

It's Alive! Resurrecting Coverage For Property Damage Through An Ensuing Loss Provision

By Bryan W. Petrilla

A water pipe, rusted and corroded by years of use, bursts. Water spills from the pipe and into the room below causing extensive damage. The owner's insurance policy clearly excludes losses caused by rust and corrosion. Yet the owner recovers for the full amount of damages to the room. How does this happen?

Policyholders denied coverage for property damage in similar situations may want to take a closer look at the chain of causation that led to their loss. Its links may very well lead to a "re-grant" or "resurrection" of coverage, even where the initial cause of the loss is clearly excluded under the terms of the policy. The key that makes this possible is an ensuing loss provision.

Commonly included in first party property policies, ensuing loss provisions vary slightly in form, but are similar in application. The provision is typically found at the end of a list of exclusions and states that while the insurance company will not pay for damages that result from an excluded cause of loss, it will pay for an ensuing loss that is otherwise covered under the policy. Sometimes the provision refers to a "resulting" loss, which is functionally identical.

The word "ensuing" has been defined as "to follow as a consequence or in chronological succession; to result, as an ensuing conclusion or effect." In other words, an ensuing loss is one that follows "as a consequence of some preceding event or circumstance." The Washington Court of Appeals described an ensuing loss provision as "an exception to an exclusion, [that] preserves coverage where a covered loss is caused by an excluded peril." The Minnesota Court of Appeals similarly defined the provision as one that "brings within coverage a loss from a covered peril that follows as a consequence of an excluded peril."

Those definitions, however, do little to shed light on how the provision actually works. One court even stated that at

"It's Alive!" continued page 2

Virginia Changes Notary Requirements

By Thomas R. Petty and
Jenessa J. Hoffman

Effective July 1, 2007, important changes went into effect throughout the Commonwealth of Virginia respecting notary public requirements for every document to be recorded in Virginia; this includes deeds, easements, deeds of trust and other loan documents.

The most important change is that all certificates of acknowledgment (otherwise known as notary blocks or notary signatures) *must appear on the same page as the signature which is being notarized.* House Bill 2058 ("HB 258"), which has been signed by the Governor of Virginia, explicitly prohibits a notary public from notarizing a signature on a document "without notarial certificate wording on the same page as the signature."

In addition, HB 258 requires that notaries include their notary registration number in their notary block. The notary seal must constitute a

"Notary Requirements" continued page 2

"Notary Requirements" continued from p1

"photographically reproducible image" of the seal. Failure to affix an official seal will not impact the legality of the document to be recorded, but after July 1, 2007, the Clerk's Offices may refuse to record any document that does not include a photographically reproducible seal. Generally, the notary seal is embossed—pressed onto the paper by a two-sided seal—and is typically very difficult to see on a photocopy. One way to provide for the image to be visible when photocopied is to use carbon paper to darken the embossed notary seal so that it will show up clearly when photocopied.

There are a number of ways to ensure that multiple signatures appear on the same page as the applicable notary block, including reducing the signature page to 10-point font, adjusting the margins for greater page usage, or repeating the signature lines on multiple pages with the respective notary block on the same page as its applicable signature. ▲



Thomas R. Petty is a partner in Anderson Kill's Washington, DC office. Mr. Petty's practice concentrates in the area of commercial real estate, with an emphasis on real estate financings and acquisitions.

(202) 218-0041

tpetty@andersonkill.com



Jenessa Jacobson Hoffman is an attorney in Anderson Kill's Washington, D.C. office. Ms. Hoffman has extensive experience in a variety of corporate and bankruptcy areas including advising lenders and borrowers

in commercial financing transactions.

(202) 218-0048

jhoffman@andersonkill.com

"It's Alive!" continued from p1

first glance the ensuing loss provision "appears to be self-contradictory gibberish." While it certainly can be difficult to conceptualize, the effort may result in coverage for attentive policyholders.

The Ensuing Loss Provision in Action

A simple example of an ensuing loss provision in action may be the best way to understand how the provision can work to any policyholder's benefit. The leaking pipe remains an appropriate illustration. As a direct result of rust and corrosion, the pipe deteriorates, weakens, and finally bursts. Water flows into the room below causing extensive damage. When the owner seeks insurance coverage for her loss, she is informed that her policy excludes any loss caused by rust and corrosion and is consequently denied coverage.

The policy, however, contains an ensuing loss provision that requires the insurance company to pay for any ensuing or resulting loss that is otherwise covered under the terms of the policy. A further review of the policy reveals that loss due to water intrusion is covered. Therefore, an excluded cause of loss, rust and corrosion, resulted in an otherwise covered cause of loss, water intrusion. Applying the ensuing loss provision, the insurance company does not have to pay for the cost to repair or replace the pipe, as that damage resulted directly from rust and corrosion, but must pay for damages caused by the ensuing water intrusion.

While the illustration appears simple enough, there are at two critical components to any ensuing loss provision analysis that must be satisfied before a policyholder can recover. The first component is the degree to which the ensuing cause of loss must be separable from the initial excluded cause of loss. The second is confirming that the ensuing loss is itself otherwise covered under the terms of the policy. Not surprisingly, courts across the country have interpreted and applied these components in different ways.

How Many Degrees of Separation?

Courts agree that the cause of the ensuing loss must somehow be separable from the initial excluded

To subscribe to this or any of the Anderson Kill & Olick Newsletters and Alerts, visit:

www.andersonkill.com/publication_subscribe.asp

To unsubscribe, please email: unsubscribe@andersonkill.com

cause of loss. The requisite degree of separation, however, varies by jurisdiction, leading to diverse results, sometimes under nearly identical ensuing loss provisions.

The Minnesota Court of Appeals tackled a heavily litigated topic when it considered whether a home damaged by mold and rot caused by water intrusion constituted an ensuing loss. In its analysis, the court held that an ensuing loss is covered even if an excluded peril is a “but for” cause of the ensuing loss. Using the previous example, “but for” the corrosion of the pipe, there never would have been ensuing water damage to the floor below. In that case, however, the court held that because there was no intervening cause other than time, the water intrusion and resulting mold and rot were a “single phenomenon” and therefore, the mold and rot damage did not constitute an ensuing loss. However, the United States District Court for the Western District of Kentucky recently took the opposite approach under similar circumstances, holding that an ensuing loss provision provided coverage for mold and rot damage caused by water intrusion because any other interpretation would be inconsistent with the policyholder’s reasonable expectations.

The Minnesota Court of Appeals has also held that, absent specific policy language to the contrary, an ensuing loss can be directly related to the original excluded loss. In that case, a property owner sought coverage for contamination after asbestos fibers were found on carpeting and other surfaces inside the insured building. Loss due to contamination was a covered risk under the applicable policy. The insurance company, however, argued that the contamination was caused by ordinary wear and tear that caused the asbestos fibers to be released and circulated throughout the building. Ordinary wear and tear was an excluded cause of loss under the policy. Therefore, the insurance company maintained, the resulting contamination was also excluded.

The court rejected the insurance company’s argument, reasoning that damage to the building arising from ordinary wear and tear, such as holes in the ceilings and walls, was separable from the resulting asbestos contamination, and the two were not merely classifications of a “single phenomenon.” The court concluded that when read together, the wear and tear and ensuing loss

provisions excluded the normal damage caused by wear and tear, but provided coverage for “distinct, separable, ensuing losses” such as the asbestos contamination.

The United States Court for the Southern District of New York adopted similar reasoning when it came to separating an ensuing loss from the initial excluded cause of loss. It held that the cost to replace a defective concrete slab was not covered because faulty workmanship or materials were excluded causes of loss under the policy. Had the slab collapsed and damaged other property, however, the court reasoned that “such losses—wholly separate from the defective materials themselves—would qualify as non-excluded ensuing losses.”

Other courts examining the chain of causation have held that in order to be covered under an ensuing loss provision: the damage must be different in kind and not just different in degree from the excluded damage; the damage must result from a cause in addition to the excluded cause; or some kind of “intervening” cause must exist between the excluded and ensuing causes of loss. Some of the strictest approaches require the ensuing cause of loss to be separable and independent from the original excluded cause of loss and not directly related to it.

All of these various approaches point to the need for policyholders to carefully examine the law in their jurisdiction as well as the precise causal chain of the damage to their property. An expert may be necessary to assist in unraveling the chain of causation that led to the loss and may also be useful when it comes time to persuade an insurance company, and a court, that coverage should be resurrected.

Ensuing Loss Otherwise Covered

Another essential component of an ensuing loss provision is that the ensuing loss be independently covered under the terms of the policy. This component is phrased in several ways, but typically states that the insurance company will pay for an ensuing loss that is “otherwise covered” or “not otherwise excluded” under the terms of the policy.

The purpose of the ensuing loss provision is not to expand coverage. Rather, its purpose is to prevent a covered cause of loss from being denied

“It’s Alive!” continued on p4

"It's Alive!" continued from p3

simply because it followed a chain of events that was set into motion by an excluded cause of loss. Courts have been careful not to interpret ensuing loss provisions in such a manner as to supersede or otherwise make meaningless any policy exclusions. An ensuing loss provision cannot be construed so broadly that it swallows an exclusion. In other words, in order for coverage to be revived, it must have been alive in the first place.

An example is found in a recent decision by the Washington Court of Appeals, which disregarded the normal chain of causation analysis as totally irrelevant because the cause of the ensuing loss was excluded under the terms of the policy. In that case, faulty construction (an excluded cause of loss) led to water intrusion (a covered cause of loss) which resulted in decay (an excluded cause of loss). The court noted that the ensuing loss provision did not focus on the penultimate cause of loss, the water intrusion, but rather the final cause of loss, the decay. Decay was specifically excluded under the terms of the policy, thus defeating the ensuing loss provision. This is usually a straight forward component, but one that can be too easily overlooked.

Ensuing Coverage

Despite the diverse holdings and technical digressions into causation and logic, many courts have resurrected coverage where it first appeared to be lost. Policyholders have litigated and won coverage under ensuing loss provisions for damage resulting from water intrusion, fire, mold, rot, decay, contamination, collapse, and numerous other perils. So the next time disaster strikes, policyholders are well advised to take a closer look at those links in the chain. Those that successfully connect them will be glad they expended the effort. ▲

This article originally appeared in the *Legal Intelligencer, Real Estate supplement* (June 25, 2007).



Bryan W. Petrilla is an attorney in Anderson Kill's Philadelphia office. Mr. Petrilla's practice focuses on the area of insurance recovery exclusively on behalf of policyholders.

(267) 216-2742

bpetrilla@andersonkill.com

IRS Circular 230 Disclosure: To ensure compliance with requirements imposed by the IRS, we inform you that any U.S. federal tax advice contained in this communication (including any attachments) is not intended or written to be used, and cannot be used, for the purpose of (i) avoiding penalties under the Internal Revenue Code or (ii) promoting, marketing, or recommending to another party any transaction or matter addressed herein.

The *AKO Real Estate & Construction Advisor* is published periodically by Anderson Kill & Olick, P.C. to inform clients, friends, and fellow professionals of developments in real estate and construction law. The articles appearing in the *Real Estate & Construction Advisor* do not constitute legal advice or opinions.

Anderson Kill's Real Estate & Construction focus group is a group of attorneys from various Anderson Kill departments, including insurance recovery, real estate, and corporate who have an interest in legal issues in the real estate and construction fields. The Real Estate & Construction focus group meets periodically to share insights on new developments in insurance, construction and real estate law, in the belief that an inter-disciplinary approach to legal problems will often maximize client profitability or recoveries, while minimizing costs.

Thomas A. Neufeld, Editor, (212) 278-1840 or tneufeld@andersonkill.com

Real Estate & Construction Group, Co-Chairs

Arnold L. Bartfeld, New York, (212) 278-1511 or abartfeld@andersonkill.com

John B. Berringer, Newark, (973) 642-5133 or jberringer@andersonkill.com

The firm has offices in New York, Chicago, Greenwich, Newark, Philadelphia, and Washington, D.C.