RECENT DEVELOPMENTS IN PROPERTY INSURANCE COVERAGE LITIGATION

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The survey period in property insurance law saw the emergence of a series of rulings involving coverage for damages caused by Chinese drywall. Cases involving Chinese drywall coverage, which are just beginning to work their way through the courts, will form a significant part of the property insurance landscape for the next few years. The cases raise common property insurance issues about causation, ensuing loss, and certain frequently litigated exclusions, but they raise those issues in unique and challenging ways that defy strict categorization in any of our common survey categories. The resulting complexity of these cases, along with their significance in the property insurance world, led us to highlight them at the beginning of this year's survey.

After reviewing the issues raised by Chinese drywall, we turn to developments in the more common issues that arise out of property insurance contracts. We begin our review by looking at significant developments in key areas of the risk transferred to the property insurer where disputes are frequent, namely the business interruption and collapse coverages. Then, we turn our focus to significant cases addressing what property is actually "covered" under the insurance contract, and then to notable cases dealing with the most common exclusions in the property insurance contract. Regular followers of this area of the law will observe that the survey period saw

some very interesting cases on the issue of "covered property." They will also note that those exclusions that usually rely heavily on fact-specific issues for their application, such as the exclusions for damage caused by earth movement or mold, continue to give rise to challenging cases that turn on a careful review of the facts, and that result in opinions that—while often thoughtful—defy easy categorization into clean rules of interpretation.

I. COVERAGE FOR CHINESE DRYWALL CLAIMS

In 2006 and 2007, the southeastern United States experienced an increase in new home construction and renovations. This increase was due, in large part, to the number of hurricanes that affected the region in 2004 and 2005. Homes that were totaled had to be rebuilt, and damaged homes had to be renovated. In addition, the United States was in a housing boom. Because of the unprecedented need for building materials, domestic drywall manufacturers were unable to keep up with the demand for drywall. This led suppliers, contractors, and builders to look for an alterative drywall source. Chinese drywall suppliers stepped in to meet the demand.

Shortly after installation of Chinese-produced drywall, some homeowners began to notice a "rotten egg" smell in their homes. Electronics and air-conditioning units in those homes began to fail for unknown reasons, and metal components began to blacken, pit, and corrode.

The U.S. Consumer Product Safety Commission ("CPSC") received its first report of a possible Chinese drywall incident from a consumer on December 22, 2008. As of December 16, 2010, the CPSC had received about 3,756 reports from residents in forty-one states, the District of Columbia, American Samoa, and Puerto Rico who believe their health symptoms or the corrosion of certain metal components in their homes are related to the presence of drywall produced in China.[1]

Testing of suspected Chinese drywall has confirmed that sulfur compounds can be released from the drywall and cause corrosion to metal components within homes.[2]

Many homeowners that suspected damage from Chinese drywall made claims with the insurer that wrote their homeowners' insurance. Typically, those insurers have denied coverage, relying on policy exclusions for latent defect, corrosion, faulty materials, and pollutants. A typical homeowner's policy incorporates the following exclusions:

1. *Where Has Problem Drywall Been Reported?*, U.S. Consumer Prod. Safety Comm'n, Drywall Info. Ctr., http://www.cpsc.gov/info/drywall/where.html (last visited Dec. 20, 2010).
2. *Executive Summary of April 2, 2010, Release*, U.S. Consumer Prod. Safety Comm'n, Drywall Info. Ctr., http://www.cpsc.gov/info/drywall/execsum0410.pdf.

SECTION I—PERILS INSURED AGAINST

* * *

COVERAGE A—DWELLING and COVERAGE B—OTHER STRUCTURES

We insure against risk of direct loss to property described in Coverages A and B only if that loss is a physical loss to property. We do not insure, however, for loss:

* * *

2. Caused by:
   e. Any of the following:
      (2) Inherent vice, latent defect, mechanical breakdown;
      (3) Smog, rust or other corrosion, mold, wet or dry rot;
      * * *
      (5) Discharge, dispersal, seepage, migration, release or escape of pollutants unless the discharge, dispersal, seepage, migration, release or escape is itself caused by a Peril Insured Against Under Coverage C of this policy. 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;

* * *

3. Excluded under Section I–Exclusions

   Under items 1. and 2., any ensuing loss to property described in Coverages A and B not excluded or excepted in this policy is covered.

* * *

SECTION I—EXCLUSIONS

2. We do not insure for loss to property described in Coverages A and B caused by any of the following. However, any ensuing loss to property described in Coverages A and B not excluded or excepted in this policy is covered.

* * *

   c. Faulty, inadequate or defective:
      (3) Materials used in repair, construction, renovation or remodeling;

of part or all of any property whether on or off the "residence premises."[3]

3. Insurance Services Office Form No. HO 00 03 04 91.

Those claim denials resulted in homeowners filing suit against their carriers for breach of contract. In some cases, insurers have filed declaratory judgment actions, asking courts to determine whether coverage exists under their insurance policy. Several lawsuits filed by homeowners against their insurers are part of the multidistrict litigation ("MDL") currently pending in the U.S. District Court for the Eastern District of Louisiana.[4] In response to these lawsuits, several insurers filed motions to dismiss and for judgment on the pleadings. These motions address the application of exclusionary language similar to that cited above. In addition, two Louisiana state courts and a Virginia federal district court have ruled on Chinese drywall coverage issues under first-party homeowner's policies.

A. *Finger v. Audubon Insurance Co*.

On March 22, 2010, a trial court sitting in the Civil District Court for Orleans Parish, Louisiana, issued the first decision regarding a Chinese drywall claim under a property policy in *Finger v. Audubon Insurance Co*.[5] The decision arose in the context of the insureds' motion to strike several affirmative defenses asserted by the insurer. The court granted the insureds' motion to strike defenses based on the exclusions for pollutants, "gradual or sudden loss" (which included inherent vice, latent defect, and corrosion), and "faulty, inadequate or defective planning" (which included faulty materials). It analyzed the key exclusions applicable to a claim for Chinese drywall and concluded that those exclusions do not bar coverage for a claim for Chinese drywall.[6] The court did not address whether the Chinese drywall itself sustained direct or physical loss, although it quoted testimony of the insurer's corporate representative that the drywall itself was not damaged directly or indirectly.[7] The court also expressly stated that its decision did not address the question of whether the claim was covered as an "ensuing loss," leaving that issue for another day.[8]

B. *Ross v. C. Adams Construction & Design, LLC*

On April 14, 2010, a Louisiana trial court in neighboring Jefferson Parish reached the opposite conclusion in *Ross v. C. Adams Construction & Design, L.L.C.*[9] That court denied the insureds' motion for partial summary judgment against its homeowners' insurer, Louisiana Citizens Property

4. *In re* Chinese-Manufactured Drywall Prods. Liab. Litig., 706 F. Supp. 2d 655, 2010 WL 5288032 (E.D. La. 2010).
5. No. 2009-08071, 2010 WL 1222273 (La. Civ. Dist. Ct. Mar. 22, 2010).
6. *Id.* at *4–9.
7. *Id.* at *7.
8. *Id.* at *9.
9. No. 676-185, 2010 WL 2916525 (La. Civ. Dist. Ct. Apr. 14, 2010).

Insurance Company, and granted the insurer's cross-motion for summary judgment. Although the judgment itself does not reflect the basis of the court's ruling, the documents filed by the parties in support of their motions and the hearing transcript shed light on the arguments presented to the court.

The insureds argued that the exclusions from coverage for losses caused by pollution, faulty workmanship and defective materials, and corrosion should not apply to preclude coverage for their claim.[10] The insurer requested judgment in its favor on all claims against it, and argued that (1) the insureds' policy provided no coverage for the cost of removing and replacing the Chinese drywall because the drywall had sustained no direct physical loss, and coverage for any loss caused by the defects in the drywall was barred by the exclusions for latent defect, defective materials, corrosion, and pollutants, and (2) the insureds' policy provided no coverage for any damage caused by the drywall or by the discharge of gases from the drywall.[11] The court apparently agreed with the insurer's arguments when it entered judgment in favor of the insurer—in direct conflict with the conclusions reached by the *Finger* court in neighboring Orleans Parish.

The insureds have appealed the trial court's ruling to the Louisiana Court of Appeal. At this writing, each side has filed its respective briefs, but no ruling has been issued.[12]

C. *TRAVCO Insurance Co. v. Ward*

The third significant opinion on Chinese drywall coverage came from the U.S. District Court for the Eastern District of Virginia in *TRAVCO Insurance Co. v. Ward*.[13] In a lengthy opinion, that court granted summary judgment to an insurer that had denied a homeowner's claim. Although the court found that the insured's "residence and its components" had suffered a "direct physical loss"[14] under the policy, the policy's exclusions for latent defect, faulty materials, corrosion, and pollutants applied to preclude coverage for the claimed losses. The court rejected the insured's arguments, including its reliance on the *Finger* decision, that none of the policy exclusions applied, and noted that *Finger* was in conflict with the *Ross* decision.

10. Plaintiffs' Mem. Supp. Mot. Partial Summ. J., Ross v. C. Adams Constr. & Design, L.L.C., No. 676-185, 2010 WL 2520773 (La. Civ. Dist. Ct. filed Jan. 15, 2010).

11. Defandants' Mem. Supp. Cross-Mot. Summ. J. & Opp. Mot. Partial Summ. J., Ross v. C. Adams Constr. & Design, L.L.C., No. 676-185, 2010 WL 2520774 (La. Civ. Dist. Ct. filed Mar. 19, 2010).

12. Original Brief of Plaintiffs-Appellants, Ross v. C. Adams Constr. & Design, L.L.C., No. 10-CA-852, 2010 WL 5015507 (La. Ct. App. filed Nov. 17, 2010); Original Brief of Defendant-Appellee, Ross v. C. Adams Constr. & Design, L.L.C., No. 10-CA-852, 2010 WL 5199349 (La. Ct. App. filed Dec. 6, 2010).

13. 715 F. Supp. 2d 699 (E.D. Va. 2010).

14. *Id*. at 701.

The court addressed individual exclusions in the policy, and assessed whether each one barred individual components of the insured's claim. Specifically, the court concluded that the policy did not cover (1) the cost of removing and/or replacing the drywall in the insured's residence; (2) the corrosion damage claimed by the insured to his air-conditioning equipment, garage door, and flat-screen televisions, and (3) any of the damages caused by the discharge of gas from the drywall, including but not limited to insured's presently claimed damages to the wiring and copper components of the home. The court found none of the claimed losses to be ensuing losses, stating "only a single claimed loss," the off-gassing of defective Chinese drywall, occurred.[15] The court also noted that even if the losses could be characterized as "ensuing losses," they would still be excluded by other provisions of the policy.[16] The court also, however, expressly stated that it would not "categorically rule out the possibility, however, that other unclaimed losses might be subject to coverage" under the ensuing loss provisions of the policy.[17]

Following the court's ruling, the insured appealed to the U.S. Court of Appeals for the Fourth Circuit. At this writing, each side has filed its respective briefs, but no ruling has been issued.[18]

D. *In re Chinese Manufactured Drywall: Products Liability Litigation*

On December 16, 2010, the MDL court issued its much-anticipated ruling on motions to dismiss filed by homeowners insurers on multiple coverage issues related to Chinese drywall.[19] Ruling for the insureds on the issue of "direct physical loss," the court found that the

> Chinese-manufactured drywall has caused a "distinct, demonstrable, physical alteration" of the Plaintiffs' homes by corroding the silver and copper elements in the homes, often to the point of causing total or partial failure in electrical wiring and devices installed in the homes, as well as by emitting odorous gases.[20]

While the mere presence of a potentially injurious material in a home might not qualify as a covered physical loss, the court found a physical

15. *Id*. at 718–19.
16. *Id*. at 719.
17. *Id*. at 707.
18. Brief of Plaintiff-Appellee, Travco Ins. Co. v. Ward, No. 10-1710, 2010 WL 3866762 (4th Cir. filed Oct. 4, 2010); Reply Brief of Appellant, Travco Ins. Co. v. Ward, No. 10-1710, 2010 WL 2010 WL 4064943 (4th Cir. filed Oct. 18, 2010).
19. *In re* Chinese Manufactured Drywall Prods. Liab. Litig., No. 09-MDL-2047, 2010 WL 5288032 (E.D. La. Dec. 16, 2010).
20. *Id*. at *6.

loss when such materials were activated, for example, by releasing gases or fibers.[21] Finally, the court found that the drywall rendered the homes useless and/or uninhabitable due to the damage to the electrical wiring, appliances, and devices, as well as the ever-present sulfur gases, thus constituting physical loss.[22]

Turning to exclusions, the court first found that the "latent defect" exclusion did not bar coverage. Under Louisiana law, the term "latent defect" was " 'a defect that is hidden or concealed from knowledge as well as from sight and which a reasonable customary inspection would not reveal.' "[23] The court rejected *Finger* because that "court commingled its analysis of the inherent vice exclusion and latent defect exclusion."[24] It declined to follow *TRAVCO* because Virginia law and Louisiana law defined "latent defect" differently.[25] The court found that the test for a latent defect focused on the cause "of the underlying defect, and not the results of the defect."[26] Under this test, the exclusion was inapplicable because "the damage caused by the drywall—the odor, the blackened wires and metals—are easily detectable through smell and sight" and because "a skilled worker such as an electrician, would immediately recognize the damage to electrical wiring, devices, and appliances."[27]

Next, relying almost exclusively on the Louisiana Supreme Court's decision in *Doerr v. Mobil Oil Corp.*,[28] the MDL court held that the exclusions for pollution or contamination did not apply.[29] The homeowners were not "polluters," as required by *Doerr*, because "Plaintiffs, who are home owners and occupants, do not constitute polluters under any sense of the word."[30]

Nevertheless, the court held that the faulty materials exclusion barred coverage. The court declined to follow *Finger* because "*Finger* failed to provide an explanation as to how it came to define faulty materials, only citing conclusions reached in the plaintiff's own memorandum and testimony, and the testimony of the insurer's corporate representative."[31] The drywall constituted "faulty materials" because "[a]lthough the drywall serves its intended purpose as a room divider, wall anchor, and insulator, the al-

21. *Id.* at *5.
22. *Id.*
23. *Id.* at *10 (quoting Nida v. State Farm Fire & Cas. Co., 454 So. 2d 328, 335 (La. Ct. App. 1984)).
24. *Id.*
25. *Id.* at *11.
26. *Id.* at *12.
27. *Id.*
28. 774 So. 2d 119, 135–36 (La. 2000).
29. *In re* Chinese-Manufactured Drywall, 2010 WL 5288032, at *12–17.
30. *Id.* at *16.
31. *Id.* at *19.

legations in the complaints provide that the drywall emits foul-smelling odors and releases gases which damage silver and copper components in the home, including electrical devices, appliances, and wiring."[32]

The exclusion for corrosion further barred coverage. The court found that "under a 'plain, ordinary and generally prevailing meaning,' corrosion is defined as 'the action, process, or effect of corroding' and 'a product of corroding.'"[33] The complaints' allegations "that the Chinese drywall in the Plaintiffs' homes emits gases which cause corrosion to metallic and electrical components in the home . . . trigger[ed] the corrosion exclusion since the corrosion is responsible for the majority of losses suffered by the Plaintiffs."[34]

Since all of the insurers, except Allstate, provided coverage for ensuing losses from faulty materials and corrosion, the court analyzed the ensuing loss provision and found that there was no ensuing loss from the faulty materials or corrosion and granted all of the insurer's motions to dismiss. The court also found that the corrosion-related losses caused by Chinese drywall did not constitute ensuing losses but "even assuming that the corrosion or corrosion-caused losses due to the Chinese drywall in Plaintiffs' homes were ensuing or resulting losses, they remain excluded losses because, as discussed above, corrosion and corrosion-related losses are specifically excluded from coverage."[35]

II. BUSINESS INTERRUPTION/CIVIL AUTHORITY

In the wake of Hurricane Katrina, several courts have addressed "experience of the business" clauses and the extent to which actual post-interruption profits should be taken into account in calculating a loss. In *Caitlin Syndicate Ltd. v. Imperial Palace of Mississippi, Inc.*,[36] the court concluded that only historical sales figures should be considered under a clause requiring that the "experience of the business before the loss and the probable experience thereafter had no loss occurred" be considered. In that case, the insured casino had increased revenues following the hurricane as other local casinos were shut down for a longer period, thus driving customers to the insured's facility. The insured unsuccessfully argued that the business income loss should be based on a hypothetical in which Katrina struck but did not damage the insured's facilities—not one in which the hurricane

32. *Id.*
33. *Id.* at *20.
34. *Id.* at *21.
35. *Id.* at *25.
36. 600 F.3d 511, 516 (5th Cir. 2010).

did not strike at all. Construing different policy language, a federal court sitting in Louisiana held that an insured could take into account favorable economic conditions after the loss where the subject policy excluded consideration of "favorable business conditions caused by the impact of the Covered Cause of Loss on customers or on other businesses" to the extent that the favorable conditions were caused by flood, which was excluded from coverage.[37]

Where the term "business income" was defined to include "net income" and "continuing normal operating expenses incurred, including payroll," a California appellate court ruled that a business income provision provided coverage for both items without the insured having to offset one against the other.[38] The court reasoned that there was nothing in the policy language to suggest that where, as under the facts presented, the insured business was not operating at a profit, the insured should not expect coverage for its continuing expenses.[39]

III. COLLAPSE

Two interesting cases during the survey period focused on whether partial damage to an insured building fell within a property policy's coverage for "collapse." First, in *Middlesex Mutual Assurance Co. v. Puerta de la Esperanza*,[40] a federal court in Massachusetts held that the collapse of one brick pier in a building that did not render any area of the building inaccessible was a covered "collapse." In granting the insured's motion for summary judgment, the court rejected the insurer's argument that the use of the word "part" in the policy's definition of "collapse" required that an area of the building, and not just one structural piece of the building like the brick pier, suffer a "collapse" in order for coverage to be triggered.[41] Additionally, the Eastern District of Missouri considered whether the failure of brick veneer on the outside of an apartment building was a "collapse" or the result of excluded wear and tear or faulty design in *Council Tower Ass'n v. Axis Specialty Insurance Co*.[42] Rejecting the policyholder's argument that the failure of the wall was a "collapse" and granting summary judgment to the insurer, that court held that the failure of the veneer did not impair

37. Berk-Cohen Assocs., LLC v. Landmark Am. Ins. Co., No. 07-9205, 2010 WL 3522959, at *4–5 (E.D. La. Sept. 1, 2010).
38. Amerigraphics, Inc. v. Mercury Cas. Co., 107 Cal. Rptr. 3d 307, 318–20 (Ct. App. 2010).
39. *Id.* at 320.
40. No. 09-30156, 2010 WL 2639859 (D. Mass. 2010).
41. *Id.* at *3.
42. No. 08-1605, 2009 WL 3806994 (E.D. Mo. Nov. 12, 2009).

the structural integrity of the building and, therefore, was not within the policy's grant of coverage.[43]

IV. COVERED PROPERTY

In *Italian Designer Import Outlet, Inc. v. New York Central Mutual Fire Insurance Co.*,[44] a New York trial court held that covered "business personal property" was not limited to items owned by the insured, but also included merchandise held for sale by the insured under a consignment agreement. The insured was a men's clothing retailer, with some of its inventory supplied under a consignment agreement, and the rest was owned by the insured outright.[45] The policy provided: "We cover your business personal property in the described buildings."[46] While the policy further excluded personal property owned by others, it also specified that business personal property included the insured's "interest in personal property of others to the extent of your labor, material and services."[47] Reasoning that the definition of business personal property was ambiguous, the court construed the term in favor of coverage.[48]

Similarly, in *Snider v. American Family Mutual Insurance Co.*,[49] a Kansas appellate court held that, because a policy's definition of "contractors' equipment" was ambiguous, air-conditioner condensers used by a heating and cooling specialist were covered property. The policy defined "contractors' equipment" as "machinery, equipment, and tools of a mobile nature that 'you' use in 'your' contracting, installation, erection, repair, or moving operations or projects."[50] The insurer argued that the condensers were not covered since they were not of a "mobile nature." In rejecting the insurer's contention, the court held that the policy language was ambiguous. The court reasoned that it was unclear whether the phrase "of a mobile nature" modified only the term "tools," or also the terms "machinery" and "equipment." Given the ambiguity, the court concluded the compressors were covered as contractors' equipment.[51]

In *Porco v. Lexington Insurance Co.*,[52] a New York federal court held that a swimming pool was covered under the more limited Coverage B for "other

43. *Id.* at *6.
44. 891 N.Y.S.2d 260, 267–68 (Sup. Ct. 2009).
45. *Id.* at 262.
46. *Id.* at 263.
47. *Id.* at 264.
48. *Id.* at 267–68.
49. No. 101,202, 2009 WL 2902588 (Kan. Ct. App. Sept. 4, 2009).
50. *Id.* at *7.
51. *Id.* at *12.
52. 679 F. Supp. 2d 432, 441, 433 (S.D.N.Y. 2009).

structures" rather than under Coverage A for the "dwelling and other structures attached thereto." The court rejected the insured's contention that the pool was attached to the dwelling via a deck, five steps, and the filtration system.[53]

In *Gieringer v. Cincinnati Insurance Cos.*,[54] a Tennessee federal court held that since a provision in a policy renewal notice reducing coverage for personal property not situated in the residence was not sufficient to notify the insureds of the reduction in coverage, the broader coverage of the original policy applied. Moreover, the court held that the original policy, which contained an exception to the $1,000 cap for personal property not in the residence, was ambiguous. Accordingly, the court declined to exclude coverage as a matter of law for personal property moved to the new residence between March 2007 and January 2008, before being destroyed by fire later in January.[55]

V. EXCLUSIONS

A. *Causation*

In *Douzart v. Balboa Insurance Co.*,[56] the policyholders' claim for the loss of their home following Hurricane Katrina was denied by the insurer based on the insurance policy's exclusions for windstorm and flood. The policyholders filed suit in Mississippi federal court, and the insurer moved for summary judgment based on those exclusions. The policyholders contended that the loss of their home fell within an exception to the policy's exclusion for an "explosion that resulted from windstorm."[57] The policyholders submitted an expert report in support of their claim that an explosion caused the destruction of their home. The district court denied the insurer's motion, finding that there were genuine issues of material fact whether all or part of the damage to the home was caused by an explosion. Further, there were genuine issues of material fact as to whether the insurer had a legitimate basis to deny the claim. The Fifth Circuit Court of Appeals affirmed, and also agreed with the district court that the bad faith claim could proceed.

In *Friedberg v. Chubb & Son, Inc.*,[58] the policyholders sued their homeowner's insurer after the insurer denied their claim for water damage

53. *Id.* at 438. *See also* Axis Surplus Ins. Co. v. Lebanon Hardboard, LLC[0], No. 07–292, 2007 WL 3171247, at *2 (D. Or. Oct. 24, 2007) (structure, which insured was dismantling and had been removed from list of covered buildings, remained a building and was therefore not instead covered as business personal property).

54. No. 08-267, 2010 WL 1050201, at *6 (E.D. Tenn. Mar. 22, 2010).

55. *Id.* at *7.

56. 367 F. App'x 563 (5th Cir. 2010).

57. *Id.* at 565.

58. No. 08-6476, 2010 WL 1286082 (D. Minn. Mar. 30, 2010).

under the policy's exclusion for rot, mold, and construction defects. The policyholders discovered water intrusion through the Dryvit cladding on the exterior of the house. The insurer's expert determined the damage was caused by the failure to properly install control joints during the original construction and had been accumulating over a period of years. The policyholders' motion for summary judgment argued that the loss was the result of covered water intrusion or, in the alternative, was a covered ensuing loss. The trial court noted that Minnesota law provides that if there are multiple causes of a loss, the policyholder may recover so long as the overriding cause is not excluded. The trial court found that there was conflicting evidence as to whether the overriding cause was poor construction, water intrusion, or both; therefore summary judgment was denied.

In *Travelers Property Casualty Co. of America v. Marion T, LLC*,[59] a fire occurred at the factory the insured had bought seven months before. The insured claimed the fire damaged a power supply used to heat and cool the facility that had been shut down, disassembled, and drained before the fire. At the time of the fire, though, the equipment could have been used if it had been reassembled.

The parties could not agree on the amount of the loss and the claim went to appraisal. During the appraisal, the insurer filed an action for declaratory judgment. The final appraisers' report provided a figure for the actual cash value of the disputed loss that consisted of the insured's claims of damage to eighty-four pieces of mechanical equipment. The insurer disputed whether any damage that might have occurred to these items was covered by the policy. The insured did not allege that fire damaged the equipment, but argued that the inability to operate the equipment following the fire's destruction of the power source had caused the equipment to sustain damage from nonuse.[60]

The insurer sought summary judgment on the ground that it owed nothing further as no direct physical loss or damage occurred to the mechanical equipment. Further, it argued that any damage that may have occurred was the result of excluded rust or corrosion. The insured claimed that the insurer was estopped from asserting the rust and corrosion exclusion and that the delay in adjusting the insurance claim damaged the equipment from nonuse.[61]

The trial court granted summary judgment to the insurer, finding that there was no evidence of direct physical loss or damage to seventy-six of the eighty-four pieces of equipment. Further, the only evidence of damage

59. No. 07-1384, 2010 WL 1936165 (S.D. Ind. May 12, 2010).
60. *Id*. at *4.
61. *Id*.

to the remaining eight pieces was evidence of rust or corrosion, both of which were unambiguously excluded from coverage.[62]

B. *Earth Movement*

In two significant cases during the survey period, state appellate courts applied the exclusion for damage caused by earth movement to bar coverage for insured homeowners' claims in unique factual circumstances. In *Walker v. Beasley*,[63] the insureds' house was built—unknown to them—on land that had not been properly filled with soil, but was instead filled with "timber and other debris."[64] After cracks appeared in the house's foundation, the insurer denied the homeowners' claim, contending that the cracks were the result of excluded "settling" or earth movement. The trial court agreed with the insurer, rejecting the insureds' argument that the settling of their house was "so excessive and extraordinary that it is more accurate to refer to it as [covered] collapse" than settling.[65] A Tennessee appellate court affirmed, relying on the insurer's own expert who had opined that the damage resulted from settling of the foundation, and holding that "certainly the settling was excessive, but it was settling nonetheless."[66] In *Liebel v. Nationwide Insurance Co. of Florida*,[67] a Florida appellate court upheld a trial court's ruling that damage to a foundation resulting from soil erosion caused by a broken water line was excluded "earth movement," but very interestingly remanded the case for a determination of whether the cost to tear out the foundation to replace the broken pipe would be covered.

C. *Vacancy*

In *Saffold v. Allstate Indemnity Co.*,[68] the policyholder sued his insurer after it failed to pay an insurance claim stemming from a fire at his rental property. The insurer had denied the claim under the policy's vacancy exclusion after an investigation determined that the fire was intentionally set and that the rental tenant had ceased residing at the property over ten months before the fire occurred. The insurer brought a motion for summary judgment, finding that the insured was not entitled to coverage under the policy's vacancy exclusion because the property had been vacant for a period of ninety days or more before the loss. The court granted the motion for summary judgment, noting that the insured's tenant had moved

62. *Id.* at *5.
63. No. W2009-00118-COA-R3-CV, 2009 WL 4801480 (Tenn. Ct. App. Dec. 15, 2009).
64. *Id.* at *1.
65. *Id.* at *3.
66. *Id.*
67. 22 So. 3d 111, 117 (Fla. Dist. Ct. App. 2009).
68. No. 08-1023, 2009 WL 3326934 (M.D. Ala. Oct. 14, 2009).

out more than ten months prior to the fire. Further, the court found that while affidavits in the record claimed that neighbors personally viewed people coming and going from the property on a regular basis, there was nothing in the record to establish whether those persons actually resided at the property.[69] The court also noted that upon seeing the property two months after the fire, the insured himself stated that the property appeared to be vacant and devoid of furnishings.[70]

In *Hollis v. Travelers Indemnity Co. of Connecticut*,[71] a commercial property insurer denied a water damage claim under the vacancy exclusion in the policy. The insurer asserted that under the terms of the vacancy exclusion, the property was vacant for more than sixty consecutive days before the loss because the insured's commercial tenants were no longer using or renting thirty-one percent or more of the total square footage of the building for customary operations, as required by the policy.[72] The insured filed suit against the insurer for breach of contract and bad faith, asserting that the policy's vacancy exclusion should be interpreted as of the time the policy is issued, that the insurer's calculation of square footage was incorrect, and that the tenant's customary operations included subleasing space in the building to others.[73] The court granted the insurer's motion for summary judgment based on the vacancy exclusion, finding that the relevant time period for determining when the building was vacant was at the time of the loss, not when the policy was issued, and that the building's tenants were using less than thirty-one percent of the building for customary operations for more than sixty days before the water leak.[74] Moreover, the court found that the fact a former tenant left valueless materials and equipment in the building after vacating it did not amount to customary operations.[75]

In *West American Insurance Co. v. Hernandez*,[76] an insurer denied coverage for a claim related to an arson fire loss pursuant to the vacancy exclusion in the policy that excluded coverage for losses caused by vandalism or malicious mischief where the property is vacant for more than sixty consecutive days prior to the loss. The insurer also filed suit, seeking a declaratory judgment that (1) it was not obligated to pay because the loss was excluded under the vacancy exclusion because the property was vacant for more than sixty days and arson is a form of vandalism or malicious

69. *Id*. at *1.
70. *Id*.
71. No. 08-2350, 2010 WL 1050991 (W.D. Tenn. Mar. 19, 2010).
72. *Id*. at *2.
73. *Id*. at *3.
74. *Id*. at *9.
75. *Id*.
76. 669 F. Supp. 2d 1211 (D. Or. 2009).

mischief excluded under the exclusion; (2) it was not obligated to pay the loss because the insureds set or conspired to set the fire; and (3) it was not obligated to pay because the insured failed to inform it of a change in ownership.[77] Both parties brought cross motions for summary judgment on the three issues, including the applicability of the vacancy exclusion. The court granted the insured's motion and held that the property was not vacant as a matter of law, but found that issues of fact existed for the two remaining issues.[78] The court found that under Oregon law, the term "vacant" meant the property "contains substantially nothing."[79] Applying the Oregon definition, the court held the property was not "vacant" because an inventory submitted by the insured with the proof of loss to the insurer showed that the property, while not fully furnished, contained furniture, appliances, and personal items.[80]

D. *Dishonest Acts*

In *Elevators Mutual Insurance Co. v. J. Patrick O'Flaherty's, Inc.*,[81] the insurer sought to introduce evidence of the insured's conviction for arson and insurance fraud as proof of the insured's dishonest and criminal acts in a civil action regarding coverage for fire damage to the insured's restaurant. The court held that because the insured's conviction was the result of a plea of no contest, evidence of both the insured's plea of no contest and the resulting conviction were inadmissible pursuant to Ohio's criminal rules and rules of evidence.[82]

A federal court in Oklahoma in *American Commerce Insurance Co. v. Harris*[83] held that an insured's fraud or misrepresentation in a portion of his claim voided all coverage under the policy. The court noted that the public policy of Oklahoma's statute on fraudulent insurance claims would be frustrated if the insured were allowed to retain the insurance benefits he previously received after a vain attempt to defraud the insurer out of additional amounts.[84]

E. *Faulty Workmanship*

In *French Cuff, Ltd. v. Markel American Insurance Co.*,[85] the Eleventh Circuit found a latent defect exception to an exclusion for design defects ambigu-

77. *Id.* at 1213–14.
78. *Id.* at 1215.
79. *Id.* at 1217.
80. *Id.* at 1219.
81. 928 N.E.2d 685, 686 (Ohio 2010).
82. *Id.* at 687–88.
83. No. 07-423, 2009 WL 3233738, at *5 (E.D. Okla. Sept. 25, 2009).
84. *Id.*
85. 322 F. App'x 669 (11th Cir. 2009).

ous as applied to materials that were inappropriately used in the design of the insured vessel. The marine insurance policy excluded loss due to manufacturing or design defects, but included an exception to the exclusion for loss due to "any latent defect in the hull or machinery." The policy defined "latent defect" as a "flaw in the material." The insured claimed that its hull cracked because it was designed and manufactured with a foam core that was too thin or friable for use as a bulkhead core. It argued that the damage was caused by a covered "flaw in the material," rather than an excluded design defect. The court agreed, ruling that the phrase "flaw in the material" could reasonably apply to a flaw created as a result of inappropriate use of a material, as well as to material that is defective regardless of use.

In *Huntingdon Ridge Townhouse Homeowners Ass'n v. QBE Insurance Corp.*,[86] a Tennessee federal district court found that faulty workmanship and latent defect exclusions applied to an insured homeowners' association's claim for collapse coverage. While there was no dispute that the "collapse" was caused by defects in the construction, installation, and design of floor trusses, there was no coverage because the policy only covered collapse caused by use of defective materials or methods in construction if the collapse occurred during the course of construction. The policy also excluded coverage for any "latent defect . . . in the property that causes it to damage or destroy itself or for any faulty [or] defective . . . construction or" materials used in construction.[87]

In a case involving "street creep" damage to the insureds' driveway due to shrinkage and expansion of an adjoining municipal street, the Eighth Circuit affirmed a Nebraska federal court's holding that the faulty workmanship exclusion barred coverage without regard to the allegation that the faulty workmanship occurred off the insured premises.[88]

F. *Mold and Water Damage*

1. No Direct Physical Loss

In *Universal Image Productions, Inc. v. Chubb Corp.*,[89] heavy rainfall caused water to enter the policyholder's HVAC system. The policyholder argued that a covered peril, water seepage, "caused it to suffer a direct physical loss in the form of pervasive odor, mold and bacterial contamination."[90] The cleansing process also caused major disruption to the policyholder's busi-

86. No. 09-71, 2009 WL 4060458 (M.D. Tenn. Nov. 20, 2009).
87. *Id.* at *5.
88. Wurtele v. Cincinnati Ins. Co., 359 F. App'x 683, 684 (8th Cir. 2010), *aff'g* No. 07-340, 2009 WL 205057, at *4 (D. Neb. Jan. 27, 2009).
89. 703 F. Supp. 2d 705 (E.D. Mich. 2010).
90. *Id.* at 709.

ness. The insurance company, on the other hand, argued that there was no physical loss because the contaminant did not alter the structural integrity of the property.[91] The court agreed and granted summary judgment to the insurance company because the mold and odors did not cause structural or tangible damage to the insured property.[92] The court also found no evidence that the entire premises were uninhabitable. Although the court noted that the finding that there was no physical loss made it unnecessary to address other exclusions, the court also granted summary judgment to the insurance company with regard to concurrent causes of loss.[93]

2. Ensuing Loss

The issue of whether water damage or faulty construction was the overriding cause of damage arose in *Friedberg v. Chubb & Son, Inc.*[94] The policyholders filed a claim for damage when water intruded through the Dryvit on the exterior of their home and caused damage to the home's wood framing and insulation as well as rot and mold. The insurance company argued that the faulty workmanship, rot, and mold exclusions barred coverage.[95] The policyholders argued that the overriding cause of the loss was water damage, a covered peril, and, even if coverage was excluded, the ensuing loss provisions provided an exception to the exclusions. The court found that there was not enough information to decide the overriding cause of the loss and denied summary judgment.[96] The court also found that a determination of the cause of the loss was necessary before it could determine if the ensuing loss provisions applied.[97]

The importance of factual findings regarding causation is also highlighted by *TMW Enterprises, Inc., v. Federal Insurance Co.*,[98] in which the Sixth Circuit reversed in part the district court's grant of summary judgment in favor of the insurance company. The court remanded for further proceedings to allow the policyholder to seek coverage for any losses not proximately caused by faulty workmanship. The court held that, "[w]hile the faulty workmanship exclusion applies to loss or damage 'caused by or resulting from' the construction defect, the 'ensuing loss' provision clarifies that the insurance company could not use the exclusion to avoid coverage for losses remotely traceable to an excluded cause."[99]

91. *Id.*
92. *Id.* at 710.
93. *Id.* at 714.
94. No. 08-6476, 2010 WL 1286082 (D. Minn. Mar. 30, 2010).
95. *Id.* at *4.
96. *Id.*
97. *Id.*
98. 619 F.3d 574 (6th Cir. 2010).
99. *Id.* at 579.

3. Anti-Concurrent Causation

Mold exclusions frequently include "anti-concurrent causation" clauses that preclude coverage. For example, in *Builders Mutual Insurance Co. v. Glascarr Properties*,[100] the mold exclusion was prefaced by language stating that "[w]e will not pay for a 'loss' *caused directly or indirectly by* any of the following. Such 'loss' is excluded *regardless of any other cause or event that contributes concurrently or in sequence to the 'loss'*."[101] When vandals broke into the house and left water taps running, the insurance company paid for the water damage but not for mold remediation.[102] The insurance company argued, among other things, that the anti-concurrent causation clause excluded losses caused by mold. The policyholder argued that, because the policy covers claims arising from vandalism, it also covers losses caused by mold, since the mold was caused by the vandalism. The court found in favor of the insurance company based on the anti-concurrent causation clause. Other interesting cases on this issue during the survey period include *Colella v. State Farm Fire & Casualty Co*.[103] and *Pisano v. Nationwide Mutual Fire Insurance Co*.,[104] each of which applied an exclusion containing an anti-concurrent causation clause.

4. Insured's Knowledge of Prior Water Damage

In *Williams v. Pekin Insurance Co*.,[105] the policy contained an endorsement for "Limited Fungi, Wet or Dry Rot, or Bacteria Coverage," which precluded coverage for loss that was

> [c]aused by constant or repeated seepage or leakage of water or the presence of condensation of humidity, moisture or vapor, over a period of weeks, months or years *unless* such seepage or leakage of water or the presence or condensation of humidity, moisture or vapor and the resulting damage is unknown to all "insureds" and is hidden within the walls or ceilings or beneath the floors or above the ceilings of a structure.[106]

The court agreed with the trial court's holding that this policy language required the homeowner to show that "(1) water seepage or leakage or the presence of humidity, moisture or vapor is unknown to the homeowner; and (2) the resulting damage is unknown and the damage is

100. 688 S.E.2d 508 (N.C. Ct. App. 2010).
101. *Id*. at 510.
102. *Id*. at 512.
103. No. 09-2221, 2010 WL 1254318 (E.D. Pa. Mar. 30, 2010).
104. No. 08-2524, 2009 WL 3415278 (E.D. Pa. Oct. 21, 2009).
105. No. 09-0799, 2009 WL 4842468 (Iowa Ct. App. Dec. 17, 2009).
106. *Id*. at *1.

hidden within the walls, ceiling, or floors."[107] In other words, the court interpreted the "lack of knowledge" requirement to refer not only to the resulting damage but also to the water seepage itself. In this case, the policyholder did not dispute that she was aware of the flooding that occurred in her basement.[108] In fact, when she had made the earlier claim for the damage, the same insurance company had paid her the limit under the endorsement for "Water Back-up of Sewers or Drains."[109] The court held, however, that coverage for the resulting mold damage was properly denied because the policyholder knew about the source of the damage.[110]

VI. DAMAGES

A. *Hold Back*

In *Buckley Towers Condominium, Inc. v. QBE Insurance Corp.*,[111] the Eleventh Circuit refused to apply the doctrine of "prevention of performance" when it reversed the trial court's award of replacement cost value for damaged property. While it would have been costly, inconvenient, and most certainly a hardship for the insured condominium association to pay for millions of dollars in repairs without receipt of insurance proceeds, the Eleventh Circuit stated that the hardship would not excuse the contractual requirement to actually repair the property before replacement cost value damages could be awarded.[112]

B. *Overhead and Profit*

In companion class action suits filed in Arkansas, national class plaintiffs alleged that insurance companies had conspired to deprive insureds of payments reflecting contractors' overhead and profit.[113] Because the named class plaintiffs had been removed from the cases, the insurers moved to dismiss, arguing that the remaining class members had no standing. The Arkansas Supreme Court rejected the insurers' argument, finding that standing was not a prerequisite for subject matter jurisdiction under Ar-

107. *Id.* at *2.
108. *Id.* at *3.
109. *Id.* at *1.
110. *Id.* at *3.
111. No. 09-13247, 2010 WL 3551609 (11th Cir. Sept. 14, 2010).
112. *See also* Vakas v. Hartford Cas. Ins. Co., 361 F. App'x 1, 4 (10th Cir. 2010) (finding that full-replacement cost recovery was not allowed because the insured's business personal property was never replaced).
113. Chubb Lloyds Ins. Co. v. Circuit Court, No. 09-553, 2010 WL 841254 (Ark. Mar. 11, 2010); Foremost Ins. Co. v. Circuit Court, No. 09-587, 2010 WL 841248 (Ark. Mar. 11, 2010).

kansas law or its state constitution. Therefore, the cases were not dismissed for lack of subject matter jurisdiction.[114]

C. *Matching*

In *Collins v. Allstate Insurance Co.*,[115] a federal district court rejected the insurer's argument that it had no obligation, as a matter of law, to replace undamaged parts of the insured's roof so as to achieve a uniform appearance when repairing covered damage. In denying the insurer's motion for summary judgment, the court held that replacement of the entire roof, including undamaged areas, might be required under a homeowners policy covering property with replacement of property "of like kind and quality" or repair costs of "equivalent construction for similar use." Genuine issues of material fact existed as to whether there were slate tiles currently available that were sufficiently similar in color, size, and texture to those on the insured's home at the time of the loss so as to make them of "like kind and quality" or "equivalent construction" within the meaning of the policy.

In *Strasser v. Nationwide Mutual Insurance Co.*,[116] matching was not required under a business owners policy because the insurer elected to pay only the value of the damaged property under the loss payment options in the policy. Thus, the insured was not allowed to present evidence at trial concerning the cost of matching the undamaged granite tiles on the façade of its building. The court rejected the insured's argument that a Florida statute governing matching under homeowners policies mandated a reasonableness standard for resolving matching disputes. The court found that the statute had no application to commercial policies in light of legislative history showing that the Florida legislature considered but rejected making the statute applicable to commercial property.

VII. OBLIGATIONS AND RIGHTS OF THE PARTIES

Like other contracts, property insurance policies include both the substance that is the core of the parties' agreement—the risk transferred to the insurer and the exclusions from that coverage—and a set of other rights and obligations. Those other obligations, while not directly related to the

114. *Id.* Similar class action suits have been brought alleging a failure to include contractor's overhead and profit. *See, e.g.*, Dupree v. Lafayette Ins. Co., 41 So. 3d 483, 488 (La. Ct. App. 2009) (certifying class status), *rev'd*, No. 2009-C-2602, 2010 WL 4844021 (La. Nov. 30, 2010); Amended Complaint at 3, Ayotte v. USF&G Ins. Co., No. 10-81243 (S.D. Fla. filed Nov. 4, 2010) (class action alleging that the defendant insurers "failed to include in [their] upfront or pre-repair payment . . . general contractor overhead and profit"), *available at* https://ecf.flsd.uscourts.gov/doc1/05118612334.

115. No. 09-01824, 2009 WL 4729901 (E.D. Pa. Dec. 10, 2009).

116. No. 09-60314, 2010 WL 667945 (S.D. Fla. Feb. 22, 2010).

coverage itself, provide a framework of rules for the parties' working relationship around the substance of the transferred risk itself, all the way from the policyholder's duty not to make false statements on the insurance application to how the parties can resolve their disputes if they disagree on coverage for a claim. Some of these issues, like the penalties for the insurer's bad faith breach of the contract, are supplied by state law outside of the contract itself, but still derive from that framework of rules. This section reviews significant developments in the parts of this framework that most affect practitioners of property insurance law.

A. *Misrepresentation*

In an unpublished opinion in *Howard v. Farm Bureau Insurance*,[117] the Michigan Court of Appeals considered the policyholder's claims that someone else filled out his insurance application and that he had signed the application without reading the false statements in the application. The court held that, by signing the application, the insured had a duty to examine the application and know what he had signed. The court also found that by cashing the insurer's premium refund check stating that the premium was being refunded because the policy had been rescinded, the insured had unconditionally accepted the rescission.[118]

In *Grenoble House Hotel v. Hanover Insurance Co.*,[119] the insurer sought to deny coverage based upon the policyholder's statement in its application that it owned the property that was being insured, when in actuality the insured was only a tenant. Because the insured had not signed the application and no evidence had been presented that the insured had provided the information on the application, the court denied the insurer's motion for summary judgment.[120]

B. *Duties*

1. Examinations Under Oath

The Massachusetts federal court in *Miles v. Great Northern Insurance Co.*[121] held that the policyholders' refusal to fully respond to document requests and questions asked during their examinations under oath (EUO) constituted a material breach of the insurance contract that discharged the insurer's obligations. One of the policyholders, an attorney, refused to answer questions during his EUO, ordered his wife not to answer certain

117. No. 289407, 2009 WL 4985469, at *1 (Mich. Ct. App. Dec. 22, 2009).
118. *Id.* at *3.
119. No. 06-8840, 2010 WL 2985789 (E.D. La. July 26, 2010).
120. *Id.* at *2.
121. 671 F. Supp. 2d 231, 239 (D. Mass. 2009).

questions during her EUO, and withheld other information from their insurer based upon an erroneous claim of attorney/client privilege.[122] The court found that since no privilege existed, the policyholders' failure to provide the requested information was willful and unexcused.[123] The court noted that, due to the policyholders' willful failure to cooperate, they had no right to cure their breach of the duty of cooperation.[124]

In *Sweeney v. Citizens Property Insurance Corp.*,[125] the court held that under the terms of the policy, an EUO is a condition precedent to a suit and the insured's failure to comply with the EUO, even if not willful, precludes an action on the policy. On the other hand, a federal court in Florida questioned whether a policy's EUO provision requires the insured to subject itself to more than one EUO.[126]

2. Proof of Loss

In *Swaebe v. Federal Insurance Co.*,[127] the insured failed to comply with the insurance policy's "no action" provision by filing suit prior to submitting a sworn proof of loss. The court found that the submission of a sworn proof of loss was a condition precedent to coverage and that the insured's telephone statements, EUO, production of documents, and post-suit proof of loss did not cure her failure to comply with the "no action" provision.[128] Since compliance with the "no action" provision was a condition precedent to recovery, the court granted summary judgment in favor of the insurer.[129]

The Oregon Supreme Court in *Parks v. Farmers Insurance Co. of Oregon*[130] considered the meaning of the term "proof of loss" as used in Oregon's statute providing for recovery of attorney fees in actions on insurance policies. The court held that based upon its prior decisions "[a]ny event or submission that would permit an insurer to estimate its obligations (taking into account the insurer's obligation to investigate and clarify uncertain claims) qualifies as 'proof of loss' for purposes of [Oregon's attorney's fee statute]."[131] The court held that a proof of loss does not have to be in writ-

122. *Id.*
123. *Id.* at 240.
124. *Id.* at 240–41.
125. 43 So. 3d 842, 843 (Fla. Dist. Ct. App. 2010).
126. El Dorado Towers Condo. Ass'n, Inc. v. QBE Ins. Corp., 717 F. Supp. 2d 1311, 1319 (S.D. Fla. 2010).
127. 374 F. App'x 855, 857 (11th Cir. 2010).
128. *Id.* at 857–58.
129. *Id.*
130. 227 P.3d 1127, 1129 (Or. 2009).
131. *Id.* at 1130 (quoting Dockins v. State Farm Ins. Co., 985 P.2d 796, 801 (Or. 1999)).

ing and that the insured's telephone calls to the insurer's agent, during which the insured discussed the amounts he had paid and expected to pay for cleanup costs, qualified as a proof of loss.[132]

C. *Appraisal*

1. Scope of Appraisal

During the survey period, several courts considered the line between "valuation" (the task of an appraisal panel) and coverage determinations (the province of the courts). In *QBE Insurance Corp. v. Twin Homes of French Ridge Homeowners Ass'n*,[133] an insurer argued that an appraisal panel's decision constituted an impermissible coverage determination rather than a loss appraisal to the extent that it "improperly determined whether coverage existed under the [p]olicy for different types of damage."[134] The panel had concluded that hail-damaged roofs in a townhome complex could not be repaired or replaced because the shingles used were no longer marketed. The panel therefore determined the value of the loss in terms of "total roof replacement" pursuant to one of the loss formulas provided for by the policy.[135] The court concluded that the panel did not exceed its authority as the panel had merely arrived at a dollar figure representing the value of the loss and there had been no "clear showing" that the appraisers exceeded their authority.[136] In *North Carolina Farm Bureau Mutual Insurance Co. v. Sadler*,[137] an insurer contended that the insured violated the terms of his insurance policy by submitting to an appraisal that went beyond providing a valuation of the loss and included the date and cause of the damage to his home. The court rejected this position, noting that "the appraisers were clearly informed as to the cause of damage—wind—and assessed [the insured's] property for loss of value considering the type of damage that may have resulted from such a cause."[138] The court also observed that the appraisers had not engaged in any interpretation of the subject policy, thus distinguishing a Fourth Circuit case upon which the insurer relied. In a case involving the appraisal of a Hurricane Katrina loss, a federal court sitting in Louisiana concluded that appraisers must consider causation to determine the scope of a loss; however, such causation determinations are not binding and are subject to challenge.[139]

132. *Id.* at 1131–32.
133. 778 N.W.2d 393 (Minn. Ct. App. 2010).
134. *Id.* at 398 & n.1.
135. *Id.* at 398.
136. *Id.* at 399.
137. 693 S.E.2d 266, 269 (N.C. Ct. App. 2010).
138. *Id.*
139. St. Charles Parish Hosp. Serv. Dist. No. 1 v. United Fire & Cas. Co., 681 F. Supp. 2d 748, 757 (E.D. La. 2010).

2. Timeliness of Demand or Refusal to Appraise

Several recent cases applying Texas law address the question of when an insurer will be deemed to have waived its appraisal rights as a result of a delay in demanding appraisal. While the analyses in these cases were ultimately fact-specific, there was agreement that the point of reference for determining whether a demand for appraisal is timely is the date of disagreement, or "impasse" with the insured.[140] The court in *In re Slavonic Mutual Fire Insurance Ass'n* held that an insurer did not waive its appraisal rights where it demanded appraisal six days after receiving a demand letter from its insured.[141] However, in a federal case predating *In re Slavonic*, a Texas federal court held that an insurer's demand for appraisal was untimely where the insurer waited almost one year to invoke an appraisal provision from the time it received a call from the insured disputing the insurer's adjustment of a Hurricane Ike claim, during which time an unsuccessful mediation took place.[142] A subsequent Texas federal court declined to find waiver based on a three-month delay between a triggering "impasse" and the appraisal demand.[143]

In *Security Storage Properties v. Safeco Insurance Co. of America*,[144] a Kansas federal court held that an insured could not be compelled to submit its claim to appraisal where two, state-specific endorsements—one containing a "mandatory" appraisal clause (Texas) and the other a voluntary appraisal clause (Kansas)—created an ambiguity. The court concluded that "[b]ecause the policy fails to make clear that Texas rather than the Kansas endorsement was intended to apply . . . the court concludes that the Kansas endorsement must be applied to the plaintiffs' claim."[145]

3. Enforcing and Modifying Appraisal Awards

In *Florida Insurance Guaranty Ass'n v. Olympus Ass'n*,[146] a Florida appellate court held that the trial court erred in confirming an appraisal award and entering final judgment in favor of an insured without first determining the Florida Insurance Guaranty Association's ("FIGA") liability as to contested coverage claims, including claims for damage to paint or waterproofing

140. *In re* Slavonic Mut. Fire Ins. Ass'n, 308 S.W.3d 556, 562 (Tex. Ct. App. 2010); Sanchez v. Prop. & Cas. Ins. Co. of Hartford, No. 09-1736, 2010 WL 413687, at *13–14 (S.D. Tex. Jan. 27, 2010).

141. *In re Slavonic*, 308 S.W.3d at 562–63.

142. *Sanchez*, 2010 WL 413687, at *5.

143. Tran v. Am. Econ. Ins. Co., No. 10-0016, 2010 WL 2680616, at *2–3 (S.D. Tex. July 2, 2010).

144. No. 09-1036, 2010 WL 1936127 (D. Kan. May 12, 2010).

145. *Id.* at *6.

146. 34 So. 3d 791 (Fla. Dist. Ct. App. 2010).

material. The court rejected an all-or-nothing approach with respect to an insurer's ability to contest coverage, explaining that FIGA could contest part of the liability without challenging coverage as a whole: "[I]t is not reasonable to order an insurer to pay for all elements set forth by an appraiser if the insurer raises an issue of coverage as to only one element and not the whole claim."[147]

4. Appraiser Qualifications

In a case arising out of Hurricane Katrina, an insurer challenged the validity of an appraisal award in favor of an insured hospital on several grounds, including that the insured's appraiser and the umpire were not impartial.[148] Noting that the insurer bore the burden of producing evidence "that the appraiser's honesty or integrity is suspect," the court concluded that there was no lack of impartiality even though the insurer's appraiser was not present for the final deliberations with respect to the award.[149] The court observed that by that point in the process, it was clear that the insurer's appraiser would not agree to the numbers that the insured's appraiser and the umpire were leaning toward and that he had nothing else to submit for rebuttal.[150]

5. Miscellaneous Issues

In two cases decided on the same day, separate panels of Florida's Fourth District Court of Appeal ruled that the Florida Insurance Guaranty Association ("FIGA") could not compel appraisal where the insureds were not informed of their right to participate in a mediation program pursuant to Florida Statutes § 627.7015(2) (2005).[151] In *FIGA I*, the court held that FIGA was bound by the failure of the insolvent insurer whose obligations FIGA had assumed to notify the insured regarding the mediation program.[152] In *FIGA II*, the court held that the application of § 627.7015(2) was not unconstitutional as applied to FIGA even though the statutory amendment that extended the reach of the statute to cover the policy at issue was not enacted until after the subject policy went into effect.[153]

147. *Id*. at 796.
148. St. Charles Parish Hosp. Serv. Dist. No. 1 v. United Fire & Cas. Co., 681 F. Supp. 2d 748 (E.D. La. 2010).
149. *Id*. at 754.
150. *Id*. at 755.
151. Fla. Ins. Guar. Ass'n v. Shadow Wood Condo. Ass'n, 26 So. 3d 610 (Fla. Dist. Ct. App. 2009) ("*FIGA I*"); Fla. Ins. Guar. Ass'n v. Devon Neighborhood Ass'n, 33 So. 3d 48 (Fla. Dist. Ct. App. 2009) ("*FIGA II*").
152. *FIGA I*, 26 So. 3d at 613–14.
153. *FIGA II*, 33 So. 3d at 53–54.

D. *Who Can Sue on the Policy and Collect Proceeds?*

In *Motorists Mutual Insurance Co. v. Teel's Restaurant, Inc.*[154] an Indiana federal district court held that a contract seller of a restaurant who was not a named insured on the restaurant's policy should be treated like a mortgagee for the purposes of recovering insurance proceeds. The court rejected the seller's argument that he should be considered a named insured under the policy because he was the sole officer of the restaurant.[155] The court reasoned that it would "not [be] legally possible" to allow the seller to benefit from the tax and liability protections of the corporate form, while simultaneously treating him as identical to the corporation for the purpose of recovering insurance proceeds. Accordingly, the court ruled that the restaurant owner was entitled to insurance proceeds only in the amount remaining on the purchase agreement at the time the restaurant burned.[156]

Conversely, in *Komondy v. Middlesex Mutual Assurance Co.*,[157] a Connecticut trial court held that the named insured's husband, who was not himself a named insured on a fire policy for a residence, nonetheless had standing as a third-party beneficiary to bring a breach of contract action against the insurer. The court reasoned that the policy's repeated use of the terms "you" and "your," which the policy defined as the " 'named insured' shown in the Declarations and the spouse if a resident of the same household," indicated that the parties intended the husband to be a third-party beneficiary of the policy.[158] The husband, however, did not have standing to sue the insurer for breach of the implied covenant of good faith and fair dealing, since he was not in privity of contract with the insurer.[159]

In *Parmelee v. Standard Fire Insurance Co.*,[160] a Missouri federal court ruled that a named insured who subsequently relinquished title of a home to her ex-husband was not entitled to payment for the property's actual cash value when the home was damaged in a fire. The loss-payment clause in the homeowners policy stipulated that the insured be paid "UNLESS SOME OTHER PERSON NAMED IN THE POLICY IS LEGALLY ENTITLED TO RECEIVE PAYMENT."[161] The policy also required the notice of loss to declare any changes in title or occupancy.[162] Reasoning that the terms of the policy allowed the insurer to take notice of changes in

154. No. 08-237, 2009 WL 4255550, at *3 (N.D. Ind. Nov. 20, 2009).
155. *Id.*
156. *Id.*
157. No. CV096000516, 2009 WL 3740745, at *5 (Conn. Super. Ct. Oct. 20, 2009).
158. *Id.* at *3.
159. *Id.* at *6.
160. 697 F. Supp. 2d 1069, 1079 (E.D. Mo. 2010).
161. *Id.* at 1076.
162. *Id.* at 1079.

title and ownership and reduce payments to insureds accordingly, the court held that the ex-wife was not entitled to payment for the home's actual cash value since she had relinquished all interest in the home to her co-named insured ex-husband upon divorce.[163]

In *Archer v. Cotton States Mutual Insurance Co.*,[164] a Georgia appellate court ruled that an executor of an estate forfeited his insurable interest in a property when he transferred the title of the decedent's home from the estate to himself. The home, which was destroyed in a fire, contained a death benefit clause that extended insurance benefits to the legal representative of the deceased. The executor, therefore, extinguished his right to insurance proceeds when he assumed title to the property outside his capacity as executor of the estate.[165]

In *Balboa Life & Casualty, LLC v. Home Builders Finance, Inc.*,[166] a Georgia appellate court addressed the extent of a mortgagee's right to insurance proceeds to satisfy the mortgage debt where the mortgagee foreclosed on the insured property after the loss. Employing an economic analysis test, the court held that a mortgagee was entitled to insurance proceeds equal to the difference between the mortgage debt at the time of the foreclosure and the value of the residence acquired at foreclosure, subject to policy limits.[167] Likewise, in *Peery v. Allstate Insurance Co.*, a Mississippi federal district court ruled that, where a bank's post-loss foreclosure fully satisfies the insured's mortgage debt, the bank's right to insurance proceeds under a mortgage clause are extinguished.[168] The court in *Peery* did, however, reject the insured's bad faith claim against the insurer for issuing a joint check to the bank and the insured. The court reasoned that neither the insured nor the bank had notified the insurer of the change in the property's ownership before the disbursement of the insurance proceeds.[169]

E. *Suit Limitations*

In *Pitts v. Louisiana Citizens Property Insurance Corp.*,[170] a Louisiana appellate court addressed whether an insured's participation in a class action tolls the running of a suit limitation. The insured in *Pitts* had sustained property damage during Hurricane Katrina.[171] Her insurance policy contained a one-year suit limitation, which was extended for an extra year by an act of

163. *Id.*
164. 695 S.E.2d 329, 330 (Ga. Ct. App. 2010).
165. *Id.*
166. 697 S.E.2d 240 (Ga. Ct. App. 2010).
167. *Id.* at 243.
168. No. 09-115, 2010 WL 1380377, at *3 (N.D. Miss. Mar. 31, 2010).
169. *Id.*
170. 4 So. 3d 107 (La. Ct. App. 2009).
171. *Id.* at 109.

the Louisiana Legislature. The insured participated in two class certifications against her insurer, which were filed within a year of the hurricane.[172] When the insured subsequently brought her own action against the insurer, after one class certification was denied and the other restricted, the trial court denied the claim, arguing the two-year prescription period had run.[173] The appeals court, reasoning that the class certification petitions in which the insured had participated tolled the suit limitation, held that the insured's filing of her own action was not proscribed.[174] Conversely, in *Dixey v. Allstate Insurance Co*.,[175] a Louisiana federal district court held that the Louisiana statute tolling liberative prescription periods for members of a class action could not also suspend contractual limitations periods. *Dixey*'s fact pattern was nearly identical to the fact pattern in *Pitts*. In reaching its holding, the court in *Pitts* declined to risk infringing on the Contracts Clauses of the Constitutions of the United States and Louisiana by allowing a state statute to alter the contractual obligations of private parties.[176]

In *Sheppard v. Travelers Lloyds of Texas Insurance Co*.,[177] a Texas appellate court held that an insured did not meet the suit limitation deadline of two years and one day following the accrual of a cause of action, when the insured waited more than five years from the insurer's closing of its claim file to sue. The court held that the date on which the insurer closed its claim file was the date the cause of action accrued since it established "an objectively verifiable event that unambiguously demonstrated [the insurer's] intent not to pay the claim."[178] The court rejected the insured's contention that subsequent reinvestigation of the claim, in which the insurer neither withdrew nor changed its denial nor made further payment, pushed back the accrual of the cause of action.[179]

F. *Bad Faith*

In *State Farm Florida Insurance Co. v. Seville Place Condominium Ass'n*,[180] an insured brought suit for breach of contract against its insurer arising from a claim for roof damage related to Hurricane Wilma. The insurer did not dispute coverage and paid part of the claim, but the parties disagreed on the total value of the claim and agreed to an appraisal under the policy to

172. *Id*.
173. *Id*.
174. *Id*. at 111.
175. 681 F. Supp. 2d 740, 747 (E.D. La. 2010).
176. *Id*.
177. No. 14-08-00248, 2009 WL 3294997, at *7 (Tex. App. Oct. 15, 2009).
178. *Id*. at *4 (citing Kuzinar v. State Farm Lloyds, 52 S.W.3d 759, 760 (Tex. App. 2001)).
179. *Id*. at *7.
180. No. 3D08-2538, 2009 WL 3271300 (Fla. Dist. Ct. App. Oct. 14, 2009).

determine the value of the remaining roof damage.[181] Following the filing of the final appraisal award, the trial court confirmed the award and granted an insured's motions to amend the complaint to add a claim for statutory bad faith and a demand for punitive damages.[182] The insurer appealed the ruling, arguing that before a bad faith claim may proceed the insured must obtain a final judgment on its original breach of contract claim, that it still had pending affirmative defenses, and that it must be allowed to exhaust all appellate remedies regarding that judgment.[183] A Florida appellate court denied the insurer's appeal, holding that, under Florida law, an appraisal award determining liability and extent of loss is a sufficient basis for the commencement of a bad faith claim.[184] The court also noted that the insurer had no affirmative defenses pending and that Florida law did not require all appellate remedies be exhausted before the insured's bad faith claim was ripe.[185]

In *One River Place Condominium Ass'n v. Axis Surplus Insurance Co.*,[186] the insured brought suit against its insurer for breach of contract and bad faith related to property damage related to Hurricane Katrina. After obtaining a verdict at trial, the insured moved for judgment as a matter of law or, alternatively, for a new trial.[187] The insured claimed that it was entitled to post-trial relief because no reasonable juror could have found that (1) the insurer did not violate an emergency order issued by the State of Louisiana in the wake of Hurricane Katrina; (2) the insured did not suffer more property and business interruption damages than awarded by the jury; and (3) the insurer was responsible for bad faith penalties for its improper conduct.[188] The court denied both motions, and on the bad faith claim held that the jury had sufficient evidence to disagree with the insured's position that the insurer arbitrarily and capriciously failed to pay the claim.[189] The court specifically referenced evidence the insurer submitted from the adjustment in finding that there was sufficient evidence to find against a bad faith claim, including that the insurer did not delay in paying exterior damages while inspecting the property, paid additional glass damage once it was able to confirm a prior miscount, paid withheld depreciation early, and presented evidence that the insured withheld documents required to process the claim.[190]

181. *Id.* at *2.
182. *Id.* at *3.
183. *Id.*
184. *Id.* at *4.
185. *Id.*
186. No. 07-1305, 2009 WL 2409142 (E.D. La. Aug. 4, 2009).
187. *Id.* at *1.
188. *Id.*
189. *Id.* at *2.
190. *Id.* at *2–3.

In *Quast v. State Farm Fire & Casualty Co*.[191] the insureds brought suit for breach of contract and bad faith against their insurer after the insurer denied a claim for the alleged theft of personal property due to fraud by the insureds. The insurer brought a motion for summary judgment on the bad faith count, arguing that it had a reasonable basis to believe the claim was fraudulent and deny the claim.[192] The court agreed and granted the motion, finding that after reviewing the insured's conduct, the insurer reasonably believed the claim was fraudulent.[193] The court noted that the insurer had investigated the claim according to its customary practices, and when the investigation raised concerns about fraud, the insurer had the claim analyzed by the insurer's special investigations unit and hired an outside attorney to investigate the claim and offer opinions about the claim's validity.[194] Further, the court found that there were a number of facts that led to the insurer's reasonable belief the theft was fraudulent, including (1) the theft occurred just three days before the policy lapsed and was not going to be renewed; (2) the insureds lacked supporting documentation for the stolen property; (3) old nonworking items were stolen while newer items were left behind; (4) the insureds had made seven other property theft claims since 1991; and (5) financial records showed the insureds were living beyond their means for some time.[195]

In *Philadelphia Indemnity Insurance Co. v. C.R.E.S. Management, LLC*,[196] the insured brought a bad faith claim against its insurer under the prompt payment provisions of chapter 542 of the Texas Insurance Code,[197] alleging the insurer failed to pay the undisputed portion of carpet loss and business income claims arising from Hurricane Ike within the seventy-five days permitted to pay for losses related to a weather-related catastrophe. The insured brought a summary judgment on the issue of the prompt payment provisions, to which the insurer responded that an award of statutory interest and attorney fees was inappropriate because it acted in good faith and diligently adjusted the large, complex loss that totaled nearly $8 million in damages to five separate multifamily developments, each containing several hundred units.[198] The court granted the insured's motion for summary judgment, holding that evidence of the insurer's good faith in adjusting the losses was not a defense to the prompt payment provisions of the Texas Insurance Code.[199]

191. No. 09-675, 2010 WL 4339132 (W.D. Wis. Oct. 26, 2010).
192. *Id*. at *1.
193. *Id*. at *6.
194. *Id*.
195. *Id*. at *5.
196. No. 09-1032, 2009 WL 5061805 (S.D. Tex. Dec. 15, 2009).
197. Tex. Ins. Code Ann. §§ 542.058(a), 542.059(b) (West 2009).
198. *C.R.E.S. Mgmt*., 2009 WL 5061805, at *3.
199. *Id*. at *4.