

COMMERCIAL PROPERTY INSURANCE 101

BUILDER'S RISK AND PERMANENT PROPERTY INSURANCE

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I. INTRODUCTION

“Insurance” may be defined as the equitable transfer of the risk of loss, from one entity (the policyholder), to another (the insurer), in exchange for a monetary consideration (premium) and in which the insurer distributes the risk across a group of similarly situated persons or entities.¹

A. Overview of Insurance for the Construction Industry

A Washington statute defines “property insurance” as “insurance against loss of or damage to real or personal property of every kind and any interest therein, from any or all hazard or cause, and against loss consequential upon such loss or damage.”² In addition to other complimentary methods of risk transfer, such as indemnity and hold harmless agreements, disclaimers of liability, and limitations on damages or liability, insurance plays the most prominent role for risk transfer in the construction industry. In the context of property insurance, the most prevalent insurance for the construction industry includes Builder’s Risk insurance and “ALL RISK” property insurance.

B. The Importance of Property Insurance in a Construction Project

Property insurance is designed to indemnify anyone with an “insurable interest”³ in property against physical loss or damage to that property interest as a result of the occurrence of a specified peril. In contrast to liability insurance, which protects a party against the

¹ Jerry, *Understanding Insurance Law*, 3rd Ed. at p. 20 (2001).

² RCW 48.11.040.

³ RCW 48.18.040; *Cope Construction Company v. American Home Assurance Company*, 28 Wn. App. 38, 622 P.2d 395 (Wn. App. 1980) (contractor has insurable interest in Builder’s Risk policy on building under construction); *Gossett v. Farmers Ins. Co. of Washington*, 133 Wn.2d 954, 948 P.2d 1264 (1977) (“insurable interest” limited to improvements made by husband and wife to property the couple intended to purchase).

consequences of its own conduct, property insurance does not depend on the policyholder's conduct, but rather the policyholder's interest in the damaged property. Property insurance and liability insurance are designed to work together, complimenting and protecting the variety of interests a property owner, developer, or contractor has in connection with a construction project.⁴

In most commercial construction projects property insurance is specified in the construction contract. For example, in the American Institute of Architects Form AIA A201 the responsibility for acquiring both builder's risk and property insurance is allocated to either the owner, developer, or contractor, while the other interests, including all contractors and subcontractors, are required to be included as "additional insureds."⁵

II. "ALL RISK" PROPERTY INSURANCE

A. Requirements for Coverage

"ALL RISK" has been described as:

A policy of insurance insuring against "All Risks" is to be considered as creating a special type of insurance extending to risks not usually contemplated, and recovery will usually be allowed, at least for all losses of a fortuitous nature, in the absence of fraud or other intentional misconduct of the insured, unless the

⁴ In this regard, there are special types of policies available for a particular project. These types of policies which provide "cradle to grave" coverage are often used in very large construction projects and are known as either Owner Controlled Insurance Programs ("OCIP") or Contractor Controlled Insurance Programs ("CCIP"). These types of policies are designed to encompass the variety of insurable interests in a project, eliminate the need for each contracting party to have separate insurance, and allow for expeditious and economical claim resolution.

⁵ See, e.g., Article 11, INSURANCE AND BONDS, § 11.4., "Property Insurance." When coupled with the "waiver of subrogation" provision under § 11.4.7 of the A201-1997, the provision of Builder's Risk policy will include all interests on the project, including Owner/Developer/Contractor and subcontractor for damages caused by any peril covered by either a Builder's Risk or property insurance policy. Inclusion of all interests on a project within a Builder's Risk or property insurance policy precludes an insurer from any subrogation claim against a negligent subcontractor, for example. *Anderson Hay & Grain Company v. United Dominion Industries*, 119 Wn. App. 249, 76 P.3d 1205 (Wn. App. 2003); but see, *Public Employees Mutual Ins. Co. v. Sellen Construction Co.*, 48 Wn. App. 792, 740 P.2d 913 (Wn. App. 1987) (where definition of the term "work" under the AIA Contract defined the scope of a contractor's protection from a subrogation action).

policy contains a specific provision expressly excluding the loss from coverage.⁶

Among the necessary elements for coverage under an “All Risk” policy are: (1) the loss must be fortuitous;⁷ (2) the loss must not result wholly from an inherent quality or defect in the subject matter; (3) it must result from at least one extraneous cause; (4) the loss or damage must not result from the intentional misconduct or fraud of the insured;⁸ and (5) the risk must be lawful.⁹

1. Is the Loss Fortuitous

Washington courts require that a loss be “fortuitous.”¹⁰ In determining whether a loss is fortuitous, the following elements are considered: (a) a loss which was certain to occur cannot be considered fortuitous and may not serve as the basis for recovery under an All Risk policy; (b) in deciding whether a loss was fortuitous, a court will examine the parties’ perception of risk at the time the policy was issued;¹¹ and (c) ordinarily a loss which could not reasonably be foreseen by the parties at the time the policy was issued is fortuitous.¹² The burden of proving fortuity is on the policyholder, although as many courts have noted, it is not a particularly onerous burden, is determined in a subjective manner,¹³ and involves questions of fact.¹⁴

⁶ *Forman v. Holland American Ins. Co.*, 47 Wn. App. 596, 597, 736 P.2d 698 (1987); *Findlay v. United Pacific Ins. Co.*, 129 Wn.2d 368, 917 P.2d 116 (1996) (any peril that is not specifically excluded in the policy is an “Insured Peril”).

⁷ See, for example, *Terminal Freezers, Inc. v. U.S. Fire Ins. Co.*, 2008 U.S. Dist. LEXIS 48280 (W.D. Wash. 2008); *Underwriters Subscribing to Lloyd’s Insurance v. Magi, Inc.*, 790 F.Supp. 1043 (E.D. Wash. 1991).

⁸ Because intentional misconduct or fraud is itself not a fortuity and the lawfulness of a risk implicates public policy, both of which would disqualify a loss from coverage, this paper will not further discuss these issues.

⁹ See, e.g., *Avis v. Hartford Fire Ins. Co.*, 195 S.E.2d 545, 549 (N.C. 1973).

¹⁰ *City of Oak Harbor v. St. Paul Mercury Ins. Co.*, 139 Wn. App. 68, 73, 159 P.3d 422 (2007); *Churchill v. Factory Mutual Ins. Co.*, 234 F.Supp.2d 1182, 188 (W.D. Wash. 2002).

¹¹ *Public Utility District No. 1 v. International Ins. Co.*, 124 Wn.2d 789, 805-806, 881 P.2d 1020 (1994).

¹² *Frank Coluccio Construction Co., Inc. v. King County*, 136 Wn. App. 751, 768, 150 P.3d 1147 (2007); *Churchill, Id.*, at 1188-89

¹³ *Id.*, *Terminal Freezers, Inc. v. U.S. Fire Ins. Co.*, 2000 U.S. Dist. LEXIS 48280 (W.D. Wash. 2008).

¹⁴ *Hillhaven Properties, Ltd. v. Sellen Construction Co.*, 133 Wn.2d 751, 758, 948 P.2d 796 (1997).

2. Is the Loss from an External Cause

To say a loss must be from an “external cause” is to say the loss must not result from an “inherent vice” or infirmity present at the time the policy was issued, or constitute the expected result of normal wear and tear or deterioration.¹⁵ An inherent vice is often defined as “any existing defect, disease, decay or the inherent nature of the commodity which will cause it to deteriorate with the lapse of time;”¹⁶ or a cause of loss not covered by the policy, [which] does not relate to an extraneous cause but to a loss entirely from internal decomposition or some quality which brings about its own injury or destruction. The vice must be inherent in the property for which recovery is sought.¹⁷

B. Is There Physical Loss or Damage

The core principle of “All Risk” insurance is the notion that an external, fortuitous, physical cause has resulted in a peril or hazard producing a loss. Indeed, a standard insuring clause under an “All Risk” policy is:

We will pay for direct¹⁸ physical loss of or damage¹⁹ to COVERED PROPERTY at the premise described in the DECLARATIONS caused by and resultant from any Covered Cause of Loss.²⁰

What constitutes “physical loss or damage”? In *Washington Mutual Bank v. Commonwealth Ins. Co.*, *supra*, n.18, an engineering firm warned Washington Mutual that one of its buildings was at a risk of collapse. Relying on the engineering investigation, Washington

¹⁵ *Port of Seattle v. Lexington Ins. Co.*, 111 Wn. App. 901, 48 P.3d 334 (2002).

¹⁶ *Id.* at n. 19.

¹⁷ *Id.* at n. 20.

¹⁸ The term “direct” has been held to be synonymous with “proximate cause.” *Great Northern Ins. Co. v. Benjamin Franklin Federal Savings & Loan Association*, 793 F.Supp. 259, 261 (D. Ore. 1990), affirmed, 953 F.2d 1387 (9th Cir. 1992).

¹⁹ Physical loss” or “damage” or its equivalent “physical loss of or damage to” have consistently been interpreted to require that both “loss” and “damage” be modified by the work “physical.” See for example, *Washington Mutual Bank v. Commonwealth Ins. Co.*, 2006 Wn. App. LEXIS 1316 (Wn. App. 2006) (unpublished).

²⁰ CP00 10 06 95 ISO (1994).

Mutual evacuated the building, incurring significant economic losses. Washington Mutual hired a second engineering firm which concluded the building was structurally sound. In order to recover on its economic losses, Washington Mutual filed an action against its property insurers for the extra expense and business interruption losses it sustained as a result of evacuation of its own operations and those of its various tenants.

In an unpublished opinion, the Washington State Court of Appeals held there was no actual “direct physical loss or damage” to the property resulting in a peril that was not otherwise excluded. Even though Washington Mutual subjectively believed the property was in an imminent state of collapse because of structural unsoundness, in fact, as later developed, the structure was safe. In short, there was no “physical loss.”

On the other hand, in *Western Fire Ins. Co. v. First Presbyterian Church*, 437 P.2d 52 (Colo. 1968), the uninhabitability of a building because of the infiltration of gasoline vapors was held to constitute a “physical loss or damage” to the structure, triggering the property policies. *First Presbyterian* is distinguished from *Washington Mutual* by the fact that in the former, the building was actually uninhabitable by the objective, physical presence of vapors, while in the latter instance, the subjective believe of the owner was insufficient in and of itself to create a “physical” loss.²¹ “Physical loss or damage” has also been interpreted to include “loss of functionality.”²²

²¹ See also *Sentinel Management Co. v. New Hampshire Ins. Co.*, 563 N.W.2d 296, (Minn. App. 1997) (asbestos contamination held to be “direct physical loss”); *Farmers Ins. Co. v. Tru Tanich*, 123 Ore. App. 6, 858 P.2d 1332 (Ore. Ct .App. 1993) (loss caused by odor from methamphetamine operation was “direct physical loss”); *Essex Ins. Co. v. Bloom*, S.Fl.Ct. 562 F.3d 399, CA 1 (2009) (under CGL policy, carpet odors rendering tenant space uninhabitable constituted “physical injury to tangible property”).

²² *Wake Fern Food Corp. v. Liberty Mutual Fire Ins. Co.*, 406 N.J.Super, 524, 968 A.2d 724 (N.J. Super. App. Div. 2009) (damage to electrical power grid in Northeast United States in 2003 resulting in loss of power to food cooperative and subsequent food spoilage constituted “physical loss or damage”); *Southeast Mental Health Center, Inc. v. Pacific Ins. Co.*, 439 F. Supp. 2d 831 (W.D. Tenn. 2006) (“physical damage” includes loss of “functionality” of a pharmacy’s computer equipment citing *American Guaranty & Liability Ins. Co. v. Ingram Micro Inc.*, 2000 U.S. Dist. LEXIS 7299 (D. Ariz. 2000); *Columbia Knit, Inc. v. Affiliated FM Ins. Co.*, 1999 U.S. Dist. LEXIS 11873

There are circumstances in the construction process that “imperil” insured property without resulting in “physical loss or damage.” For example, in *Fujii v. State Farm Fire & Casualty Co.*, 71 Wn. App. 248, 857 P.2d 1051 (1993), heavy rainfall caused a landslide on a hillside above the policyholder’s home. Based on an expert’s opinion that the landslide damaged the “integrated engineering unit” of the home, the insureds argued they had suffered a “direct physical loss” under the Insuring Clause of their homeowner’s policy. The appellate court disagreed, observing:

. . . there was no discernable physical damage to the dwelling during the effect period of the policy.

The insured property, the “dwelling,” was not physically damaged by the landslide and, therefore, did not sustain a “direct physical loss” sufficient to trigger the policy.

C. Principles of Causation

Ultimately, analysis of an All Risk Property Policy devolves into a consideration of the principles of “causation.” A typical “All Risk” language employs the concept of “causation” as a link to coverage. Insurers, policyholders and courts have therefore been required to develop principles of causation that provide the nexus between the insured peril and the sought after indemnity.²³ Note that the common formulation of an Insuring Clause in an All Risk policy requires that the physical loss or damage to “covered property” be “caused by or resulting from any Covered Cause of Loss.” Since the 1983 case of *Graham v. Public Employees Mutual Ins. Co.*, 98 Wn.2d 533, 656 P.2d 1077 (1983), Washington has applied the rule of “efficient proximate cause” to determine whether a loss was caused by a covered or excluded peril under

(E. D. Ore. 1999) (mildew contamination was direct physical loss); *Murray v. State Farm Fire & Casualty Co.*, 203 W. Va. 477, 509 S.E.2d 1, 16-17 (W. Va. 1998) (“losses covered by the [all risk] policy, including those rendering the insured property unusable or uninhabitable, may exist in the absence of structural damage to the property.”)

²³ Under Washington law, whenever the term “cause” appears in exclusionary language, “it must be read as ‘efficient proximate cause.’” *Safeco Ins. Co. v. Hirschmann*, 112 Wn.2d 621, 773 P.2d 413 (1989).

circumstances in which two or more independent perils occur, either simultaneously or successively, to create a loss. The *Graham* court defined the “efficient proximate cause” rule as follows:

It is that cause which, in a natural and continuous sequence, unbroken by any new independent cause produces the event, and without which that event would not have occurred . . . or a peril specifically insured against sets other causes in motion which, in an unbroken sequence, in connection between the act and final loss, produced the result for which recovery is sought, the insured peril is regarded as the “proximate cause” of the entire loss.²⁴

Id., at 538. The efficient proximate cause rule applies only if two or more independent forces operate to cause the loss.²⁵ If the loss is the result of but a single cause, the rule does not apply since the causative peril is either covered or excluded.²⁶

The case of *Terminal Freezers, Inc. v. U.S. Fire Ins. Co.*, *supra*, at n.7, is illustrative of the application of the efficient proximate cause rule in a construction case. Terminal Freezers operated a cold storage facility in California. Areas of the facility were damaged by ice and Terminal Freezers made a claim for loss under its “All Risk” insurance policies. U.S. Fire denied, claiming the exclusion for “faulty design/workmanship” precluded

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²⁴ See, also, *Findlay v. United Pacific Ins. Co.*, 129 Wn.2d 368, 917 P.2d 116 (1996); *Safeco Ins. Co. v. Hirschmann*, 112 Wn.2d 621, 773 P.2s 413 (1989) (the rule of efficient proximate cause cannot be circumvented by anti-concurrent causation lead-in language to the exclusionary section of the policy).

²⁵ *Kish v. Insurance Company of North America*, 125 Wn.2d 164, 171, 883 P.2d 308 (1994).

²⁶ Recasting or renaming a peril in an attempt to create “separate perils” will not change the efficient proximate cause rule. See, e.g., *Kish v. Insurance Company of North America*, *id.*, n.24; *Capelouto v. Valley Forge Ins. Co.*, 98 Wn. App. 7, 990 P.2d 414 (Wn. App. 1999) but see also *American States v. Rancho San Marcos Properties*, 123 Wn. App. 205, 97 P.3d 775 (Wn. App. 2004) (arson is not the same peril as “vandalism”); *Sunbreaker Condominium Association v. Travelers Ins. Co.*, 79 Wn. App. 368, 376, 901 P.2d 1079 (Wn. App. 1995) (“characterization of perils focuses on whether the events are contractually distinct, with reference to specific policy language and the perils allegedly involved in the particular factual setting.”)

coverage. Thus, the court was faced with two independent perils, one potentially covered “ice,” and one clearly excluded, “faulty design/workmanship.”²⁷

In many construction defect cases, the contest is between an excluded construction defect and potentially covered water damage. For example, defective construction results in water intrusion which, in turn, results in dry rot which, in turn, results in either mold or collapse. What is the efficient proximate cause under circumstances in which several perils occur in a logical sequence to result in the final event, a “collapse?”²⁸

The “efficient proximate cause” doctrine is perhaps the most important property insurance principle at work in determining coverage. The doctrine provides the analytical framework for determining whether a covered peril is to be considered the cause of the loss or, if one of many multiple excluded perils, are to be considered the cause of the loss.

D. Consideration of Potential Coverages and Common Exclusions in Construction-Related Claims

1. Efficient Proximate Cause and Anti-Concurrent Causation Language

The principle of efficient proximate cause is the analytical tool employed by Washington courts to determine coverage when two or more independent causes concur to cause a loss. In an effort to eliminate coverage following decisions from California in the 1980’s, the insurance industry developed what has been characterized as “anti-concurrent causation” language. A

²⁷ Generally, the issue of causation is one of fact for a jury or fact-finder to determine unless “the facts are undisputed and the inferences therefrom are plain and incapable of reasonable doubt or difference of opinion.” *Allstate Ins. Co. v. Raynor*, 143 Wn.2d 469, 479-80, 21 P.3d 7070 (2001); *Graham v. Public Employees Mutual Ins. Co.*, 98 Wn.2d 533, 656 P.2d 1077 (1983).

²⁸ See, for example, *Dally Properties, LLC v. Truck Insurance Exchange*, 2006 U.S. Dist. LEXIS 30524 (W.D. Wash. 2006) and *Dally Properties, LLC v. Truck Insurance Exchange*, 2006 U.S. Dist. LEXIS 30623 (W.D. Wash. 2006). In the context of a Builder’s Risk policy, see *North Coast Enterprises v. St. Paul Fire & Marine Ins. Co.*, 2006 U.S. Dist. LEXIS 20245 (W.D. Wash. 2006), in which the contest was between a potentially covered “weather condition” and faulty, defective, or inadequate workmanship, specifications, etc.” where water intrusion damaged a building during the course of construction.

common formulation of the industry's reaction to the efficient proximate cause doctrine is the following language:

We will not pay for loss or damage caused directly or indirectly by any of the following. Such loss or damage is excluded regardless of any other cause or event that contributes concurrently or in any sequence to the loss.²⁹

The purpose of the foregoing lead-in language to the exclusion section of the policy is to uniformly exclude losses in which an excluded peril is a concurrent, causal factor. Thus, for example, if the triggering cause of a loss is a covered peril, but an excluded peril concurs to produce the ultimate result, then, consistent with the anti-concurrent lead-in language, the loss will be excluded.³⁰

Only four states have either legislatively or by case law precluded application of the anti-concurrent causation language. These states are California,³¹ North Dakota,³² West Virginia,³³ and Washington. Every other jurisdiction that has considered application of the anti-concurrent causation lead-in language, has upheld application of the language and circumvention of the efficient proximate cause rule. Fortunately, under Washington law, the anti-concurrent causation language has no application and, in most instances, insurance companies attach special endorsements to property forms eliminating the lead-in language.

²⁹ Form CP 10 10 06 95 (ISO 1994).

³⁰ The "anti-concurrent causation" language has received a work out in the dozens, if not hundreds, of cases arising out of Hurricane Katrina in both Louisiana state and Fifth Circuit courts. Treatment of the "anti-concurrent causation" language is exemplified by a case such as *Leonard v. Nationwide Mutual Ins. Co.*, 499 F.3d 419 (5th Cir. 2008) ("The Doctrine of Efficient Proximate Cause, The Katrina Disaster, Prosser's Folly, and the Third Restatement of Torts: Cracking the Conundrum," 54 Loyola Law Review 1 (Spring 2008).

³¹ California Insurance Code § 530, *Julian v. Hartford Underwriters Ins. Co.*, 35 Cal.4th 747, 27 Cal.Rptr.3d 648, 110 P.3d 903 (Cal. 2005).

³² *Western National Mutual Ins. Co. v. University of North Dakota*, 643 N.W.2d 4 (N.D. 2002) (rule codified at N.D. Cent. Code §§ 26.1-32-01, 26.1-32-03).

³³ *Murray v. State Farm Fire & Casualty Co.*, 203 W.V. 477, 509 S.E.2d 1 (W.V. 1998); *Safeco Ins. Co. of America v. Hirschmann*, 112 Wn.2d 621, 773 P.2d 413 (1989).

2. Exclusion for Faulty, Inadequate or Defective Workmanship, Design , Specifications, Etc.

The greatest hurdle a policyholder must overcome in a construction case is the exclusion for “construction defects” comprised of any “faulty, inadequate or defect workmanship, materials, specifications, repair, maintenance, etc.” Under Washington’s formulation of the efficient proximate cause rule, it is the triggering or initiating cause which is to be deemed the “efficient proximate cause.” If the triggering cause of property damage in a construction defect case is the faulty workmanship or design then, absent an “ensuing loss provision,”³⁴ there will be no coverage. A good example of application of the faulty workmanship exclusion is *Wright v. Safeco Ins. Company of America*, 124 Wn. App. 263, 109 P.3d 1 (Wn. App. 2004).³⁵

In *Wright*, a condominium owner sued its insurer, Safeco, for losses caused by water overflowing from an interior fountain which, in turn, resulted in water and mold damage to portions of Mrs. Wright’s condominium. The court found that construction defects, excluded perils, initiating the sequence of events resulting in water intrusion which, in turn, resulted in mold, also an excluded peril. *Wright* illustrates the breadth of the faulty workmanship, etc., exclusion as well as application of the Ensuing Loss Clause incorporated within the faulty workmanship exclusion. Here, in *Wright*, the sequence of events was that an excluded peril (faulty workmanship) resulted in water intrusion (covered peril) which, in turn, resulted in mold (excluded peril). Consequently, the court found that the initiating cause, faulty workmanship, eliminated most all of the coverage save for that that might have ensued from the faulty

³⁴ See, e.g., *Costco Wholesale Corporation v. Commonwealth Ins. Co.*, 45 F. Appx. 646, 2002 U.S. App. LEXIS 17395 (Circuit 2002); *McDonald v. State Farm Fire & Casualty Co.*, 119 Wn.2d 724, 837 P.2d 1000 (1992); *Wright v. Safeco Ins. Co.*, 124 Wn. App. 263, 109 P.3d 1 (Wn. App. 2004); *Assurance Company of America v. Wall & Associates, LLC of Olympia*, 379 F.3d 557 (9th Cir. 2004); *Dally Properties, LLC v. Truck Insurance Exchange*, 2006 U.S. Dist. LEXIS 30524 (W.D. Dist. 2006).

³⁵ See also *Capelouto v. Valley Forge Ins. Co.*, 98 Wn. App. 7, 990 P.2d 414 (Wn. App. 1999); *Terminal Freezers, Inc. v. U.S. Fire Ins. Co.*, *supra.*, n.7; *Dally Properties, LLC v. Truck Insurance Exchange*, *supra.*, n.28; *Churchill v. Factory Mutual Ins. Co.*, 234 F.Supp.2d 1182 (W.D. Wash. 2002).

workmanship. *Wright* argued that the water intrusion, a covered peril, ensued, and it was therefore covered. However, since the damage went further and included mold, an excluded peril, the court held the entire loss was excluded.

3. Collapse: Is it Covered or Excluded?

In most ISO-related policies, collapse is an excluded peril subject to a limited number of circumstances in which collapse will be covered. Many manuscript policies do not mention “collapse” as either an excluded or covered peril.

In most collapse cases, the issue is *first*, what is the definition of the term “collapse;” and *second*, if there is collapse coverage, under what circumstances is the coverage triggered?

The short answer to the first question is collapse is either undefined or, if defined, often defined as requiring a “falling down or caving in.”³⁶ If undefined, collapse has been considered to mean either “imminent collapse” or “substantial impairment of structural integrity.”³⁷

4. Coverage for Changes in Law and Ordinance

Between the time a building is constructed and loss or damage discovered, local zoning ordinances and building codes may have changed. Absent coverage for “Law and Ordinance” coverage, (code upgrade coverage), a property owner will not be entitled to compensation for the cost of meeting the then current building codes at the time of the loss, even if the property owner has replacement cost coverage.³⁸ The contours of code coverage have also been the subject of some analysis in the State of Washington. While much depends on the language of the “Law and

³⁶ Under a common ISO policy formulation, collapse is defined to mean “an abrupt falling down or caving in of a building or any part of a building with a result that the building or part of the building cannot be occurred for its intended purpose.”

³⁷ *Assurance Co. of America v. Wall & Associates, LLC*, 379 F.3d 557 (9th Cir. 2004); *see also Allstate Ins. Co. v. Forest Lynn Homeowner’s Association*, 892 F. Supp. 1310 (W.D. Wash. 1995), opinion withdrawn, 914 F.Supp. 408 (W.D. Wash. 1996); *The Bedford, LLC v. Safeco Ins. Co.*, 2007 Wn. App. LEXIS 2675 (Wn. App. 2007) (where the issue became one of how to define “substantial impairment of structural integrity” in engineering terms).

³⁸ *See, e.g., Dombrowski v. Farmers Ins. Co.*, 84 Wn. App. 245, 928 P.2d 1127 (Wn. App. 1996); *Roberts v. Allied Group Ins. Co.*, 79 Wn. App. 323, 901 P.2d 317 (1995).

Ordinance” coverage, ultimately, the issues turn around the scope and extent to which code upgrades will be allowed where the loss or damage is only to a portion of a building.³⁹

E. Suit Limitation Provisions

No discussion of first party property insurance would be complete without brief mention of a trap for the unwary: the Suit Limitation Provision. By regulation, the mandated policy form for fire and extended coverage insurance in the State of Washington is the 1943 New York Standard Fire Insurance Policy (165 Lines).⁴⁰ This policy form contains a 12-month period of time within which a policyholder has to initiate an action against its insurer or forever be barred. A contractual period of limitation is allowed under RCW 48.18.200(1)(c), and have been consistently upheld in the State of Washington.⁴¹

Possible salvation, however, is the WAC regulation 284-30-380 which provides:

Insurer shall not continue negotiations for settlement of a claim directly with a Claimant who is neither an attorney nor represented by an attorney . . . without giving notice that the time limit may be expiring and may affect the Claimant’s rights. Notice shall be given to first party claimants 30 days, and to third party claimants 60 days before the date on which such time limit may expire.

Similar provisions have resulted in an insurer’s inability to assert application of the suit limitation provision under circumstances in which it failed to give notice to a policyholder not represented by an attorney.⁴²

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³⁹ *Commonwealth Ins. Co. of America v. Grays Harbor County*, 120 Wn. App. 232, 84 P.3d 304 (2004); *DePhelps v. Safeco Ins. Co. of America*, 116 Wn. App. 441, 65 P.3d 1234 (2003).

⁴⁰ WAC 284-20-010(3).

⁴¹ *Simms v. Allstate Ins. Co.*, 27 Wn. App. 872, 621 P.2d 155 (1980).

⁴² *Spray, Gould & Bowers v. Associated International Ins. Co.*, 71 Cal. App. 4th 1260, 84 Cal. Rptr. 2d 552 (Cal. App. 2d 1999); *Superior Dispatch, Inc. v. Insurance Corporation of New York*, 176 Cal. App. 4th 12, 97 Cal. Rptr. 3d 533 (Cal. App. 2d, July 30, 2009); *Mathis v. Lumbermen’s Mutual Casualty Ins. Co.*, 354 Ill. App. 3d 854, 822 N.E.2d 543 (2004).

III. BUILDER'S RISK INSURANCE⁴³

Builder's Risk insurance is specialized property insurance designed to insure against the accidental loss or damage to a contractor's work and property occurring during the course of construction.⁴⁴ Builder's Risk insurance is first party property insurance and subject generally to the same rules of construction and interpretation as an All Risk policy. What separates Builder's Risk insurance from "All Risk" property insurance is the finite character of a Builder's Risk policy, i.e., it is a policy in effect for a limited period of time, usually circumscribed by the "course of construction" of a building.

In most cases, Builder's Risk insurance is patterned after a typical "All Risk" property policy, whether in manuscript form or a form developed by the Insurance Service Office (ISO). The policy is designed to cover "all risks of physical loss or damage except as specifically excluded." Perils such as faulty workmanship, design, specifications, materials, repair or maintenance are often excluded as are other typical perils such as settling, cracking, expansion, mechanical breakdown, wear and tear, deterioration, corrosion, latent defect, or inherent vice.

There are a number of issues, however, to be aware of in connection with Builder's Risk policies.

1. Is there an exclusion for "pre-existing property" in the "Covered Property" section of the policy? Generally, absent language to the contrary, damage to pre-existing property during the course of construction will be covered. *See, e.g., Homestead Fire Ins. Co. v. DeWitt*, 245 P.2d 92 (Okla. 1952); *Thompson v. Trinity Universal Ins. Co.*, 708 S.W.2d 45 (Tex. App. 1986).

⁴³ For a more complete review of Builder's Risk insurance see *Kingman, Builder's Risk Insurance*, the Seminar Group, CLE, "Insurance in the Construction Industry" (October 16, 2008) (available from the author).

⁴⁴ *Russ & Segalla, Couch On Insurance 3d*, ¶ 1:53 (1997).

2. Builder's Risk policies can either be "one off" policies designed for a specific project, or "blanket" policies covering multiple projects. Many blanket policies are "reporting policies" in which the insured is required to report either the dollar value of construction in place or the percentage of completion of the construction. Failure to timely report will result in either a rejection of coverage or a limitation on coverage to the last reported value.

3. Builder's Risk policies usually encompass all "insurable interests" of a project, including the developer, owner, general contractor and all subcontractors. Often, architects and engineers are not covered under a Builder's Risk policy and the language of the policy must be reviewed if that is the desired outcome.

4. To the extent that a Builder's Risk policy encompasses all of the insurable interests of every level and tier on a project, there will be no right of subrogation by the Builder's Risk insurer against any interest.⁴⁵

5. Builder's Risk policies often incorporate "Ensuing Loss" provisions. "Ensuing Loss" provisions provide for an element of coverage even though the "efficient proximate cause" is an excluded peril (faulty workmanship, for example) and results in a fire, collapse or explosion. The resulting loss is covered, the initiating peril is not.⁴⁶

⁴⁵ AIA Form A201-1997 provides for a waiver of subrogation in § 11.4.7: "To the extent covered by property insurance obtained pursuant to this § 11.4 or other property insurance applicable to the work . . ." While it is clear there will be no right of subrogation under a Builder's Risk policy, it is unclear whether a successive All Risk property policy on a completed project will also incorporate that waiver of subrogation. A number of cases have held, however, that the waiver of subrogation extends even into the future and binds "All Risk" insurers providing post-construction policies. See, *Argonaut Great Central Ins. Co. v. DiTocco Construction, Inc.*, 2007 U.S. Dist. LEXIS 93846 (Dist. N.J. 2007); *TX.C.C., Inc. v. Wilson/Barnes General Contractors*, 233 S.W.3d 562 (Tex.App.5th 2007); *Touchet Valley Grain Growers v. Opp & Seibold General Construction, Inc.*, 119 Wn.2d 334, 831 P.2d 724 (1992); *Anderson Hay & Grain v. United Dominion Ins. Co.*, 119 Wn. App. 241, 76 P.3d 1205 (Wn. App. 2003).

⁴⁶ See, for example, *McDonald v. State Farm Fire & Casualty Co.*, 119 Wn.2d 724, 837 P.2d 1000 (1992); *Allianz Ins. Co. v. Impero*, 654 F.Supp. 16 (E.D. Wash. 1986); *Houser & Bolduan*, "Special Causation Problems in First Party Property Insurance," 52 FDCC Quarterly (Winter 2002).