Collapse Coverage

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Collapse claims are an emerging concern in the first-property insurance arena. These claims are typically raised under the Additional Coverage for Collapse clauses found in many homeowners and commercial property policies. Generally, these claims involve progressive decay that has occurred over several years or defective material or methods used in construction, remodeling or renovation, both of which ultimately affect the structural members of the covered buildings. Frequently insureds will claim that this decay or defective material or methods caused structural impairment tantamount to a collapse. Therefore they claim coverage under the collapse provision of the policy, even though there is no actual "falling down" of the building. Because this is an emerging area of claims, there are relatively few court decisions addressing the critical issues relating to collapse. Those jurisdictions that have considered these claims are divided on the key issue of what constitutes collapse, the actual falling down of the building or the mere substantial impairment of the structural integrity of the building. Another key issue is the issue of when decay is "hidden" and therefore covered by the collapse provision of the policy.

The standard policy language in an All Risk Commercial Property policy and in a Multi-peril Homeowners' policy provides a general grant of coverage for loss or damage resulting from direct physical loss, except for those losses excluded under the policy. The policies list several exclusions to coverage such as: wear and tear, deterioration, rust, corrosion, settling, shrinking, cracking or collapse. Coverage for collapse is therefore excluded in the first instance, other than that provided for within the additional coverage for collapse. Thus, collapse coverage is an exception to the policy's exclusion, and notwithstanding that "all risk" coverage may be provided, the insured has the duty of demonstrating that the collapse was caused by one of the specifically identified covered causes. *Borg-Warner Corp. v. Insurance Company of North America*, 174 A.D.2d 24, 577 N.Y.S.2d 953 (3rd Dept. 1992) *lv. app. den.* 80 N.Y.2d 753, 587 N.Y.S.2d 905, 600 N.E.2d 632 (1992).

The additional coverage for collapse provides coverage for risk of direct physical loss involving the collapse of a building or any part of a building caused by: (a) specified causes of loss in the commercial property policy1 and covered perils in the homeowners' policy , (b) hidden decay, (c) hidden insect or vermin damage, (d) weight of people or personal property, (e) weight of rain that collects on the roof, (f) use of defective material or methods in construction, remodeling or renovation, if the collapse occurs during the course of the construction, remodeling or renovation. The terms "collapse", "hidden" and "substantial impairment" are not defined in the policies and therefore raise issues with respect to how they will be defined by the courts. In addition, the collapse provision creating coverage states that "Collapse does not include settling, cracking, shrinking, bulging or expansion." Therefore, a further issue for litigation is whether the cause of the "collapse" resulted from settling, cracking, shrinking, bulging or expansion, which would be excluded from coverage. See, *Medina v. Liberty Mutual Fire Insurance Company*, 243 A.D.2d 544, 665 N.Y.S.2d 294 (2nd Dept. 1997).

Interpretation of the insurance policy is a matter of state law. Therefore, we must look to the courts of the State of New York for an interpretation of terms "collapse" and "hidden". There are

two standards for collapse that have been recognized by the courts around the country. Historically, the courts have required an actual falling down of a building to constitute a collapse. This is now the minority view. The trend more recently is to find coverage under the collapse provision for lesser events such as the substantial impairment of the structural integrity of the building and this standard has now become the majority view in this country and in the State of New York.

In 1977 the United States Court of Appeals, Second Circuit, in *Bailey v. Hartford Fire Insurance Co.*, 565 F.2d 826 (2nd Cir. 1977), recognized that there was a division in the courts of New York in dealing with the word "collapse" and that the law of New York was unsettled on the point. The Court, while not answering the question, predicted that the issue would be resolved by the courts to extend beyond the requirement that the building need actually fall down or be demolished or reduced to rubble. The Court found that the "parties to the contract certainly did not contemplate that the insured would be called upon to wait for a total destruction to take place to achieve coverage under the policy." *Id* at 831.

The issue arose again in *Royal Indemnity Company v. Grunberg*, 155 A.D.2d 187, 553 N.Y.S.2d 527 (3rd Dept. 1990). There the Court found that "determining whether a collapse has occurred rests largely on the degree of damage (citation omitted)." *Id* at 528. The court, following the view of the majority of American jurisdictions, held that "a substantial impairment of the structural integrity of a building is said to be a collapse (citation omitted)." *Id.* The Court went on to hold that an interpretation of the policy faulting the insured for preventing the actual collapse of the building and "triggering coverage only in the event their property was actually demolished or reduced to rubble would be unreasonable, to say the least (citation omitted)." *Id* at 529. See also, *M-Square Theaters, Inc. v. Transamerica Insurance Co.*, 1993 WL 42231, 3 (S.D.N.Y. 1993)("In order to be considered a 'collapse', the roof does not need to have actually fallen. New York law provides that 'a substantial impairment of the structural integrity of a building is said to be a collapse.'")

By reason of the foregoing, New York has now adopted the position of the majority of the jurisdictions in this Country that a showing of substantial impairment of structural integrity is sufficient in order to trigger coverage under the policy. See, also, *Beach v. Misslesex Mut. Assur. Co.*, 532 A.D.2d 1297 (Conn. 1987). It is interesting to note that in many of the cases where the courts adopt this lesser standard of collapse, the facts of the case indicate that the building, or a part thereof, is in imminent danger of collapse. It is therefore uncertain whether the lesser standard of "substantial impairment" would still result in collapse coverage under facts showing no imminent threat of collapse.

A minority of jurisdictions still require an actual and sudden falling down of the building for the collapse coverage of the policy to be triggered. See, *Mundy v. Narragansett Bay Insurance Company*, 1995 WL 941523, 3 (R.I.Super. 1995)("For plaintiffs to be able to recover for their loss, the loss to the property must have been due to a falling in, loss of shape, or reduction to flattened form or rubble of the building."); *Heintz v. United States Fidelity and Guaranty Company*, 730 S.W.2d 268, 269 (Mo.App. 1987)("There must have been a falling down or collapsing of a part of a building. A condition of impending collapse is insufficient." "Without actual collapse there is no recovery under the insurance policy and no cause of action.")

Even if there is a "collapse", for coverage to ensue the "collapse" must result from one of the stated causes set forth in the additional coverage provision. Most of the "collapse" cases involve

"collapse" allegedly caused by "hidden decay" and the "use of defective material or methods in construction, remodeling or renovation if the collapse occurs during the course of the construction, remodeling or renovation", both of which are covered causes under the typical collapse provision. Interestingly, the issue of "hidden decay" has received very little attention by the courts prior to this time. However, as these claims are reported and adjusted, the issue of the insured's knowledge of the decay becomes critical. Whether the decay was known or unknown can determine whether the loss is excluded or covered. At this time, there is only one published case in New York which addresses this issue.

In *M-Square Theaters, Inc. v. Transamerican Insurance Co., supra*, the Court was faced with the collapse of a roof allegedly caused by hidden decay. The issue before the Court was whether or not the decay found on the underside of the concrete roof was "hidden". The insured contended that the decay was "hidden" because it was neither disclosed to or recognized by the insured or anyone else prior to the collapse. The insurer contended that the decay was not "hidden" because it was visible. With respect to the definition of "hidden", the Court held as follows:

> "Hidden" means more than a lack of knowledge or awareness of a condition. Although no case law interpreting the term "hidden" in a comparable context is available, the dictionary defines "hide" as "to put or keep out of sight; secrete" or "to prevent the disclosure or recognition of; conceal." American Heritage Dictionary, 621 (New College Ed. 1976). Secreted or concealed describe the position of that which is "hidden", not the knowledge of the searcher. Thus, something is "hidden" if it is situated in such a way as to make it difficult for someone to see or recognize. Consequently, for the decay to be "hidden", not only must M-Square have been unaware of the decay, but M-Square's ability to recognize the decay must have also been hindered or impaired.

1993 WL 42231, 3.

The Court found that given that understanding of "hidden", a material question of fact

> existing as to whether the decay therein, which was only visible from the plenum space between concrete roof and the decorative ceiling of the cinema, was "hidden".

Other jurisdictions apply an objective standard that decay is not "hidden" if the insured knew or should have know that the decay existed. See, *Island Breakers v. Highland Underwriters Ins. Co.*, 665 So.2d 1084 (Fla.App. 1995); *West American Ins. Co. v. Chateau La Mer II Homeowners Ass'n, Inc.*, 622 So.2d 1105 (Fla.App. 1993). The policy behind this objective standard is that the insured should not be allowed to claim that damage resulting from its decision to avoid proper maintenance and repairs is covered by the policy as "hidden decay" when the insured is aware, or should have been aware, of the developing decay and structural damage.

One difficulty with collapse claims is that the covered cause of loss, collapse caused by hidden decay, is closely intertwined with other excluded causes of loss. The law in the State of New York on this issue is that the efficient proximate cause of the loss is what controls. "In determining whether a particular loss was caused by an event covered by an insurance policy where

other, non-covered events operate more closely in time or space in producing the loss, the question of whether the covered event was sufficiently proximate to the loss to require that the insurer compensate the insured will depend on whether it was the dominant and efficient cause (citations omitted)." *Throgs Neck Bagels, Inc. v. GA Insurance Company of New York*, 241 A.D.2d 66, 671 N.Y.S.2d 66, 68 (1st Dept. 1998). In *Molycorp, Inc. v. Aetna Casualty and Surety Company*, 78 A.D.2d 510, 431 N.Y.S.2d 824, 825 (1st Dept. 1980) the Court held that there "was no merit to plaintiff's claim that the applicable law in ... New York ... would look to the cause nearest to the loss. Rather, the operative test where damage results from two causes, one within and one without the scope of coverage, is to establish which was the proximate cause of the loss-what would the ordinary and reasonable businessman conclude was the cause of the loss?"

In *Home Insurance Company v. American Insurance Company*, 147 A.D.2d 353, 537 N.Y.S.2d 516, 517 (1st Dept. 1989) the Court held that "'the causation inquiry stops at the efficient physical cause of the loss; it does not trace events back to their metaphysical beginnings' (citation omitted)." The court there found that "the efficient or dominate cause of the loss was the short circuit in the electrical system; the steam merely set the stage for that later event, and therefore, the escape of steam was the remote and not the proximate cause of the loss." *Id.* In addition, the Court in *Molycorp* held that the determination of which of the two causes of loss was the dominate and efficient cause is "generally a factual issue to be determined by the trier of fact". *Id.*

As a cautionary matter, one should be aware that not all policies are the standard ISO policies cited herein. The policy language governs what is excluded and what is covered by the policy. Therefore, one must read the policy in full to determine whether or not collapse is excluded or covered, and the terms for such exclusion or coverage. For example, in *ABI Asset Corp. v. The Twin City Fire Insurance Company*, 1997 WL 724568 (S.D.N.Y. 1997) the policy was an all risks policy which neither covered nor excluded "collapse". Section 5 of policy contained the following exclusions: "(e) loss or damage directly or indirectly caused by fault, defect, error or omission in design, plan or specification; * * * (l) loss of use, delay, loss of market, bankruptcy foreclosure, deterioration, latent defect, inherent vice, moth, vermin, termites or other inspects, wear, tear or gradual deterioration, rust, wet or dry rot, mold, smog, contamination." In addition, Section 5 of the policy contained an "anti-concurrent cause clause" in which the introductory language in Section 5 states: "This policy does not insure against loss or damage caused by, resulting from, contributed to or aggravated by ..." The Court in *ABI Asset* found that New York courts have interpreted similar anti-concurrent cause clauses to mean "that where a loss results from multiple contributing causes, coverage is excluded if the insurer can demonstrate that any of the concurrent or contributing causes of loss are excluded by the policy." *Id* at 2.

The insurer in *ABI Asset* took the position that the collapse was due to an inherent vice and design defect and therefore was excluded by the terms of the policy. The insurer accepted the findings of the insured's expert that "creep" caused the buckling of the wall and foundation system which led to the collapse of the building. The expert defined "creep" as "time dependent deformation due to sustained load." *Id.* The expert also stated that creep is "an inherent and predictable property of cementicious material like mortar and concrete." *Id.* The Court noted that New York courts have interpreted "inherent vice" to mean "a natural defect in material which causes a failure to occur. (citation omitted)." *Id.* The Court concluded that there "can be no doubt that creep, as defined and described by ABI's own expert, is an inherent vice, and therefore falls under an exclusion to the insurance policy's coverage." *Id.* The insured unsuccessfully argued that creep did

not fall into the category of inherent vice by citing to *Essex House v. St. Paul Fire & Marine Ins. Co.*, 404 F.Supp. 978 (S.D.Ohio 1975). The Court in *ABI Asset* found that the holding in *Essex House* did not support the insured's argument. In *Essex House* the court found that creep was one of eleven factors which contributed to the collapse of a building, but that negligent workmanship and faulty design were the primary causes. Because the policy in *Essex House* did not contain an anti-concurrent clause and did not exclude design defect, the *ABI Asset* Court found the holding therein inopposite.

Alternatively, the Court in *ABI Asset* found that the loss was further excluded under the terms of the policy as the insured's expert testified that design defect was a contributing factor in the collapse of the building, and design defect was a peril which was specifically excluded under the policy.