From Katrina to Sandy: Lessons from the whirlwind

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It has been five months since Superstorm Sandy battered the East Coast of the United States. With several hundred thousand residents still without homes, and many businesses still operating out of temporary facilities, it is too early to tell precisely what insurance coverage issues will arise, what positions insurers will take and where the battle lines will be drawn in the inevitable coverage litigation that will make its way through the New York and New Jersey courts over the next several years.

But this is not the first time an enormous windstorm and rainstorm has combined with storm surges to cause catastrophic losses across an entire region of the country. Seven and a half years ago, Hurricane Katrina made landfall along the central Gulf Coast, causing widespread devastation across parts of Louisiana, Mississippi and Alabama. Like Superstorm Sandy, damage from Hurricane Katrina was caused by high winds, heavy rainfall and storm surges, often in sequence.

Katrina resulted in several years of insurance coverage litigation, setting the stage for what we can expect to follow from Sandy. Recognizing that what is past is prologue, this commentary reviews key procedural and substantive issues that arose after Hurricane Katrina. Reviewing this litigation history with the benefit of hindsight helps us to better understand the road ahead as policyholders with Sandy-related losses begin the difficult task of obtaining the full benefit of the insurance coverage they purchased.

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Like Superstorm Sandy, damage from Hurricane Katrina was caused by high winds, heavy rainfall and storm surges, often in sequence. Damage from Sandy in Ortley Beach, N.J. (L), and Katrina in Venice, La. (R), is shown here.

REUTERS/Lee Celano

One issue should be highlighted at the outset. As with Hurricane Katrina, it is difficult in the aftermath of Superstorm Sandy to determine which damage resulted from which cause (*i.e.*, wind, rain or storm surges). After Katrina, many insurers capitalized on this uncertainty, denying claims in cases in which it appeared damage resulted from an excluded cause unless the policyholder could demonstrate otherwise.

Developments in the law after Katrina show that the insurers' claims-handling approach was backward. If there is a loss, the insurer is not permitted to deny the claim unless it can demonstrate that the damage resulted from an excluded cause. We discuss this and other important lessons learned in greater detail below.

COMPARING THE DAMAGE FROM KATRINA AND SANDY

Hurricane Katrina reached the Gulf Coast Aug. 29, 2005, as a category 3 hurricane with wind speeds of 125 miles per hour.[1] In New Orleans, winds gusted to over 100 mph.[2] Rainfall from Katrina for the first several hours exceeded rates of 1 inch per hour, and total rainfall accumulation exceeded 10 inches along much of the hurricane's path.[3] Storm surges driven by heavy winds reached 19 feet in eastern New Orleans, 22 feet along the eastern half of the Mississippi coast and as high as 28 feet on the Mississippi coast just east of St. Louis Bay.[4] In New Orleans, the effects of the storm surge were compounded when a number of floodwalls and levees were breached.[5] In Mississippi, the storm surges penetrated more than 6 miles inland.[6]

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By comparison, although Superstorm Sandy covered a much larger area than Katrina, it was less intense. Sandy made landfall as a post-tropical cyclone rather than a hurricane, although wind gusts in some areas reached 90 mph.[7] Rainfall from Sandy totaled over 12 inches in parts of Maryland and over 11 inches in parts of New Jersey.[8] Like Katrina, Sandy's winds caused storm surges, including a surge of nearly 14 feet in Lower Manhattan and a storm surge of over 13 feet in Sandy Hook, N.J.[9]

Hurricane Katrina was the costliest storm in U.S. history. Total damages caused by Katrina have been estimated to be $108 billion, with total insured losses of $41.1 billion.[10] Another $25.8 billion in losses were paid from the National Flood Insurance Program, which is administered by the Federal Emergency Management Agency, leaving $41 billion in uninsured losses.[11]

Katrina resulted in more than 1.7 million claims.[12] Of those, 1.2 million were for personal property, 346,200 were for damaged vehicles and 156,600 were commercial claims.[13] Although the commercial losses accounted for less than 10 percent of the claims, they accounted for about half of the $41.1 billion in claims payments.[14] Of the 1.2 million homes damaged by Katrina, 275,000 were destroyed.[15]

Although it is too soon to determine the total cost of Superstorm Sandy, it is estimated to be the second costliest storm in U.S. history. Indeed, it has been reported that as many as 305,000 homes were destroyed by Sandy in New York alone, more than the total number of homes destroyed by Katrina.[16]

Total damage has been estimated at $62 billion,[17] and insured losses have been estimated to be between $20 billion and $25 billion.[18] The nearly $47 billion disparity between estimated damage and estimated "insured loss," both of which are generated by insurance industry sources, is ominous. The insurance industry already assumes that a very large portion of Sandy-related losses fall outside the coverage policyholders purchased. Policyholders should not blindly accept this assumption.

INSURANCE COVERAGE ISSUES

Procedural issues

Policyholders with disputed claims will first confront the issue of when and where to sue. First-party property damage and business interruption policies typically contain provisions requiring that any lawsuit must be filed within one year after the loss. After Katrina, the Louisiana Legislature extended the time to file suit until two years and a day after the hurricane.[19] Notwithstanding, policyholders rushed to the courthouse in advance of the one-year anniversary of Katrina. This created an enormous backlog of cases in the Louisiana and Mississippi courts and caused substantial delay.

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To add to the delay, many policyholders who filed in state court were met with insurers' procedural maneuvers. In particular, in cases in which any arguable basis for federal jurisdiction existed, such as diversity of citizenship — where the plaintiff and defendants are citizens of different states — insurers typically removed cases to federal court.

To counter this, Katrina plaintiffs often amended their complaints to include claims against a local broker.[20] Frequently, they argued that the broker either gave assurances that the coverage being purchased would cover hurricane damage (whether or not it was caused by flooding) or failed to properly advise the policyholder to purchase flood insurance. By adding a local defendant, diversity was destroyed and the case could remain in state court.

In Louisiana, however, claims against insurance brokers were subject to a one-year limitations period that, the brokers argued, began to run on the date the policy was first issued. Accordingly, many courts ruled that the broker claims were time-barred, and the federal courts therefore maintained diversity jurisdiction.[21]

Policyholders with Sandy-related claims can learn from the procedural battles that played out after Katrina. First, to avoid getting bogged down in the inevitable Sandy litigation rush, policyholders who expect they will have to litigate can file their claims early. This may be difficult for practical purposes, since policyholders will want as much time as possible to negotiate with insurers, investigate the legal and factual bases for their claims, and quantify their damages. However, filing even a few weeks ahead of the end of the suit limitations period may substantially affect the speed at which the case proceeds.

In addition, those policyholders who want to litigate their claims in state court should carefully consider whether an arguable basis for federal jurisdiction exists and, if so, whether the case can be structured to avoid it. One difference between Katrina and Sandy is that many insurers arguably are citizens of New York and New Jersey, and therefore diversity jurisdiction will not exist.[22] In cases in which policyholders and insurers are citizens of different states, policyholders should carefully consider whether they have cognizable claims against their local brokers. If so, policyholders should immediately determine the applicable statute of limitations and be sure to file suit in a timely manner.

There is, however, a countervailing consideration here, and policyholders should be careful not to allow procedural maneuvering to become the "tail that wags the dog." There may be strategic reasons not to assert claims against the insurer and broker simultaneously. For example, the policyholder may not want to be in the position of arguing that the policy provides coverage for damage caused by flooding while at the same time arguing that the broker was negligent for failing to advise the policyholder to purchase flood insurance. In such circumstances, it is often advisable to enter into a tolling agreement with the broker while pursuing the claim against the insurer.

Coverage issues

By way of background, there are two species of first-party property damage policies: "named peril" and "all risk." Named-peril policies cover losses only from specifically enumerated causes, whereas all-risk policies cover losses from all causes except for those that are excluded (*i.e.*, excluded perils).

Under either type of policy, the policyholder bears the burden of proving that the loss arose from a covered peril (or, in the case of

all-risk coverage, simply that a loss occurred), and the insurer bears the burden of proving that an exclusion applies.

After Katrina, many policyholders were surprised to learn that even though they had coverage for "windstorms" — either because windstorms were a specifically enumerated named peril or because they were not excluded from their all-risk coverage — insurers nevertheless denied their claims because they did not have coverage for water damage. This seemed counterintuitive to most policyholders given that the massive storm surges and devastating flooding all resulted from a hurricane.[23]

Not surprisingly, the central battles after Katrina related to coverage for damage caused by water.

Flood exclusions

First, policyholders argued that so-called "flood exclusions" (which typically exclude "water damage" from various sources) were ambiguous under the circumstances and did not apply to water damage resulting from negligence. Specifically, policyholders had argued in the wake of Katrina that the ruptured levee was caused by inadequate design, construction and maintenance.[24] Although this argument prevailed in the lower federal court, the 5th U.S. Circuit Court of Appeals reversed, finding that flood exclusions were unambiguous and flooding caused by the failure of levees fell within the exclusion.[25]

The case law addressing this issue after Katrina involved standard-form language in homeowner policies. It is unlikely that New York and New Jersey courts will reach a contrary result and find that the same standard-form water exclusions do not apply to damage caused by storm surges, even if there may also have been some intervening cause, such as negligent design of flood walls.

However, policyholders should keep in mind that the specific policy language will control. In particular, commercial policyholders often purchase first-party property policies with manuscripted or non-standard language. Thus, post-Katrina case law may involve different policy language, and policyholders with Sandy-related claims should review their policies closely before assuming that all flood damage, whether caused by negligence or storm surges, necessarily is excluded.

Concurrent causation

Even if water damage, standing alone, may be excluded, in most instances Sandy policyholders, like Katrina policyholders, suffered damage resulting from both wind and water. This raises the issue of whether there is coverage when damage is caused by one peril that is covered (windstorm) and another peril that is excluded (flood).

Insurers had encountered analogous issues long before Katrina. In many states, courts applied the concurrent causation doctrine, holding that in cases in which damage resulted from concurrent causes, one covered and the other not, the damage would be covered so long as the covered cause is the "dominant and efficient proximate cause" of the damage.[26]

In an attempt to avoid application of this rule, insurers began including so-called "anti-concurrent cause" provisions in their policies. Such clauses typically appear in the introductory language to the policy exclusions and state: "We do not cover loss to any property resulting directly or indirectly from any of the following. Such a loss is excluded even if another peril or event contributed concurrently or in any sequence to cause the loss."[27]

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In a case involving a combination of wind and water damage — a storm surge pushed ashore by Hurricane Katrina's winds — a federal district court held that the anti-concurrent-cause provision was ambiguous and allowed coverage for "that portion of the loss which [the policyholder] can prove to have been caused by wind."[28] In that case, the parties appeared to agree that the relevant loss was damage from a storm surge, and that wind and water therefore acted together (*i.e.*, concurrently) to cause the loss. The 5th Circuit, however, overruled the court, finding that the clause unambiguously excludes coverage for water damage even if wind contributed to cause the same loss.[29]

More recently, however, the Mississippi Supreme Court in *Corban v. USAA* clarified the meaning of the anti-concurrent-cause provision under circumstances in which the policyholder alleged that wind and water acted separately to cause different damage resulting in separate losses.[30] Under such circumstances, the court found that the term "in any sequence" was ambiguous and could not be read to divest the policyholder of coverage for a loss that resulted from a covered peril (*i.e.*, wind).[31]

Corban is significant in two respects. First, before *Corban*, insurers adjusting Katrina claims took the position that they only needed to show that water damage contributed to the loss. If so, then the insurers, relying on the "in any sequence" language in the anti-concurrent-cause provision, arguably could deny coverage for the entire loss, even if wind damage caused some portion of the loss.

As an illustration, before *Corban*, if hurricane wind destroyed half of a policyholder's home, and a storm surge subsequently destroyed the remainder of the home, the insurers would contend that the anti-concurrent-cause provision applied to exclude coverage for the entire loss. However, after *Corban*, the anti-concurrent-cause provision could not be read to exclude coverage for the damage to the home caused by wind, even if the storm surge would have destroyed the entire home if the wind damage had never occurred.

Second, the *Corban* decision clarified how the burden of proof operates when multiple causes contribute to the loss. Under an all-risk policy, the insured bears the initial burden to prove that the loss occurred, and the burden then shifts to the insurer to prove that an exclusion applies.[32] Thus, under circumstances such as a hurricane loss, when some damage may have been caused by wind and other damage may have been caused by water, the insurer bears the burden of proving the extent of the loss that was caused by water, or that water and wind acted together to cause the same damage.[33]

The importance of this allocation of the burden of proof cannot be overstated. The Mississippi Supreme Court's decision in *Corban* was issued in October 2009, more than four years after Hurricane Katrina. During the intervening four years, insurance

adjusters applied the so-called "wind/water protocol," under which a claim related to a storm surge would be denied unless there was physical evidence of wind damage.[34] Under *Corban*, however, the so-called wind/water protocol is exactly backward. Particularly under an all-risk policy, if there is a loss, the claim must be covered unless the insurer can demonstrate that the damage was caused by an excluded peril.

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Although *Corban* may have come too late for many policyholders with Katrina claims, it provides persuasive authority for policyholders with Sandy-related claims. Although Mississippi law obviously will not be applicable to Sandy-related claims, *Corban* is the most recent case from a state supreme court addressing the precise issue that many policyholders with Sandy-related claims will face.

CONCLUSION

Policyholders with Superstorm Sandy claims should take heed of the lessons learned from the years of claims-handling practices and insurance coverage litigation following Hurricane Katrina. First, where practicable, Sandy claimants who anticipate litigation should take steps to avoid delays that will otherwise result as other policyholders rush to the courthouse before suit limitation periods expire. Policyholders should explore whether alternative forums are available and whether there is any downside to filing their claim early.

To the extent policyholders want to file their claims in state court, they should determine whether there is a basis for federal jurisdiction that would permit the insurers to remove the case to federal court. If so, then policyholders should determine whether the claim can be structured to avoid the basis for federal jurisdiction or, if filing in state court would be futile, consider filing in federal court to avoid the delay associated with removal.

With respect to coverage issues, policyholders who have suffered water-related damage should not automatically assume the resulting loss is not covered. Policyholders must carefully review the language in their policies to determine whether there is an arguable basis for coverage, either because the water exclusion in the policy is ambiguous under the particular circumstances or because all or some portion of the loss may also have been caused by wind.

Armed with the holding of *Corban v. USAA*, policyholders who suffered damage from both wind and water should remember that it is the insurer's burden to prove an exclusion by showing that a loss is attributable solely to an excluded cause. Absent such a showing, policyholders should insist that their insurers pay every dollar of loss for which they are entitled to coverage under their policies. WJ

NOTES

[1] Nat'l Oceanic & Atmospheric Admin., Special Report: Hurricane Katrina (Dec. 29, 2005), *available at* http://www.ncdc.noaa.gov/special-reports/katrina.html.

[2] *Id.*

[3] *Id.*

[4] Richard D. Knabb, Jamie R. Rhome & Daniel P. Brown, Tropical Cyclone Report: Hurricane Katrina 9 (2011), *available at* http://www.nhc.noaa.gov/pdf/TCR-AL122005_Katrina.pdf (lasted visited Jan. 7, 2013).

[5] *Id.*

[6] *Id.*

[7] Grace Muller, *The Stats Are In: Superstorm Sandy Totals,* AccuWeather.com (Nov. 1, 2012), *available at* http://www.accuweather.com/en/weather-news/sandy-statistics-rain-wind-snow/876665; NASA, Hurricane Sandy (Atlantic Ocean): Comparing the Winds of Sandy and Katrina (Nov. 9, 2012), *available at* http://www.nasa.gov/mission_pages/hurricanes/archives/2012/h2012_Sandy_prt.htm; New Jersey Exec. Order No. 107 (Nov. 2, 2012), *available at* http://nj.gov/infobank/circular/eocc107.pdf.

[8] *See* The Stats Are In, *supra* note 7.

[9] Ins. Info. Inst., Hurricane Katrina: The Five Year Anniversary (July 2012).

[10] *See* Knabb, *supra* note 4, at 12-13.

[11] *Id.*

[12] *See* Ins. Info. Inst., *supra* note 9, at 3.

[13] *Id.*

[14] *Id.*

[15] La. Recovery Auth., Overview of Comparative Damage from Hurricane Katrina 2 (Dec. 9, 2005), *available at* http://www.cbr.tulane.edu/PDFs/LRA_Katrina.pdf.

[16] Hilary Russ, *New York, New Jersey Put $71B Price Tag on Sandy,* Property Casualty 360 (Nov. 27, 2012), *available at* http://www.propertycasualty360.com/2012/11/27/new-york-new-jersey-put-71b-price-tag-on-sandy.

[17] *What We Know About Superstorm Sandy a Month Later,* Ins. J. (Dec. 4, 2012), *available at* http://www.insurancejournal.com/news/east/2012/12/04/272698.htm.

[18] Chad Hemenway, *RMS: Sandy Insured Losses Could Reach $25B,* Property Casualty 360 (Nov. 26, 2012), *available at* http://www.propertycasualty360.com/2012/11/26/rms-sandy-insured-losses-could-reach-25b.

[19] La. Rev. Stat. Ann. § 22:1894 (2012).

[20] Frequently, they argued that the broker either gave assurances that the coverage being purchased would cover hurricane damage (whether or not it was caused by flooding) or failed to properly advise the policyholder to purchase flood insurance. *See Bates v. Allstate Ins. Co.,* No. 06-10566, 2007 WL 2029489 (E.D. La. July 11, 2007).

[21] *Id.*

[22] In cases involving liability coverage, insurers often claim to be citizens of New York in an effort to take advantage of what they perceive to be more favorable law. Policyholders who want to litigate their Sandy claims in New York will have little difficulty locating court filings in which the insurer they are suing has argued that it is a New York resident.

[23] According to the National Hurricane Center, a hurricane is a tropical cyclone with maximum sustained winds of 74 miles per hour or higher. *See* http://www.nhc.noaa.gov/climo/.

[24] *In re Katrina Canal Breaches Litig.,* 495 F.3d 191, 196 (5th Cir. 2007).

[25] *Id.*

[26] 7 Lee R. Russ & Thomas F. Segalla, Couch on Ins. § 101:55 (3d ed. 2007).

[27] *See ,e.g., Leonard v. Nationwide Mut. Ins. Co.,* 499 F.3d 419, 430 (5th Cir. 2007).

[28] *Leonard v. Nationwide Mut. Ins. Co.,* 438 F. Supp. 2d 684, 695 (S.D. Miss. 2006).

[29] *Leonard,* 499 F.3d at 430.

[30] *Corban v. USAA,* 20 So. 3d 601, 614-15 (Miss. 2009).

[31] *Id.* at 615-16. ("The policy establishes a duty to indemnify for covered 'direct physical losses.' ... The ACC clause applies only if and when covered and excluded perils contemporaneously converge, operating in conjunction, to cause damage resulting in loss to the insured property. If the insured property is separately damaged by a covered or excluded peril, the ACC clause is inapplicable.").

[32] *See* Russ & Segalla, *supra* note 26, at § 101:7.

[33] *Corban*, 20 So. 3d at 619.

[34] *See* William F. "Chip" Merlin Jr., *Corban v. USAA: A Case Providing Far Too Little Because It Was Rendered Far Too Late,* 79 Miss. L.J. Supra 129 (2009), *available at* http://mississippilawjournal.org/wp-content/uploads/2012/04/Supra-79-Essay-Merlin.pdf.