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The "Great Fire" Did It

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Since the advent of property hazard insurance, courts have struggled to address real-world implications of poorly drafted policies. Such was the case in San Francisco over a hundred years ago. December 2010 marked the centennial of the landmark California Supreme Court decision that resolved the critical insurance coverage dispute arising from the 1906 San Francisco earthquake and fire. The earthquake and ensuing fires laid waste to the city, destroying 28,000 buildings and causing the nation's largest casualty loss before 9/11, Hurricane Katrina, and likely the Deepwater Horizon disaster.[1] Immediately after the fires were extinguished, the city's Real Estate Board convened to pass a remarkable resolution that "the calamity should be spoken of as 'the great fire' and not as 'the great earthquake.'"[2] Why? Many property insurance policies issued to San Franciscans covered fires but contained exclusions for losses caused by earthquake.

Many policyholders were forced to sue property insurers that invoked earthquake exclusions to deny coverage. While most courts sided with the policyholders, the insurance companies prevailed in a few early cases by arguing that the proximate cause of the losses was the quake and not the fires that ravaged the city in its wake. Thankfully for the City of San Francisco, the leading cases of the day established the now nearly universal rule of "concurrent causation" or "efficient proximate causation": when excluded causes (earthquake, flood) combine with covered causes (fire, hurricane) to cause a loss, the insured is entitled to coverage.

The case that best illustrates these early policyholder victories was filed by the California Wine Association,[3] which lost millions of gallons of wine that it had stored in warehouses throughout San Francisco. After fire consumed the warehouses, the Wine Association tendered to its insurers millions of dollars of claims for damage to buildings and loss of inventory. One of these insurers, Commercial Union Fire Insurance Company of New York, denied coverage, invoking the exclusion in its policy for "loss caused directly or indirectly by earthquake."

Alfred Sutro of Pillsbury, Madison & Sutro (now Pillsbury Winthrop Shaw Pittman) filed suit on behalf of the Wine Association against Commercial Union in San Francisco Superior Court. The case was tried to a jury. The insurer's attorneys argued that the fire in question was caused by the quake and "continuously and uninterruptedly" reached and destroyed the plaintiff's property. In response, Sutro obtained the court's approval to ask the jury to answer specific questions in the form of special verdicts which addressed separate factual premises of the insurer's argument. One asked whether any of the fires that followed the earthquake were "not caused directly or indirectly by the earthquake." Two others asked whether it was one of these latter fires that reached and destroyed the Wine Association's warehouses.

The jury answered these questions in favor of the Wine Association, establishing that the losses resulted from fires that were started by intervening causes. (Hours after the quake struck, for example, someone making breakfast on a stove sent sparks through a cracked chimney and launched what is known to posterity as the "Ham and Eggs Fire.") The insurer appealed, but without satisfaction. The California Supreme Court held that the jury's factual finding mooted the only potential legal issue in the case, namely, whether the fire itself had been caused by the earthquake or had an independent origin.

Advent of the "ACC" Clause

California's Rejection of ACC

Following the decision of *California Wine Association*, the California legislature amended the state's insurance code to provide that property insurers would in the future be required to cover fire damage ensuing from earthquakes regardless of whether the fires are "caused" by the earthquakes or merely "follow" them and result from an intervening cause.[4] Outside the earthquake context, however, the "concurrent causation" or "proximate causation" issue has continued to dominate almost every dispute over insurance coverage for man-made or natural disasters. For the last century, California has remained on the cutting edge of this issue.

In the 1970s and 80s, the California Supreme Court issued a series of decisions making the state the most pro-policyholder jurisdiction in the country on the concurrent causation question. One example is *State Farm Mutual Auto Insurance Company v. Partridge.*[5] The insured and two friends were shooting rabbits from his automobile with a "hair trigger" pistol when the car hit a bump and the gun discharged, hitting one of the passengers. She sued the insured for her injuries and he tendered the claim to his homeowner's insurer. The policy covered injuries caused by negligence but excluded injuries arising out of the use of an automobile, and the insurer denied coverage on that basis. The California Supreme Court held that there was coverage because the insured's "use" of the car was not the sole cause of the injuries, but was only one of two joint causes of the accident: the other contributing cause – the fact that the insured had recklessly modified his gun to put it on a hair trigger – was covered.

Similarly, in *Garvey v. State Farm Fire & Casualty Company*,[6] the California Supreme Court held that the mere fact that an excluded risk had contributed to a loss would not preclude coverage. The *Garvey* Court ruled that subsidence damage to the insured's house would be covered, notwithstanding the policy's express exclusion for "earth movement," if the predominant or "efficient proximate" cause of the damage was the covered negligence of the contractor who had designed and built the house.

The Anti-Concurrent Causation Clause

Following these and other pro-policyholder decisions in California and a few other states, insurers responded by attempting to contract around the "concurrent" or "efficient proximate" causation rules. The new fight was over enforcement of anti-concurrent causation (ACC) clauses that are now found in the exclusions section of almost all standard property forms. Those clauses say, in essence, that if damage is caused even partly by a concurrent excluded cause (such as flood, earthquake, or earth movement), then there is no coverage even if a covered cause (wind, fire, or third-party negligence) contributes to the loss.[7] In response, California again sided with policyholders by holding that ACC clauses were unenforceable as a matter of public policy. For example, in *Howell v. State Farm Fire & Casualty Company*,[8] the Court of Appeal reversed a summary judgment in favor of the insurer and held that under Insurance Code section 530, an insurer is liable for all loss proximately caused by a covered peril regardless of any exclusionary language used in the policy, including an ACC clause.

Even California, however, has its limitations. In *Julian v. Hartford Underwriters Insurance Company*,[9] the California Supreme Court held that where the insuring clause of a policy provided that weather conditions would be covered unless they "contribute[d] in any way with" excluded causes of loss including earth movement, there was no coverage for a landslide caused by rain. The Court reasoned that because the policy's anti-concurrent causation language was located in its insuring clause, rather than in its exclusions section, the rain that caused the landslide was not a covered cause of loss; hence, the efficient proximate cause doctrine did not apply. In other words, *Julian* held that insurers could contract around the doctrine after all, by inserting anti-concurrent causation provisions into the insuring clauses of their policies rather than into the exclusions sections.

The Majority Rule and Newer Approach

Outside California, ACC clauses have been enforced in a majority of states.[10] However, recently, as states have faced their own versions of "the great fire," some courts have started to shrink from "all or nothing" results, and have been finding new ways to secure coverage for policyholders faced with major disasters.

In *Corban v. United Services Auto Association*,[11] Mississippi took a new approach when it found coverage for property damage resulting from Hurricane Katrina – the largest hurricane ever to hit the United States and the largest natural disaster since the 1906 San Francisco earthquake and fire. As in scores of other cases in which courts had held that ACC clauses precluded coverage for hurricane losses, the policy at issue in *Corban* covered windstorm loss but excluded flooding. The insurer took the position that the ACC clause precluded all coverage for property damage resulting from Katrina's storm surge because flooding that occurred in the storm's wake contributed to the loss. While agreeing that the storm surge was an excluded "water loss," the court disagreed with the insurer on the application of the ACC clause. The court held that the ACC clause only applies when two perils converged at the same point in time, contemporaneously and operating in conjunction: only then would there be a truly "concurrent" cause or event.[12] In the absence of true "concurrence," the insured was entitled to coverage to the extent that damage had been caused by wind, regardless of whether excluded flooding later contributed to or exacerbated the damage. The court explained that:

> [A] finder of fact must determine what losses, if any, were caused by wind, and what losses, if any, were caused by flood. If the property suffered damage from wind, and separately was damaged by flood, the insured is entitled to be compensated for those losses caused by wind. Any loss caused by "[flood] damage" is excluded. If the property first suffers damage from wind, resulting in a loss, whether additional "[flood] damage" occurs is of no consequence, as the insured has suffered a compensable wind-damage loss. Conversely, if the property first suffers damage from flood, resulting in a loss, and then wind damage occurs, the insured can only recover for losses attributable to wind.[13]

Under *Corban*, if the insurer can prove that the damage was increased by some amount by an excluded cause, then it may be entitled to allocation of the loss between covered and excluded losses. To the extent the policyholder can prove that the damage was caused by a covered cause of loss, it will be entitled to coverage even if the damage was exacerbated by an excluded cause.

Other post-Katrina opinions have reached similar conclusions, holding the ACC inapplicable where covered and excluded causes act separate and are not truly "concurrent" causes of the loss.[14] Time will tell how influential *Corban* will be, but it seems likely that its approach will find sympathy in jurisdictions that are less policyholder-friendly than

California but nevertheless adopt a "plain meaning" approach to the interpretation of insurance policies, given that it is based squarely on the wording of the ACC clause. *Corban's* equitable approach should also appeal to courts interested in avoiding the result of coverage being precluded because an excluded cause makes a *de minimus* contribution to the loss.

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[1] The estimated damage was roughly $500 million. It is equivalent to roughly $10 billion in 2010 dollars—once the country's greatest casualty loss in constant dollar terms. This estimate was about the same as the entire United States federal budget or 1.8 percent of the gross domestic product in 1906. MUNICH RE, THE 1906 EARTHQUAKE AND HURRICANE KATRINA 3 (2006); Kerry A. Odell & Marc D. Weidenmier, *Real Shock, Monetary Aftershock: The 1906 San Francisco Earthquake and the Panic of 1907*, 64 J. ECON. HIST. 1002, 1003 (2004).

[2] *Big Structures Now Planned Preparations to Rebuild San Francisco on Lines Recommended by Burnham*, S.F. CHRONICLE, April 25, 1906, *available at* http://www.sfmuseum.org/1906.2/burnham.html.

[3] *California Wine Association v. Commercial Union Fire Insurance Co. of New York*, 159 Cal. 49 (1910).

[4] Cal. Ins. Code § 2081 ("Nothing in this section exempts an insurer from, or permits an insurer to limit, its liability or obligation under a fire insurance policy to cover the losses from a fire that is caused by, or follows, an earthquake.").

[5] 10 Cal. 3d 94 (1973).

[6] 48 Cal. 3d 395 (1989).

[7] A typical Insurance Services Office Inc. (ISO) form will read: "We will not pay for loss or damage caused directly or indirectly by any of the following [including earth movement, water, fungus, rot or bacteria]. Such loss or damage is excluded regardless of any other cause or event that contributes concurrently or in any sequence to the loss."

[8] 218 Cal. App. 3d 1446 (1990).

[9] 35 Cal. 4th 747 (2005).

[10] *See, e.g.*, *Thompson v. State Farm Fire & Casualty Co.,* 165 P.3d 900 (Colo. App. 2007) (insureds' loss was not covered because the presence of the ACC clause assured that any water damage loss caused by "water below the surface of the ground" was excluded from coverage, regardless of the cause or origin of the subsurface water itself); *T.H.E. Insurance Co. v. Charles Boyer Children's Trust*, 455 F. Supp. 2d 284 (M.D. Pa. 2006) (applying Pennsylvania law) (the fact that a covered peril might have contributed to the loss was irrelevant in light of the clear language of the ACC clause); *Arctic Slope Regional Corp. v. Affiliated FM Insurance Co.*, 564 F.3d 707 (5th Cir. 2009).

[11] 20 So. 3d 601 (Miss. 2009).

[12] *Id.* at 615.

[13] *Id.* at 617.

[14] For example, *Dickinson v. Nationwide Mutual Fire Insurance Co.*, Case No. 1:06CV198 LTS-RHW, 2008 BL 87575 (S.D. Miss. Apr. 25, 2008) (applying Mississippi law), the court found that the ACC clause did not apply because the covered wind and excluded water acted separately, and not concurrent, causes of the disputed loss; *accord Maxus Realty Trust, Inc. v. RSUI Indemnity Co.*, Case No. 06-0750-CV-W-ODS, 2008 BL 104206 (W.D. Mo. May 16, 2008).