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INSURERS DODGE THE ASBESTOS TRAP

The traditional cozy relationship between insurance carriers and corporate policyholders has been strained by a high-stakes legal battle over occupational health liability. The troubles may only be beginning.

BY PAUL G. ENGEL

Who pays? How much? And when?

As one insurance executive puts it: "The answers are fairly easy when you're talking about a car accident or somebody getting his hand cut off in a machine." But when a multibillion-dollar corporation is awash in litigation over a commonly used toxic substance—and when four federal appeals courts have issued three different legal interpretations—the answers are a bit more elusive. "If I had an answer, I'd bottle it and sell it," quips the insurance executive.

Health hazards, liability, insurance hassles—mention any or all and, chances are, Manville Corp.'s current asbestos woes will be cited. Although there is no denying the catastrophic financial and human consequences, Manville's situation is only a reflection of the potential problems associated with life-threatening substances like diethylstilbestrol (DES), dioxin, or formaldehyde.

Chemical and pharmaceutical firms would seem to be the most vulnerable. But virtually no corporation, no matter how "safe" its product or work environment, can be certain that it is immune to potential liability arising from unexpected health hazards. Corporate risk managers, who make decisions on insurance coverage, talk in upbeat terms about state-of-the-art medical surveillance systems; and their insurance carriers keep lists of suspicious substances. But no one really knows where the next "asbestos" case is lurking—or when it will erupt.

When it does, manufacturers and insurance companies alike may be forced to relive the nightmare of frantic fingerpointing and conflicting court rulings that marked the asbestos controversy.

What's covered? It all seemed so simple 50 years ago. Insurance carriers wrote comprehensive-general and product-liability policies for corporate clients, using standardized language. Premiums were dutifully paid, both for primary and excess coverage. But then, observes Dennis Connolly, senior counsel for the American Insurance Assn. (AIA), New York, "everything changed, both in a legal and scientific sense."

About ten years ago Manville and other asbestos manufacturers and processors began to be hit with lawsuits from former workers, surviving family members, and others who charged that debilitating lung diseases and rare cancers had been caused by contact with asbestos 20, 30, or even 40 years earlier.

At the latest count there were more than 13,000 claims pending. Roughly 3,500 claims have been settled—with awards averaging an estimated $76,000.

Workers compensation statutes, which normally provide benefits for job-related illness and injury, have tra-

Is the insurer at the time of exposure liable, or . . .?

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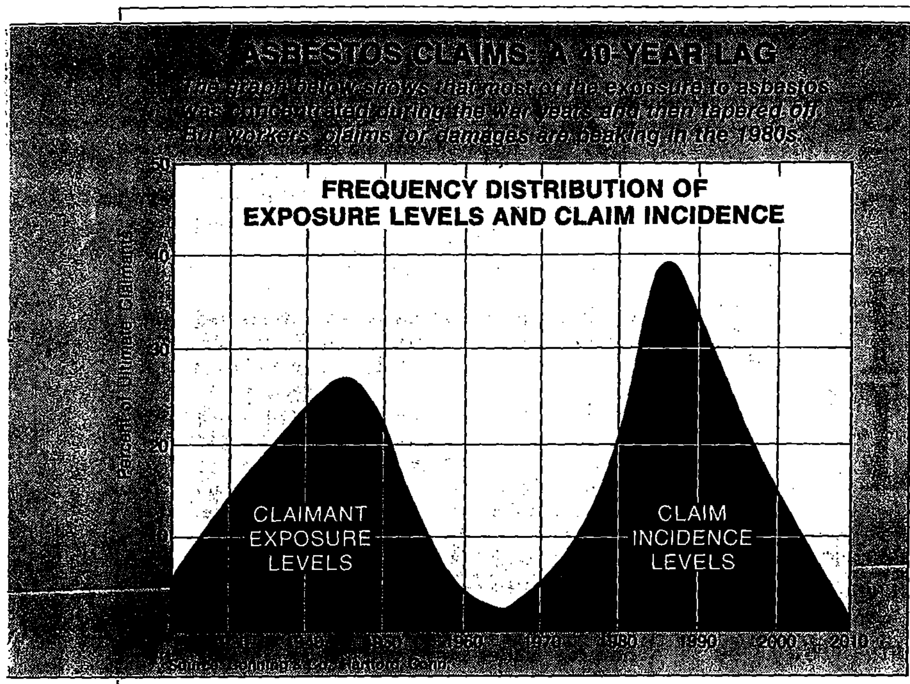

Chart/ John Szucs

ditionally offered little, if any, occupational-disease coverage. Hence, the rush to the courthouse.

When Manville and the other asbestos defendants looked to their insurers to live up to what they saw as the clearcut language in their policies, they got a rude awakening. Marcy Kahn, an attorney with Anderson Russell Kill & Olick, a New York law firm which represents one of the defendants, Keene Corp., a diversified New York firm, recalls: "Our litigation started, so we went to [Keene's] insurers and said, 'It's time to defend and indemnify.' Their response was, 'Well, not really.'"

"Few, if any, people knew of the hazards of asbestos 30 or 40 years ago," explains the AIA's Mr. Connolly, "and the policies issued then were not written to cover the losses being experienced today." Of course, plaintiffs—the workers—and their attorneys argue vociferously that both the asbestos companies and their insurance companies knew—or should have known—of the dangers involved.

Pick a theory. In any case, some of the nation's largest insurance companies were soon faced with the prospect of paying out hundreds of millions of dollars in claims —with no limit in sight. Diving back into their policies and taking a flinty look at the liability language, insurers broke into two widely divergent camps over the meaning of the word "occurrence" and when a particular company's liability coverage was triggered.

One camp embraced the "exposure theory"—contending that the insurer that wrote the policy at the time the victim was breathing asbestos dust should be held responsible. But other carriers asserted a "manifestation theory," claiming that the burden was on the insurer that held the policy when the disease was finally diagnosed—usually decades after the initial contact with asbestos.

Critics dismiss the insurance industry split as a rationalization for welching on solid, paid-up policies. Carriers choose one theory or the other, it's argued, depending on which will minimize their losses.

"It looks like hell when someone says he's insured, and the carrier says no," acknowledges one insurance executive. "It's bad for the industry." But most insurers maintain that their decisions have been based solely on medical and scientific evidence, rather than financial considerations. "With all the different approaches taken on definitions of policy language," says John Shea, vice president and claims counsel at Aetna Life Insurance Co., "at least we can't be accused of a conspiracy to adopt one uniform position." (Aetna has adopted the manifestation theory in most cases.)

NO LEGAL CONSENSUS

In March 1980, having paid more than $6 million in liability premiums, Manville filed suit in a California state court against its carriers, alleging breach of contract.

"The whole subject disgusts me," says John McKinney, Manville's chairman, president, and CEO. He blames insurance-carrier recalcitrance for the company's decision to file for bankruptcy last summer. The day after the Chapter 11 filing, Manville filed additional papers with the California court seeking $5 billion in punitive damages from its insurers. Pre-trial negotiations are still underway.

The legal dispute involves "when, if, and how the company was protected from losses," says Jeffrey Haney, an attorney representing one of Manville's carriers—Commercial Union Insurance Co. "Obviously, our opinion on all three points differs from Manville's."

Federal appeals courts have come down on both sides of the exposure vs manifestation dispute. And last year, in a case in which Keene Corp. sued its insurer, the District of Columbia appellate court issued its own precedent-setting variation—which was quickly dubbed the "triple-trigger" theory.

The D. C. court held that "inhalation exposure, exposure in residence [to substances that accumulate in the body], and manifestation *all* trigger coverage under the policies." Under the decision each carrier's financial obligation would be prorated, based on the number of years it provided coverage.

One common thread in all of the disparate court decisions on asbestos coverage is that all have been decided in favor of the corporate policyholders. Although the U. S. Supreme Court has repeatedly rejected appeals seeking a definitive judgment, most observers expect that the high court will eventually issue a ruling to resolve the lingering legal, medical, and policy-language conflicts.

Infighting. Meanwhile, relations between corporate asbestos defendants and their insurance carriers remain strained. "Keene has had lots of difficulty and little or no cooperation from its insurers," says Ms. Kahn, the firm's outside attorney. "Exhorbitant premiums and high deductibles have, in effect, meant that the company was uninsured. The carriers protected their interests, and didn't look out for ours."

Thomas O'Day, assistant vice president of the Alliance of American Insurers (AAI), a Chicago-based carriers' group, counters: "Contrary to what some may say, insurers don't like to fight with clients, whether an individual or a corporation." But he quickly adds: "We also believe in responsible people being held responsible."

The insurance industry looks foolish, argues Anthony Lanzone, a partner with Lanzone & Kramer, New York, when carriers are unable "to make a determination and tell

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the courts what was intended." The result of such infighting, he concludes, could be "a number of insurance companies whose names are going to be quoted in the *past tense*."

Liability losses. Liability insurance—which covers a wide range of hazards—has never been a highly profitable venture for insurance carriers. And, over the last few years, it has been a money-loser.

The problem, insurers note, is falling interest rates. Explains AAI's Mr. O'Day: "When interest rates were running at 20% and higher, the return that carriers were getting on their investments more than made up for any underwriting losses. But even though interest rates have come down appreciably," he adds, "insurers have continued to write liability policies at a loss. The safety net between investment income and underwriting losses is shrinking."

Observers agree that shrinkage will cause insurance rates to go up over the next 12 months. Few, however, expect a repeat of the volatile mid-1970s when, recalls one insurance executive, "carriers panicked . . . and rates went through the ceiling, then fell just as quickly when the expected losses didn't materialize."

With rates on a downward slide for the last few years, liability insurance has been a buyer's market. "Any risk manager worth his salt is going to get what he's paying for—the best policy he can buy," asserts Justin Murphy, insurance manager at Nestle Co. Inc., White Plains, N. Y. Mr. Murphy and many of his peers have trimmed their premiums by assuming large deductibles. "We use our insurance company primarily as a claims processor," he explains.

How narrow? One insurance industry insider is uneasy over what is being bought and sold in the soft liability market. "Companies want broadly worded liability policies which allow interpretation," he points out, "but the Manville situation has shown that that can lead to controversy and ligitation. Conversely, insurers want to write narrow policies to protect themselves. But, if they do, they have to ask: 'Who's going to buy it?'"

Carriers fear that loose, inexpensive policies will come back to haunt them. Myra Tobin, a managing director with the New York-based brokerage firm of Marsh & McLennan, warns: "The premiums being collected today are not sufficient to cover the next asbestos-like hazard that comes along."

One thing that's needed, contends Ms. Tobin, "is closer communication between the underwriting and the claims departments in each insurance company." What's happening now, she says, "is that the people doing the underwriting are on the offense—they have a green light to write policies. Then a claim comes due, and the defense goes in. The claims department's job is to find a way not to pay a claim."

INSURANCE AGAINST INSURERS?

How do you cope with problems in interpreting the language of liability policies? That depends on your point of view.

- The Insurance Services Office (ISO), New York, a voluntary ratemaking and standards-setting body representing insurance carriers, is attempting to draft a simplified version of the basic general liability policy sold to corporate customers. An ISO draft was circulated last summer and a final version is expected sometime in 1985. However, its applicability may prove to be limited, since most corporate risk managers use such standard policies only as a steppingstone in designing the protection their companies need. "We'll start out with the standard form, and then make 40 changes concerning cancellation-of-policy language, notice of accident terms, and the like," advises Richard VanWagoner, risk manager at Phelps Dodge Corp.
- Companies suspecting that their policies aren't ironclad might want to consider insuring themselves against their insurers. One New York broker—Professional Indemnity Agency Inc.—is now offering a policy that would cover up to $5 million in legal fees in the event that a company becomes embroiled in litigation over coverage with its primary insurance carrier.

WORST IS YET TO COME

Some answers on handling asbestos claims are needed soon—to avert bigger headaches later. Exposure statistics indicate that the brunt of asbestos-related litigation won't be felt until later in this decade. (See chart on Page 26.)

At the moment, plaintiffs in damage suits seem to have the upper hand. A report commissioned by the insurance industry indicated that the attorneys for the asbestos victims are better organized than the attorneys representing corporate defendants. At least one company lawyer concurs. At a legal seminar sponsored by the Center for Public Resources in New York earlier this year, Robert Sand, general counsel for Allied Corp., complained: "We are our own worst enemy." Referring to the lack of cooperation between corporate defendants in toxic tort suits, he added, "We are settling many cases—not because the plaintiffs are so good, but because we are so *bad*."

Lack of unity is also evident among insurers. The insurance industry report, issued late last year by Hamilton, Rabinowitz & Szanton, Los Angeles consultants, urged the creation of an independent body to improve asbestos claims-handling. The result was the formation earlier this year of the Asbestos Claims Council representing 11 major asbestos insurers.

The council "will establish uniform funding and coverage [guidelines], establish a central claims facility, and propose streamlined court proceedings for those cases which are litigated," explains Raymond Stahl, chairman of the new group and a senior vice president at Travelers Insurance Cos. "Not every case needs to go to trial."

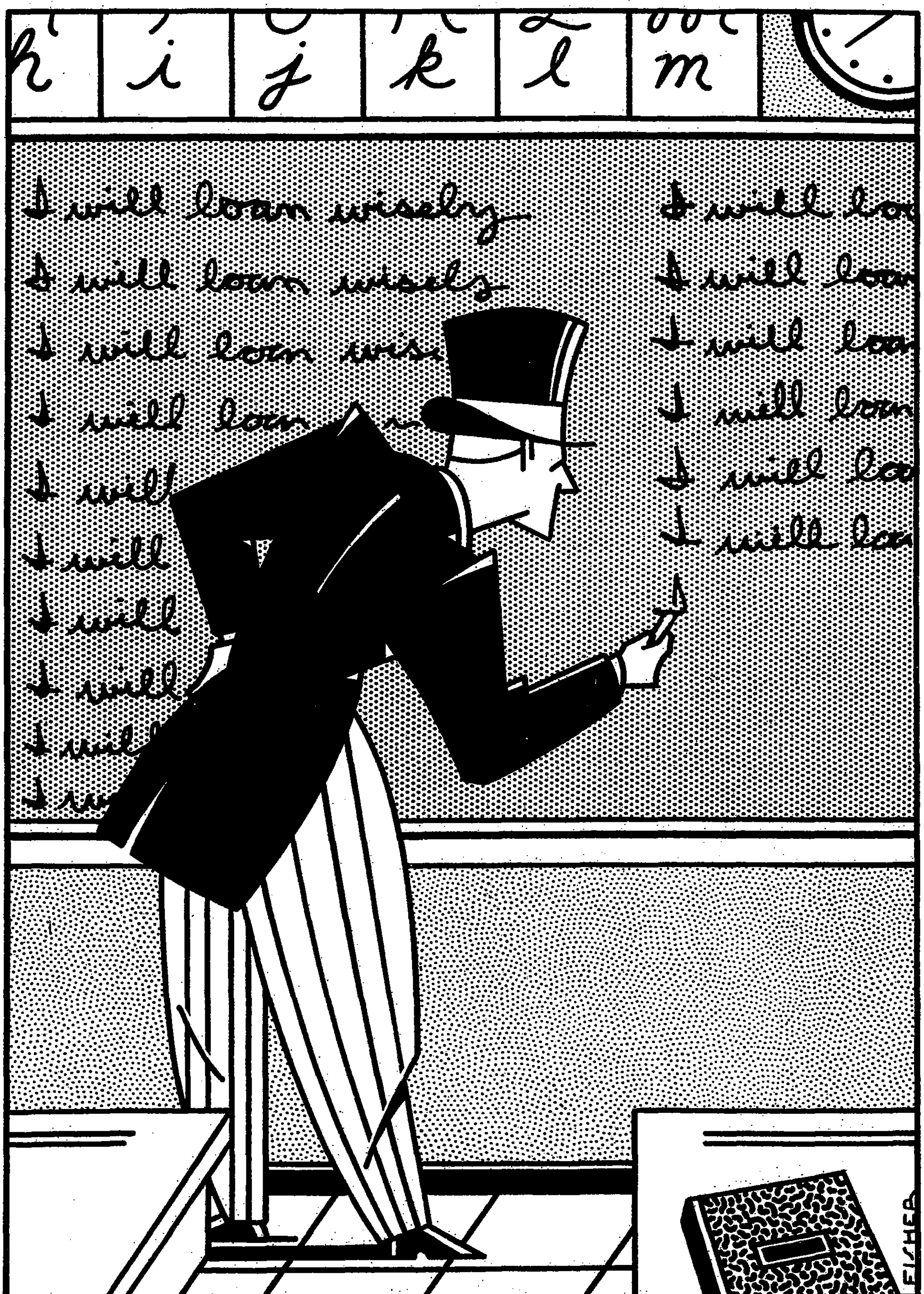
Bailout? Asbestos companies have been hoping for some sort of legislative solution, a solution under which the federal government would pay a share of any damage costs to the victims, many of whom were exposed to asbestos as workers in government shipyards during World War II.

Rep. George Miller (D, Calif.), chairman of the House labor standards subcommittee, is planning to introduce a bill that would establish a trust fund, supported by a tax on asbestos companies, to compensate claimants. But he adamantly refuses to include the government in any payment plan.

Obviously, the smartest way to head off liability hassles is prevention of occupational-health hazards.

Nestle's Mr. Murphy doesn't foresee his company experiencing a calamity like that which engulfed Manville. But he talks in good news-bad news terms when commenting on existing safeguards and the possibility of future shocks. By working closely with in-plant safety and health personnel, and Nestle's insurance carriers, "we hope to head hazards off at the pass—to keep abreast of developments and make sure that things don't get out of control," Mr. Murphy notes.

"Our operation and products are fairly simple, thank God, and if any health-related catastrophe came along it would be a hell of a surprise. Of course, I'm sure the asbestos industry felt the same way back in the 1940s." ■



Illustration/ Mark Fisher

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