



Feature Article

Flood Exclusions in Windstorm Policies: Knowing the Insurance Coverage Issues*

————— Dennis J. Wall, Esquire



Hurricanes arrive with wind and water. Windstorm policies are usually received with expectations that they cover losses resulting from winds and windstorms. Windstorm coverage is provided in a great number of policies that may be better known by other names, including those that were considered in many of the cases analyzed in this article, such as homeowners' policies, special multi-peril policies, all risk policies, and policies extending piers, wharfs and docks coverage.

Almost all insurance policies which extend coverage to loss caused by wind or windstorms contain a "flood" exclusion. The standard flood exclusion presently in use purports to exclude 'loss caused by or resulting from flood, whether or not driven by wind.'

Flood insurance, in contrast, is expressly underwritten specifically for losses caused by floods. Flood insurance is available under a program administered and effectively underwritten by the United States government, pursuant to the National Flood Insurance Act. Flood insurance is not within the reach of the present article.

On September 15, 2005, the Mississippi Attorney General filed a complaint naming many insurance companies as defendants. The Mississippi Attorney General's complaint provides several legal theories for requesting Mississippi's state court to refuse to enforce, or to declare void, the flood exclusion in windstorm policies issued to Mississippi policyholders. In addition to the starting points served by that complaint, many decided cases exist revealing the arguments and issues surrounding windstorm policies and flood exclusions, and the focus of this article will be on a review of what courts decided in reported cases. The arguments and issues from past decided cases will presently confront most policyholders, insurance companies, coverage counsel, and courts in many insurance coverage cases to come.

Evidence of the Meaning of the Standard Flood Exclusion.

In any insurance coverage case, proof of what the insurance policy language *means* can go a long way toward obtaining the desired result. In Florida, for example, that issue is not in doubt, at least where only one of the parties presents expert testimony on the crucial issue discussed in this article, which is how the court should interpret and apply the meaning of the flood exclusion in a windstorm policy.

Florida courts are on top of that situation. A business partnership was the plaintiff and policyholder in an insurance coverage case and was the only party in that case to provide the trial court with opinion testimony of an expert witness as to "the meaning of the language contained" in a flood exclusion. The same expert testified about the meaning of the language that the insurance industry used in other exclusions in the policy at issue. A verdict was returned finding coverage, in favor, of course, of the policyholder under that windstorm

policy. On appeal, Florida's appellate court wrote in a reported opinion that because of the uncontradicted expert testimony, the trial court's judgment entered upon the verdict was supported by substantial, competent evidence. In effect, based on such evidence, that judgment was virtually irreversible. As the Florida appellate court summed up: "no dispute existed as to the interpretation of the policy language since the plaintiff presented the only competent evidence on this point." *West American Insurance Company v. Rauch*, 412 So. 2d 956, 958 (Fla. 4th DCA 1982), *review denied*, 424 So. 2d 764 (Fla. 1983).

Findings and holdings that determine the issue of whether the flood exclusion is applicable to a particular case, may thus depend in the final analysis upon the evidence presented on the central question of policy meaning, before the court or jury reaches any questions about coverage causation doctrines, discussed below.

"Loss Resulting" from Wind or from Flood.

Legal or proximate cause of the policyholder's loss is almost beside the point in the decided cases confronting flood exclusions in windstorm policies. *Proof of the factual causes of the policyholder's loss, i.e., proof of what the claimed losses resulted from, ordinarily determines the outcome of whether a jury will find or a judge will determine a loss was caused by excluded flood waters or was caused instead by wind, a covered peril.*

First, where the proof in the particular case shows *only one* cause of loss, and that cause is excluded, such as loss resulting from the sea or ocean water, then a flood exclusion has been held to apply. Such was the situation confronting a New York appellate court nearly 25 years ago. The court's ruling in that case ought to be reviewed by counsel who represents any of the large number of Hurricane Katrina's victims who suffered losses when one or more levees broke.

Policyholders on the Gulf Coast in particular, who suffered losses as a result of broken levees holding back bodies of water, will thus probably need to address a 1981 decision of New York's appellate court. In that case, a dike held back waters in a barge canal. The dike burst. Damage resulted. The insured argued that the dike was negligently maintained. Thus, argued the insured in that case, when heavy rains fell, the dike broke and the policyholder suffered a resulting loss. The policyholder, a business, argued that this event was therefore not the result of a "flood" excluded from coverage under its policy.

New York's Third Appellate Division, in the case of *E.B. Metal & Rubber Industries, Inc. v. Federal Insurance*

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Company, 84 A.D.2d 662, 663, 444 N.Y.S.2d 321, 322 (App. Div. 3d Dep't 1981), disagreed: "All the policy requires is that there be rising waters which break through boundaries and flow upon the insured's land to constitute a flood. It is irrelevant that a defect in the dike may have also contributed to the break."

From published news reports, it appears to be fairly clear that levees gave way to hurricane winds or, perhaps waters driven by hurricane winds or both. When the levees broke, further, they apparently released many gallons of water from Lake Pontchartrain and other waterways directly into the City of New Orleans and surrounding areas. If courts in Louisiana, Mississippi, Alabama, or elsewhere are going to decide cases based on a judicial determination making it significant that a defect in the levees may have also contributed to the loss, together with rising waters of an excluded flood, then most if not all such courts will be faced with, and likely asked to distinguish, the decision to the contrary by New York's appellate court in *E.B. Metal*.

Another set of losses resulting from Hurricane Katrina, again according to widely broadcast news reports, was the result more specifically of storm winds and waters that destroyed oceanfront property. Oceanfront buildings and other property faced damage as a result of storm surge, in a case decided by New York's appellate court in 1987. The New York appellate court held that such damage was excluded in that case.

The policy in that case contained a flood exclusion. New York's Appellate Division described the loss in terms of legal or proximate cause based on the facts and policy language involved in that case. The court reached what it called "the only reasonable conclusion to be drawn," which was that the proximate cause "of the damage was that water from Long Island Sound, driven by the wind, propelled objects into the [insured business's] damaged building. Where, as here, the water was the [legal] cause of the damage, coverage is excluded," the New York appellate court held in *Steve's Pier One, Inc. v. Insurance Company of North America*, 131 A.D.2d 834, 517 N.Y.S.2d 194, 195 (N.Y. App. Div. 2d Dep't 1987).

Other courts follow instead what they call the "efficient proximate cause doctrine." This doctrine, which is followed in Louisiana, for example, holds that "[i]t is sufficient to show that the particular peril was the efficient cause of the loss notwithstanding that another cause or causes contributed to the loss." *Riche v. State Farm Fire & Casualty Company*, 356 So. 2d 101, 103 (La. Ct. App.), *cert. & review denied*, 358 So. 2d 639 (La. 1978). There, the loss of fishing gear while the policyholder was on a boat that sank on a reservoir was held covered by a windstorm policy and not subject to a flood exclusion: "We find that damage caused by windstorm (or resulting waves) over a body of water, such as a lake or reservoir, does not come within the scope of this exclusion." *Riche*, 356 So. 2d at 104.

In some insurance coverage cases, apportionment becomes the coverage problem. Courts in apportionment cases may apply the flood exclusion where part of the claimed damage is the result of flood, either to exclude identifiable damage which is shown to be the result of excluded flood¹, or to exclude all of the claimed damage where the loss just cannot be apportioned between covered and excluded causes of the resulting loss. See *Transcontinental Insurance Company v. RBMW, Inc.*, 262 Va.

502, 511-14, 551 S.E.2d 313, 317-19 (2001).

In some jurisdictions, even where apportionment might be the rule, such as in a case decided by the Texas Supreme Court, it may nonetheless result that the appellate court will hold that coverage exists where the proof shows that the loss resulted from a covered peril and it may not matter if some other, perhaps excluded cause, was the *legal or proximate cause* of the loss. See *State Farm Lloyds v. Marchetti*, 962 S.W.2d 58, 61 (Tex. Ct. App. Houston [1st Dist.] 1997), *review denied (unreported)* (Tex. July 3, 1998).

If the Flood Exclusion is "Ambiguous" in a Windstorm Policy, Then it Should be Strictly Construed.

Ambiguity in cases involving interpretation of insurance policies means that any such sufficiently challenged provision of the policy at issue will be construed strictly against the insurance company which wrote it. For good or ill, the courts just do not apply this rule unless there *is* an ambiguity. Parenthetically, in most jurisdictions, the fact that the flood exclusion is an *exclusion* in a windstorm policy will cause the court to follow the same rule of strict construction concerning an insurance policy.

The courts which have addressed the issue of ambiguity of the flood exclusion in past cases have held that the "flood" exclusions of the past were *unambiguous*. *E.g.*, *E.B. Metal*, 84 A.D.2d at 663, 444 N.Y.S.2d at 322; *Hardware Dealers*, 393 S.W.2d at 314.

In the *E.B. Metal* case, the policy at issue defined the word, "flood." That policy definition was quoted at length by New York's highest court in holding that the flood exclusion at issue there was not ambiguous. On the other hand, the language of the *E.B. Metal* flood exclusion is very similar to today's standard flood exclusion.

In the Texas Supreme Court's opinion in *Hardware Dealers*, the policy language which extended coverage for losses resulting from wind and which exclude coverage for losses resulting from flood, reads very nearly the same as the policy language most often used by the insurance industry today.

Clearly, cases like *E.B. Metal* and *Hardware Dealers* must be made known to counsel who face arguments that flood exclusions in windstorm policies are ambiguous at the present time.

"Adhesion Contracts" May Not Be Argument Enough, Yet "Unconscionability" May Perhaps be Found after the Disasters of 2005.

In his complaint, Mississippi's attorney general raised the issue of adhesion to basically void the standard flood exclusion after Hurricane Katrina. The courts have defined an "adhesion contract" as a preprinted, standard form contract presented to the consumer on a take-it-or-leave-it basis. *E.g.*, *Hospital Authority of Houston County v. Bohannon*, 272 Ga. App. 96, 98-99, 611 S.E.2d 663, 666 (2005), *cert. denied (unreported)* (Ga. September 19, 2005). Under that judicial definition, flood exclusions in windstorm policies issued by insurance companies would clearly appear to qualify

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¹ See *Hardware Dealers Mutual Insurance Company v. Berglund*, 393 S.W.2d 309, 312-13 (Tex. 1965).

as adhesion contracts.

However, in the decided cases, proof that an insurance contract is a contract of adhesion is not enough to reach the result of a judgment that it or any part of it is void and unenforceable. In the reported cases in which appellate courts were confronted with issues of unconscionability, a holding of unconscionability even concerning an insurance policy is a relatively rare achievement. There must be proof of unconscionability in most jurisdictions and in most cases in which the issue of unenforceability is raised, or the court will negatively decide that issue and perhaps move on to other issues.

Therefore, in most jurisdictions, according to a review of the litigated cases resulting in appellate opinions through September 2005, proof of adhesion only will not move the courts to judge that the insurance policy is void and unenforceable. Generally, if not mostly or always, the policyholder that raises “adhesion” must *also* prove that an undesired provision of the insurance policy is “unconscionable.” Specifically, in an insurance coverage case in which the policyholder attacks the standard flood exclusion in any one of a number of windstorm policies on the ground that it is a preprinted provision presented to the policyholder on a take-it-or-leave-it basis so that such a flood exclusion in the policy at issue is void and should not be enforced because the exclusion is part of an adhesion contract, the policyholder according to the decided cases must be prepared to also prove that it would be “unconscionable” for the court to enforce the flood exclusion in that particular case.

This is a burden of proof that has not been addressed to date in many reported cases involving flood exclusions issued as a part of windstorm policies, *but it is a burden of proof that has often been discussed by courts confronted with litigation over other alleged unconscionable contracts. E.g., Blue Cross Blue Shield of Alabama v. Rigas*, ___ So. 2d ___, 2005 WL 2175451 *5 - *6 (Ala. September 9, 2005)²; *Norwest Financial Mississippi, Inc. v. McDonald*, 905 So. 2d 1187, 1192-95 (Miss. 2005)³.

If an Interpretation of the Flood Exclusion Favorable to the Insured is Available to Suggest to the Court, then “The Reasonable Expectations of The Insured” Should Require that Interpretation to be Followed.

The doctrine of “reasonable expectations of the insured” is accepted in some jurisdictions in the United States. That doctrine holds that insurance policies must be interpreted in light of the “reasonable expectations of the insured” and that where there may be competing and reasonable interpretations, the reasonable expectations of the insured proffered on behalf of the policyholder will govern the interpretation of the insurance policy provisions. The doctrine of reasonable expectations of the insured has been raised against exclusions similar to the flood exclusion in past reported cases, and it has been raised in the Mississippi attorney general’s complaint.

Courts in past cases have *applied* those similar exclusions, although the courts also applied the doctrine of reasonable expectations of the insured in those cases. In *Julian v. Hartford Underwriters Insurance Co.*, 35 Cal. 4th 747, 761, 110 P.3d 903, 912, 27 Cal. Rptr. 3d 648, 658-59 (2005), a “weather conditions” exclusion provision was applied by the California

Supreme Court to bar coverage. In that same case, the California Supreme Court also applied the reasonable expectations of the insured doctrine. *Cf. Hospital Authority of Houston County v. Bohannon*, 272 Ga. App. 96, 99, 611 S.E.2d 663, 666 (2005), *cert. denied (unreported)* (Ga. September 19, 2005).

In *Hospital Authority*, the Georgia Court of Appeals *rejected* a contractual limitation on stem cell transplants on the evidence that was presented in the case at bar. The evidence showed that the stem cell transplants limitation was inserted into the employer’s self-funded health benefits plan, but the limitation was not provided to the plaintiff insured-employee. The subject plan was interpreted under the doctrine that “[l]ike an insurance policy, the subject health benefits plan should be construed as reasonably understood by an enrollee.” To say again, the evidence and proof often determine the outcome of insurance coverage cases to which the legal theory of Coverage then molds itself.

Newly Invoked, Not Yet Frequently Applied: “Consumer Protection Acts” and Flood Exclusions in Windstorm Policies.

No decided case has been found as of this writing, in which a state’s consumer protection act was applied to a flood exclusion in a windstorm policy. The Mississippi Consumer Protection Act is *alleged* by the Mississippi attorney general in the complaint seeking to void flood exclusions in windstorm policies issued to Mississippi policyholders.

As a rule, consumer protection acts generally require fault on the part of the defendant. Consumer protection acts were enacted to enable courts to impose penalties or award damages or both, for “deceptive,” “unfair,” “fraudulent,” and similar trade practices. Whether a flood exclusion in a windstorm policy violates a state’s consumer protection act will ordinarily, then, require proof of one or more other reasons that such exclusions should be inapplicable to the losses suffered by the policyholder.

EPILOGUE: “Brownie, you’re doing a heck of a job.”

Many will bear responsibility for the deadly and delayed response to Hurricane Katrina. Some will also bear responsibility for destruction thereafter, and perhaps for disaster yet to come. Some of those responsible will respond by being forced to pay damages, some will not. At this writing, a great deal of the reported damage following the path of Hurricane Katrina in the City of New Orleans and in the immediately surrounding areas, at least, was caused in whole or in part by

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² In this case, the opinion of the Supreme Court of Alabama contains a thoughtful and informative review of many procedural unconscionability and substantive unconscionability issues in a case involving an arbitration provision in a group major-medical policy. The Supreme Court of Alabama held that, in the end, there was no unconscionability of either kind in that case and remanded with directions to grant the group insurance company’s motion to compel arbitration.

³ In this decision, the Supreme Court of Mississippi’s opinion related many different concepts of unconscionability in relation to an arbitration agreement that was printed within documents constituting a loan agreement and particularly with respect to a sale of credit life and disability insurance. The Supreme Court of Mississippi held that there was no evidence relating to the arbitration agreement to which those unconscionability legal concepts would be applied.

breaks in one or more levees that once held back Lake Pontchartrain and other watercourses from otherwise dry and populated ground. In a recent case, a municipality was exonerated on the basis of “the emergency response” or emergency rescuer doctrine – which by all accounts will *not* often exonerate all or some of those likely to become involved in cases filed after Hurricane Katrina. That recent case is quoted below, not because it lends support to any particular legal position but rather because it contains thought-provoking language about duties and responsibilities.

This kind of language has been sorely lacking, in the minds of many people, since Hurricane Katrina made landfall on August 29, 2005. It suggests the possibility that in appropriate cases, courts may recognize a cause of action, or a claim upon which relief can otherwise be granted, against governmental entities or other entities or persons responsible for failing to maintain the now-broken levees *or* who failed to repair them to hold back the waters during and immediately after passage of the hurricanes and windstorms. *See* the unofficially reported opinion in the case of *Merchants White Line Warehousing, Inc. v. City of Des Moines*, 665 N.W.2d 439, 2003 WL 1022838 **1 (Iowa Ct. App. 2003):

Plaintiffs [four business entities] sued the City of Des Moines (City) claiming the City was negligent in failing to fill an opening in a levy prior to and during a flood....

This action stems from the massive floods experienced in the Des Moines area during the summer of 1993. According to the provisions of the local flood plan, adopted in 1967, the City was responsible for the operation and maintenance of facilities, such as levees and embankments, created for flood protection. The City was also responsible for developing and

implementing an “emergency flood plan” in coordination with the [U.S. government] Army Corps of Engineers.

Conclusion

In sum, many insurance coverage arguments have been made in past cases concerning the application of flood exclusions in windstorm policies. Many arguments are justifiably available or can reasonably be made that suggest that flood exclusions in all kinds of windstorm policies should not be allowed or applied to bar insurance coverage to pay claims for losses that result from covered perils. My purpose in this article holds to present the arguments and many of the decided cases from the far past and from the immediate past as well, using as a springboard or as a catalyst the allegations in the complaint filed by the Mississippi attorney general in September of 2005. If those arguments are to be extended, such must be left to the talents and abilities of creative Insurance Coverage Counsel for policyholders and, yes, for insurance carriers alike, who will directly confront the many issues of insurance coverage in particular cases for the many, many losses left behind by hurricanes in 2005 -- and who will similarly confront the untold losses yet to result from future events.

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