively reading negligence out of comprehensive general liability insurance coverage.

In Morton International there were findings of knowing and intentional environmental damage from deliberate dumping of wastes containing mercury. In contrast, Diamond's ordinary operations resulted in introducing valuable industrial chemicals into the environment because Diamond's storage and handling of the chemicals was negligent or, at worst, grossly negligent. The Appellate Division failed to draw the kind of clear line that must be drawn between deliberate dumping of toxic wastes and negligent or sloppy housekeeping if environmental cleanup in this State is to go forward an an acceptable pace. This is precisely the kind of question which this Court is suited to resolve.

b) Agent Orange Products Liability Claims

Having upheld the Chancery Division's ruling that New York law is applicable to the determination of coverage for Diamond's

settlements of the Agent Orange products liability class action, the Appellate Division refused to follow the only decision applying New York law directly on point, Uniroyal, Inc. v. Home Insurance Co., supra (slip op. at 77-78), relying instead on a mish-mash of decisions involving different exclusions and clauses, which the Court admitted are not directly on point (slip op. at 84). The Appellate Division upheld the Chancery Division's adoption of an arbitrary allocation scheme, based upon assumptions contradicted by facts of record (e.g., that all of Diamond's Agent Orange was sprayed in Viet Nam, while the evidence is that a significant part of Diamond's Agent Orange was never used), on the basis of evidence and stipulations among the parties in the Uniroyal case. The Appellate Division remarkably admitted that "we know of no evidentiary rules that would permit judicial notice of this material [and we] also acknowledge the danger of uncritically accepting representations concerning documentary evidence in an entirely different court in an unrelated case" (slip op. at 65-66). Incredibly, the Court also stated that if "the insurers were to attack the accuracy or existence of this evidence, we would undoubtedly be obliged to reverse and remand for a plenary hearing" (id.; emphasis added). Diamond did dispute the existence and accuracy of that evidence, but the Appellate Division nonetheless affirmed the Chancery Division.

Finally, the Appellate Division's ruling that Diamond's excess insurers are not obligated to pay prejudgment interest because

"the primary policies have not been exhausted and there was no adjudication of the primary insurer's responsibility to pay the policy limits" (slip op. at 103), fails to apply the decisions of this Court and other panels of the Appellate Division, which make clear that the purpose of an award of prejudgment interest is compensatory.

CONCLUSION

For all the foregoing reasons, it is respectfully requested that this Petition for Certification be granted.

CERTIFICATION

I certify that this Petition presents substantial questions and is filed in good faith and not for purposes of delay.

Dennis R. LaFiura, Esq.

Dated: July 6, 1992

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