CASE COMMENTARY:

MINNESOTA SUPREME COURT ISSUES WOODDALE BUILDERS DECISION: "*MORE ISSUES RAISED THAN RESOLVED*"[1]

October 5, 2006.

Today the Minnesota Supreme Court issued its long-awaited decision in Wooddale Builders, Inc. v. Maryland Cas. Co., et al. Court File Nos.: A04-1442, A04-1612 (October 5, 2006). The case was postured before the court to address just a few "discrete and identifiable" issues. However, the court chose instead to inject new life into a previously resolved allocation issue, introduce new confusion on what constitutes a trigger of coverage in water intrusion cases, and promised that the high court will need to hear more cases before carriers and policyholders will have the "last word" on the trigger and allocation rules applicable to water intrusion coverage litigation. In other words, the case raises more issues than it resolved.

Wooddale Builders arrived at the court to ostensibly resolve two specific issues:

1) Is the "end date" of a pro-rata-by-time-on-the-risk allocation of coverage the date the claim is made known to the insured or the date the damaged property is remediated? and

2) Do carriers obligated to defend the insured equally share defense costs, or allocate defense costs in a manner consistent with the parties' "time-on-the-risk" indemnity exposure?

The carriers involved in the case stipulated to several points; therefore, it seemed the reason the court took further review was to correct certain errors apparently made by the court of appeals in its opinion. Technically, the court did so in issuing the following holdings:

[1] This Update is educational in that the content is intended to both inform the reader of the court's new opinion, and to present thoughts and questions which encourage discussion and rebuttal. The views expressed in this Update are not necessarily those of Johnson & Condon, P.A. or its clients. Responses, questions or comments are invited.

1) In water intrusion cases *which are subject to a pro-rata-by-time-on-the-risk allocation of coverage*, the allocation end date is the date the insured becomes aware of the claim *(subject to a major caveat discussed below)*; and

2) Carriers share defense costs equally under pro-rata-by-time-on-the-risk allocation of coverage scenarios where recovery of defense costs is not barred by Minnesota's Iowa National[2] rule.

If the court ended its analysis with these technical rulings (and without the caveats), Wooddale Builders would have merely been a case which provided litigants with logical and workable rules to follow in these coverage cases. Unfortunately, the court went far beyond these specific rulings. In so doing, the supreme court has invited several more years of trigger and allocation coverage actions to address issues which, to this point, seemed relatively settled.

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The Court Upsets Several Established Certainties Enunciated in Past Trigger and Allocation Caselaw.

The Insurance Industry Business Climate is Now a Factor in Allocating Damages. The specific allocation issue raised to the high court in Wooddale Builders was whether policies on the risk *after the insured received notice of a claim* were triggered and share in the allocation of the damages at issue. Despite the fact the insured knew of damages at a house, the court of appeals ruled that policies in effect after the time the insured was notified of a loss were to have damages allocated to their time periods on a pro-rata basis. In rejecting this proposition, the supreme court correctly observed that allocating damages to policies on the risk after the claim was asserted runs counter to the concept that a policyholder is entitled to coverage for damage which is "expected" by the insured. Therefore, despite the fact new property injury is created after the date the policyholder becomes aware of the damage, the policies on the risk after the date the insured is notified of the claim are not obligated to pay for an allocated share of the damages.

Unfortunately, at this point, the court chose to address an issue which admittedly had not even been addressed at the trial court level (Opinion at p. 6, fn. 3) and which has been described as being the "twilight zone" of coverage issues – whether the business climate surrounding the insurance industry alters the application of trigger and allocation rules. The court rejected this invitation in 1997 when it declined to transfer policyholder obligations for uninsured years of coverage to the carriers in Domtar, Inc. v. Niagara Fire Ins. Co., 563 N.W.2d 724 (Minn. 1997). Today, however, the court enunciated an exception to the allocation rules which shifts the responsibility for payment

[2] Iowa Nat'l Mut. Ins. Co. v. Universal Underwriters Ins. Co., 276 Minn. 362, 150 N.W.2d 233 (1967). The Iowa National decision bars carriers from seeking equitable contribution for defense costs from other carriers who may also owe the insured a defense obligation.

of damages from the policyholder to triggered coverages from later years which were uninsured if the policyholder can show coverage for the risk at issue was "unavailable."

Here's how the new allocation exception rule works. Assume a claim involves a house which was built ten years prior to the policyholder being notified of a water intrusion loss. For the first nine years, the contractor bought insurance which covered it for this water intrusion loss. However, in year ten, insurance for this type of water intrusion loss was "unavailable," so the contractor's policy did not insure this claim. Under the court's new exception to the pro-rata-by-time-on-the-risk allocation of damages rule, *no* damages are allocated to the year the claim is asserted against the contractor. Instead, those damages are compressed back into the first nine years to then be allocated pro-rata among these earlier nine time periods. This is true despite the fact none of these earlier policies covered the contractor for damages occurring in the tenth year after the house was built.

If the damages claimed were $250,000.00, this new exception to the allocation rule would be applied as follows:

Application of Traditional Allocation Rules:		Application of "Unavailable" Allocation Exception:	
Year 1:	$25,000.00	Year 1:	$27, 777.78
Year 2:	$25,000.00	Year 2:	$27, 777.78
Year 3:	$25,000.00	Year 3:	$27, 777.78
Year 4:	$25,000.00	Year 4:	$27, 777.78
Year 5:	$25,000.00	Year 5:	$27, 777.78
Year 6:	$25,000.00	Year 6:	$27, 777.78
Year 7:	$25,000.00	Year 7:	$27, 777.78
Year 8:	$25,000.00	Year 8:	$27, 777.78
Year 9:	$25,000.00	Year 9:	$27, 777.78
Year 10:	$25,000.00	Year 10:	$ 0.00

The court rationalized this exception by stating that application of Minnesota's allocation rules do not rigidly adhere to the "actual injury" rule that a policy will only cover property damage which happens during its policy period.[3] Therefore, "the allocation of liability between insurers requires

[3] The court supports this statement by citing, not to allocation cases, but to the trigger cases of SCSC Corp. v. Allied Mut. Ins. Co., 536 N.W.2d 305 (Minn. 1995) and In Re Silicone Implant Ins. Coverage Litigation, 667 N.W.2d 405 (Minn. 2003) to support this proposition. SCSC and Silicone Implant never addressed allocation principles. Instead, these cases involved factual determinations which allowed the court to determine that the injuries at issue were "complete" at or about the time of the events involved in the cases. This factual determination only triggered the concurrent policies (primary and excess) on the risk at the time of the "discrete and identifiable event" involved in those cases. In other words, the character of the completed injuries in SCSC and

a flexible approach." Opinion at p. 24 (citing N. States Power Co. v. Fid. & Cas. Co. of N.Y., 523 N.W.2d 657, 661 (Minn. 1994).[4] The "flexibility" here is to provide the policyholder with the exact windfall it would not provide in Domtar by having an insurer pay for damages because of property damage (or bodily injury) which occurred outside of its policy period.

Unfortunately, rules based on economic business conditions do little more than focus coverage litigation on issues which have nothing to do with an application of the facts of the claim to the language in the applicable insurance policies. In the recent decades, the insurance industry has been required to exclude coverage for a wide variety of losses because of the unforseen financial impacts of the claims. Asbestos, lead, groundwater contamination, employment issues, mold and completed operations for residential contractors are but a few of the risks many insurers no longer cover. The rule enunciated today will allow an insured to obtain coverage for these risks under older policies if the insured is lucky enough to have at least one policy predating the change in the insurance environment, and can retain an expert to convince the trial court that such insurance is no longer "available."

This rule naturally raises the question of what is meant by the concept of "unavailability." Coverage can still be procured for many types of risks which are otherwise excluded under a variety of other liability policies. The point is whether the insured is "willing" to pay the heightened premium associated with these specialized insurance products. Most policyholders will not to purchase these specialized products because of price. Does "unavailability" mean "commercially unavailable" because the price is too high? Or, so long as any insurance product is "available," no matter the price, will the damages then be allocated to the insured? These questions can only be answered by hiring specialized insurance market experts to testify about what the policyholder's options were in the marketplace. This no doubt will turn rather simple allocation cases into questions of whether "available" coverage is actually unavailable because of price, the lack of knowledge of the product, or even perhaps that the product available did not have the capacity to provide insurance to an entire line within the geographic area at issue. In other words, allocation coverage cases will now be

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Silicone Implant evolved over time, much like disc herniations in car accidents which lead to deteriorating muscle tissue in years after the accident. These "evolving complete" injuries have nothing in common with newly created injuries over consecutive years of time from the point of initial injury until the time the claim is asserted. Indeed, the court recognized this distinction when it cited Domtar to observe that "[t]he factual presumption of continuous damage cannot be amended solely to benefit the insured." Opinion at p. 20. Unfortunately, the court has now done just that with its holding.

[4] The irony of this citation is that the court is not considering an allocation "among insurers," but an allocation *between* insurers and the policy holder. There is a reason to be flexible in the allocation of damages *among* insurers, but nowhere does the court provide a valid reason to alter the allocation rules when the insured might be adversely impacted by an allocation of damages pro-rata-by-time-on-the-risk. As noted above, the court rejected this concept in Domtar.

decided by insurance industry economic dynamics, and not by the facts of the case as applied to the policy language. These types of considerations will only exponentially increase coverage action costs to all parties (and the court) by a diversion of valuable resources to answer the proverbial question: "How many fairies can dance on the head of a pin?"

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The Court Invites Litigation to Address Whether Water Intrusion Cases are Governed by a Trigger of a Single Policy or of Multiple Polices. One of the stipulations involved in Wooddale Builders was that all parties agreed the damages were allocable pro-rata-by-time-on-the-risk. Therefore, technically, the parties had also agreed that multiple policies were triggered by the water intrusion claims at issue because the damage was caused by the new introduction of the "contaminant" (water) into the houses' cavities over the years from the time of house's sale until at least the date of the claim. Because of this, the court observed:

> "[F]or the purposes of this opinion, the applicability of the pro-rata-by-time-on-the-risk method is the law of the case. *Accordingly, the issue whether the pro-rata-by-time-on-the-risk method is generally applicable to water intrusion damage cases is not before us.*"

Opinion at p. 9, fn. 6. Despite the fact trigger issues were not before the court, the Opinion contains several passages which question whether the court believes this was a prudent stipulation for the parties. For example, the court makes comments such as the following:

> "Arguably, the damage to the homes is traceable to a discrete and identifiable event, such as installation of windows, installation of the flashing, or the application of the building paper." Id.

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> "[W]hen a discrete event gives rise to damages, it is reasonable for the insured to expect that its insurer on the risk at the point of initial injury will pay all damages that flow from that discrete event, regardless of when remediation occurs. The result is consistent with our consideration of the parties' intent or reasonable expectations in construing insurance policies." Id. at p. 18-19 (citation omitted).

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> "If the parties had assumed that damages resulted from a single discrete occurrence, such as faulty installation of the windows or the flashing, then under our holding in SCSC, the insurer on the risk at the time of that occurrence would bear liability for all of the resulting damages,