UPDATES FROM THE INSURANCE DOCKETS

NEW JERSEY

Limitations Period Tolled Absent Clear, Unequivocal Denial of Coverage

As Superstorm Sandy related claims continue to move through the dockets in New York and New Jersey, the US District Court for the District of New Jersey recently applied the equitable tolling doctrine to find that the insured's claims for breach of contract and bad faith were not barred by the statute of limitations. *See Liguori v. Certain Underwriters at Lloyds London, No. 14-5898 (RBK/KMW),* 2015 WL 4402851 (D.N.J. July 17, 2015).

There, the insured suffered property damage caused by Superstorm Sandy and notified its insurer. The insurer retained an engineer who determined that while wind may have caused some insignificant cosmetic damage to the home, water surge/flooding ultimately demolished the home. Although the policy covered loss caused by wind, it did not provide coverage for loss caused by flood.

On February 25, 2013, the insurer issued a letter to the insured addressing the claim for property damage. The letter stated that damage caused by wind was covered under the policy and that damage was found at the property. The letter then claimed to enclose an estimate for repairs, applicable depreciation, deductible, and net payment owed on the claim. However, the dollar amount for each of these items was left blank. The letter then stated that the claimed damage caused by flood was expressly excluded under the policy. Finally, the letter stated that the insurer "reserved the right to amend, alter or supplement this letter should information become known in the future that would affect the content of this letter."

The insured did not respond to the February 25 letter and instead filed suit on August 21, 2014, nearly 19 months later. The insurer moved for summary judgment, arguing that the claims were barred by the policy's statute of limitations.

The parties agreed that the policy's one-year statute of limitations controlled. However, the insured argued that the insurer was estopped from raising a statute of limitations defense because its alleged denial letter was ambiguous.

Under New Jersey law, a statute of limitations contained in a contract for insurance is enforceable subject to the "equitable tolling doctrine." Generally, a claim accrues and the statute of limitations begins to run from the date of loss. Under the equitable tolling doctrine, the limitations period stops running from the time when notice is given to the insurer until the time when coverage is formally denied. For the limitations period to begin to run again, there must be a clear and unequivocal denial of coverage.

Here, the court found that while the insurer's letter denied flood coverage, the letter stated that damage caused by wind was covered. Although dollar amounts in the letter were left blank, the letter suggested that damage was found and payments would be made. Additionally, the insurer's reservation of rights to amend the letter as new information came in might cause an insured to assume that the denial was not final. Moreover, the insured need not show actual reliance on the letter to survive summary judgment, only that the letter was ambiguous. Accordingly, the court found that the letter was not a clear, unequivocal denial of coverage and, therefore, the limitations period continued to toll.

NEW YORK

Court Enforces Anti-Concurrent Causation Clause in Sandy Claim

The US District Court for the Southern District of New York recently granted an insurer's motion for summary judgment, finding that property damage caused when a wooden dock was driven into the insured property during Superstorm Sandy was excluded by the policy's anti-concurrent causation provision excluding coverage for water damage. *See Clarke v. Travco Ins. Co.*, No 13-cv-5140 (NCR) (S.D.N.Y. Aug. 7, 2015).

There, the insured property, located only twenty feet from the Hudson River in Nyack, New York, experienced substantial damage during Superstorm Sandy. Water and debris, including a 15' x 10' wooden dock from another property, were driven into the insured property, with flood waters rising roughly four feet in the lower level of the insured's home. The parties disputed whether water or wind drove the dock into the property.

The insurer's adjuster inspected the property and determined that the damage was almost exclusively caused by water. The insurer denied coverage based on this opinion. The insured, however, hired a professional engineer who opined that the wooden dock was driven into the property by wind, not water. On the insured's claim for breach of contract, the insurer moved for summary judgment.

The court first addressed whether it could consider the report of the insured's expert witness. On summary judgment, a court may consider only admissible evidence. Expert testimony is admissible in federal court only upon a showing that it rests on knowledge rather than subjective belief or unsupported speculation. Here, the PE's opinion that wind drove the dock was based on his living in the area during Sandy and on his incorrect belief that the storm hit land as a hurricane. He did not present any methodology or concrete data to support his views. Accordingly, the court ruled that his report could not meet federal standards for expert testimony. Nonetheless, the court considered his report as the opinion of a lay witness.

Even considering the report, however, the court found that the anti-concurrent causation language of the policy excluded coverage for the insured's claim. The policy in question stated that it did not cover "any direct or indirect loss or damage caused by, resulting from, contributing to or aggravated by [Water Damage]." It further provided that "loss from [Water Damage] is excluded regardless of any other cause or event contributing concurrently or in any sequence to the loss."

Here, a wooden dock sat on top of water and was driven by wind into the insured home. Even if the insured could somehow differentiate between damage caused by the dock and the general damage caused by the flood, the distinction could not overcome the policy's exclusion for water damage. The insured's own theory was that wind pushed the dock into the house *while on top of the water*. It was undisputed that water played a role in the dock's movement. Given the unambiguous exclusion for water damage, summary judgment entered for the insurer.

MASSACHUSETTS

Insured's Mere Request for Reference Will Not Toll Statute of Limitations

The Massachusetts Appeals Courts recently held that in order to toll the two-year statute of limitations under MGL c. 175, § 99, the parties must have actually begun the reference procedure before the limitations period has run. A mere request for reference will not suffice. The case is *Hawley v. Preferred Mut. Ins. Co.*, 88 Mass. App. Ct. 360 (2015).

On June 11, 2004, a ceiling in the insured premises collapsed after a tenant noticed water leaking from the above bathtub. The leak was caused after a shower door in the second-floor bathroom fell into the tub and caused the tub to crack. After further investigation, the insurer concluded that continued use of the shower after the crack developed caused additional leakage and allowed dangerous levels of mold to form. After months of adjusting and investigating the loss, the insurer denied the claim on November 8, 2004, due to the insured's failure to make repairs. However, the insurer reserved its rights to resort to other policy exclusions.

On May 26, 2006, the insured sent a 93A demand letter alleging violations of MGL c. 93A & 176D. On June 5, 2006, only 5 days before the expiration of the two-year limitations period provided by the policy and by c. 175, § 99, the insured sent the insurer a request for reference. On July 11, 2006, the insurer declined the request for reference and denied all liability under c. 93A & 176D. The insured sent three more requests for reference and a second 93A demand letter, all of which were denied, before filing suit on June 2, 2008, nearly four years after the date of loss.

After a seven-day bench trial, a Superior Court judge ruled that the insured's claims for breach of contract were barred by the statute of limitations and that the insured's bad faith claims lacked factual support. The insured appealed.

On appeal, the insured argued that his request for reference tolled the statute of limitations because it was made before the two-year limitations period had run. Under c. 175, § 99, the two-year limitations period may be tolled "if, within said two years,… the amount of loss shall have been referred to arbitration," in which case the insured may file suit within 90 days after an award has been made.

In affirming the judgment below, the Appeals Court declined to extend the statutory tolling provisions to apply where reference has been requested within the limitations period but has not yet begun. Notably, c. 175, § 100 grants the insurer 10 days to respond to a request for reference and gives the insured an additional ten days to answer that response. Moreover, § 99 allows an insured to timely file suit, the start of which may be delayed while reference proceeds. Given the insured's failure to utilize mechanisms provided by statute and by the policy for the timely filing of suit, the Appeals Court declined to create an additional vehicle for tolling the statute of limitations. Lastly, even if the request for reference did toll the statute of limitations, the insured waited an additional two years after the denial of the request before filing suit. Equitable tolling doctrines require a plaintiff to commence the action within a reasonable time. Given the insurer's clear denial, it was not reasonable for the insured to wait two additional years before filing suit.

Accordingly, the insured's suit was barred by the statute of limitations and judgment for the insurer was affirmed.

CONNECTICUT

Misrepresentations in Property Sale Do Not Constitute "Property Damage" Under Homeowners Policy

The Connecticut Appellate Court recently held that an insurer did not have a duty to defend its insured for claims of misrepresentations made during the sale of the insured property, because damages flowing from these misrepresentations could not be deemed "property damage" as defined under the policy. The case is *Lew London Mut. Ins. Co. v. Sielski*, 159 Conn. App. 650 (2015).

There, the insured contracted to sell the insured property to a buyer. As part of the contract, the insured stated that he had no knowledge of any issues with water seepage, rot and water damage, or faulty drainage on the property. On the closing date for the sale of the property, the contract for insurance between the insurer and insured was canceled.

After closing on the property, the buyer encounter several drainage and flooding issues with the property and discovered rotten and moldy beams in the basement. Given the extent of the flooding, as well as the existence of new beams attached to rotted beams, the buyer argued that the insured knew or should have known of these issues at the time of sale. When the buyer brought suit for misrepresentation, the insurer brought a separate action seeking a declaration that it had no duty to defend the insured in the underlying suit. After summary judgment was entered for the insurer, the insured appealed.

On appeal, the court considered whether the lower court properly determined that the suit for negligent misrepresentation and resulting injury did not constitute property damage as defined by the policy.

The policy provided that the insurer would defend the insured for suits brought "for damages for 'bodily injury' or 'property damage' caused by an 'occurrence' to which… coverage applies." Such an occurrence (i.e., an accident) must have resulted in "bodily injury" or "property damage." The policy defined "property damage" as "physical injury to, destruction of, or loss of use of tangible property."

Affirming summary judgment for the insurer, the court held that the buyer's damages resulting from the insured's alleged misrepresentations constituted economic and pecuniary losses, and not property damages as defined in the policy. In reaching its conclusion, the court echoed the analysis presented by each Connecticut Superior Court decision that had addressed the issue to date. Additionally, the court found significant support from several other jurisdictions that have reached similar conclusions.

Moreover, the court held that even if the buyer's complaint had alleged property damage as defined in the policy, the alleged misrepresentations could not constitute an "occurrence," as required for coverage, as those misrepresentations could not have resulted in the alleged property damage. Where the buyer's allegations necessarily require that the property damage existed before the sale in order for the insured to have made misrepresentations concerning their existence, the buyer's reliance on these misrepresentations could not have caused the damage. Rather, the damage must have predated the misrepresentations.

Where the insured could not show that there was an "occurrence" resulting in "property damage," summary judgment was properly entered for the insurer.

MASSACHUSETTS

First Circuit Finds Coverage in MA Commercial General Liability Policy Due to Ambiguities in Exclusion

The First Circuit Court of Appeals recently held that an insurer had a duty to defend and indemnify its insured after finding multiple ambiguities in the policy's Bodily Injury Exclusion, including its use of the term "contractor." The case is *US Liability Ins. Co. v. Benchmark Const. Services, Inc.*, 2015 WL 4747164 (1st Cir. 2015).

There, the dispute centered on the insurer's duty to defend and indemnify its insured for personal injury claims brought by another party's employee working on a home renovation site on which the insured was acting as general contractor. Although the homeowners had hired the insured as general contractor, they also hired a separate architect. The architect then hired a painter, whose employee fell on the job. Though no contractual or employment relationship existed between the insured and the architect, painter or her employee, the employee sued the insured for negligence. Relying on a Bodily Injury Exclusion, the insurer denied coverage and brought a declaratory action in the District Court for the District of MA.

The exclusion in question provided that the policy would not insure against "'Bodily injury' to any… 'employee'… of any contractor… arising out of … rendering services of any kind… for which any insured may become liable in any capacity." On cross motions for summary judgment, the district court entered judgment for the insurer. Finding that the term "contractor" unambiguously meant "anyone with a contract," the court reasoned that the painter, by virtue of her contract with the architect, constituted a "contractor" as used in the policy and the exclusion applied. The insured appealed.

In reversing the district court's decision, the First Circuit found two separate ambiguities in the above exclusion – including the term contractor – each of which were construed to trigger the insurer's duty to defend and indemnify.

First, the First Circuit looked to the terms "for which any insured may become liable." The insured argued that the phrase modified "service," i.e., the exclusion was triggered only if the injury occurred during the performance of services for which the insured may be liable. Because the insured could not be liable on the employee's painting contract, the exclusion did not apply. The insurer, however, argued that the phrase modified "injury," i.e., the exclusion was triggered if the insured may be liable for the actual injury. The exclusion's repeated use of the term "any" reveals the breadth of its intended scope.

Concluding that reasonable people could differ as to the proper interpretation, the court held that the exclusion was ambiguous and, therefore, the insured was entitled to have the ambiguity resolved in its favor. Accordingly, coverage applied under the policy. Moreover, the court reasoned that the outcome matched the reasonable expectations of the insured in that CGL insurance is meant to protect against losses to third parties arising from operation of the insured's business.

The First Circuit reached a similar conclusion as to the term "contractor." While the district court's construction was reasonable, the insured's interpretation – that the term referred only to those with whom the insured had contracted – was equally reasonable. Resolving the ambiguity in favor of the insured, the claim fell outside of the exclusion.

MISSOURI

Eighth Circuit Holds Equipment Repair, Replacement and Relocation Costs Covered as "Extra Expenses"

The Eighth Circuit Court of Appeals recently held that the costs to repair, replace and relocate specialty medical equipment used in the insured's office was covered under the Extra Expense provision of the insured's business owner's policy and was not subject to the policy limits for Building and Business Personal Property. *See Midwest Regional Allergy v. Cincinnati Ins. Co.*, 795 F.3d 853 (2015).

There, the insured building suffered extensive damage from a tornado, including damage to the insured's MRI machine, X-ray machine, and other specialized medical equipment. After the destruction rendered the insured building inoperable for medical practice, the insured chose to permanently relocate. In order to make the new location fully operational, the insured had to work out of a temporary location at reduced capacity, repair or replace the specialized medical equipment that was damaged or destroyed by the tornado, retrofit the new location to house this equipment, and hire a crane to move the equipment to the new office.

The insurer paid the policy limits for both building and personal property loss and also paid the full extent of the insured's losses from business income interruption. However, when the insured sought reimbursements for the cost to repair or replace the specialized medical equipment needed to resume normal operations, the insurer denied coverage. The insurer reasoned that these costs did not fall under the policy's Extra Expense coverage, but instead were losses covered by the Building or Business Personal Property provisions, for which the policy limits had been paid.

The insured brought suit in federal court. On cross motions for summary judgment, the district court ruled that the claimed expenses were covered Extra Expenses and, alternatively, that the policy was ambiguous and therefore afforded coverage. The insurer's appeal followed.

The dispute centered on the policy's definition of Extra Expense. In short, the policy provided coverage for necessary extra expenses incurred during the period of restoration caused by a covered cause of loss that would not have been incurred absent direct physical loss. The policy provided three definitions for Extra Expenses. After the third definition of Extra Expense, the policy contained a condition that the expense must reduce the amount of loss otherwise payable as Business Income coverage.

The insured argued that the first definition applied and that it defined Extra Expense as extra expenses incurred to continue operations at a replacement location including costs to equip the new location. The insurer argued that the condition tied to Business Income coverage modified all three definitions of Extra Expense and that because the costs to repair and replace the machines did not reduce payments that were otherwise payable under the Business Income coverage, no Extra Expense coverage applied.

The Eighth Circuit held that under the plain language of the policy, the costs of equipping the new office were covered Extra Expenses. The court reasoned that an ordinary person of average understanding in the insured's position would interpret the three definitions of Extra Expense as separate and distinct. Absent some connector indicating that all three definitions were modified by the condition requiring a reduction in Business Income losses, this provision applied only to the definition immediately preceding it.

The insurer further argued that even if Extra Expense coverage applied, the insured could not use this provision to circumvent applicable policy limits. Because the losses were covered as Building and Business Personal Property loss and because the policy limits had been paid for that coverage, no further payments were owed.

The court disagreed. Where the policy provided that Extra Expense coverage was not subject to the Limits of Insurance and the policy failed to exclude Extra Expenses also covered by a separate policy provision, an ordinary persons in the insured's position would expect coverage. Summary judgment was affirmed.

KANSAS

Under Kansas Law, Insurers May Depreciate the Cost of Labor when Calculating Actual Cash Value

On motion for summary judgment, the US District Court for the District of Kansas recently ruled that the insurer's practice of depreciating the cost of labor when determining actual cash value was lawful under Kansas law and applicable policy provisions. *See Graves v. American Family Mut. Ins. Co.*, No. 14-2417-EFM-JPO, 2015 WL 447868 (D. Kan. July 22, 2015).

There, a storm damaged the insured's roof and ceiling, and the insurer paid the actual cash value of her loss, depreciating both the cost of materials and labor. The policy defined "actual cash value" as "the amount which it would cost to repair or replace damaged property with property of like kind and quality, less allowance for physical deterioration and depreciation, including obsolescence." Replacement cost payments – which would essentially reimburse the depreciation costs subtracted from actual cost value – were available upon actual, timely replacement of damaged property.

When the insured failed to replace the damaged property, she filed suit seeking to recover the cost of depreciation attributed to labor. The insured argued that depreciation applies to items subject to physical deterioration. Because labor is not subject to physical deterioration, it therefore cannot be depreciated. The insurer argued that its practices were consistent with Kansas law, the recommendations of the Kansas Insurance Department, and policy language.

Concluding that a reasonable person in the position of the insured would expect the insurer to depreciate all costs required to repair the property, even labor costs, the court granted summary judgment to the insurer. The court reasoned that the policy covered the damaged property as an indivisible output, even if it consisted of tangible and intangible inputs (i.e., material and labor). The court drew an analogy to a new car's diminished value after being driven off the sales lot – we say that the car's value has depreciated without distinguishing between materials-value and labor-value. Where the policy requires actual replacement before replacement costs are recovered, the insurer may properly depreciate new replacement labor costs.

RHODE ISLAND

New York Court Rules Rhode Island Auto Liability Insurance Policy May Not Be Terminated Retroactively

The Civil Court of the City of New York recently ruled that a Rhode Island automobile liability insurance policy may not be rescinded *ab initio* due to material misrepresentations made by the insured in procuring the policy. *See 37 Ave Med., P.C. v. Metlife Auto & Home Ins. Co.*, 2015 NY Slip Op 51293(U) (Sep. 2, 2015).

There, the insured assigned his rights under his auto policy to medical providers after being injured in a car accident in New York. The insurer denied coverage, claiming that the policy was terminated *ab initio* due to material misrepresentations made by the insured when securing the policy. Apparently, the insured resided with his family in New York while listing on both his license and policy a Rhode Island address for a property owned by friends. The insured testified that he only resided at this Rhode Island address on weekends.

The policy in question was issued through the Rhode Island Automobile Insurance Plan governed by Rhode Island General Laws § 31-33-8(a). The parties disputed whether, under any circumstances, an insurer may retroactively terminate the liability coverage of such a policy.

After analyzing applicable statutes and regulations, the court determined that under Rhode Island law an insurer may not rescind *ab initio* mandatory automobile liability insurance, even if the policy was procured by material misrepresentation. While the regulations provide means and grounds for prospectively canceling coverage, an insurer may not do so retroactively. The court found support for this interpretation from the RI Automobile Insurance Handbook as well as the RI Department of Business Regulation's January 31, 2003 Insurance Bulletin. Accordingly, the claims of the insured's assignees were covered under the policy.

MASSACHUSETTS

Material Breach by Insured Precluded Coverage under Auto Policy's Optional Bodily Injury Provisions

The Supreme Judicial Court recently held that use of the insured automobile by an "excluded operator" constituted a breach of the insurance contract and relieved the insurer of its duty to pay optional coverage for bodily injury to a third party. *See Commerce Ins. Co. v. Gentile*, 472 Mass. 1012 (2015).

There, the insured executed an "operator exclusion" form promising that her grandson would not operate the insured vehicle under any circumstances. Given the grandson's driving record, the form served to decrease the insurer's risk while lowering the insured's premiums. The grandson later crashed the vehicle, causing injuries to a third party.

The SJC held that the insured's failure to prevent the grandson from operating the vehicle was a material breach of the insurance contract. Accordingly, the insurer was relieved of its contractual duty to pay for the injuries to the third party.

MASSACHUSETTS

Appeals Court Holds Corporate Insured Deemed to Have Knowledge of All Forms Listed in its Policy

Sloane and Walsh attorney Christopher Reilly successfully argued before the Massachusetts Appeals Court that summary judgment was properly entered for the insurer on an insured's suit seeking coverage related to a notice of violation letter issued to the insured by the California Center for Environmental Protection. The case is *30 Magaziner Realty, LLC v. Liberty Mut. Ins. Co.*, 87 Mass. App. Ct. 1137 (2015).

There, the insured argued before the Appeals Court that coverage should apply because the policy form allegedly disclaiming coverage was not provided to the insured during the applicable policy year. The Appeals Court discounted this argument, concluding that "[the insured] is deemed to have knowledge of the form through the policy's forms and endorsements lists, as well as through communications with the insurer]." Moreover, the motion judge had concluded that the insured could not show that coverage existed regardless of whether the form was included in the policy. Where the insurer had a duty to indemnify the insured for "suits for damages resulting from bodily injury or property damage," a notice of violation that was punishable by civil penalties could not constitute an occurrence that triggered coverage under the policy. Accordingly, The Appeals Court affirmed summary judgment for the insurer.

In a related case, Sloane Walsh also obtained a successful judgment from the Appeals Court upholding a reference award that valued the Actual Cash Value for the insured's claim below the amount already paid by the insurer. That case is *30 Magaziner Realty, LLC v. Peerless Ins. Co.*, 88 Mass. App. Ct. 1102 (2015).

There, the court disagreed with the insured's contention that the applicable policy did not incorporate prior policy provisions, because the parties clearly treated the applicable policy as a renewal of prior coverage and the newer policy unambiguously referenced the prior policy. Additionally, the court found that the insured's claims of unfair bias in the reference process were without merit and lacked support in the record. Summary judgment for the insured was affirmed.

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