No. 48045-0-II

COURT OF APPEALS OF THE STATE OF WASHINGTON

DIVISION II

LORETTA LESURE,

Appellant;

v.

FARMERS INSURANCE COMPANY OF WASHINGTON,

Respondent.

BRIEF OF RESPONDENT FARMERS INSURANCE COMPANY OF WASHINGTON

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I. INTRODUCTION

This appeal arises from the Superior Court's dismissal on summary judgment of a claim by Loretta Lesure that she is entitled to additional benefits under her Farmers Insurance Company of Washington, (hereinafter "Farmers"), homeowner's policy. CP 009-010.

Specifically, this appeal involves Ms. Lesure's claim for additional benefits under her policy following a fire loss to her residence. Ms. Lesure claims that she is entitled to payments beyond the amount necessary to repair the residence to its pre-fire condition. Ms. Lesure also claims that Farmers should pay additional costs to comply with building code requirements in an amount which exceeds the policy limit for Building Ordinance or Law coverage.

Ms. Lesure fails to provide any legal authority from this or any other jurisdiction supporting the argument that she is entitled to more than the repair costs for the "equivalent construction" of the residence. She also fails to provide any legal authority in support of her claim that the Policy's Building Ordinance or Law coverage limit is somehow unenforceable.

To the contrary, this ***exact*** issue has been ruled upon by the Washington Courts. In *Allemand v. State Farm Ins. Co.*, 160 Wn. App. 365, 248 P.3d 111 (2011), Division III of this Court specifically held that

the limitation set forth under the exact same building code coverage as it at issue in this matter, was valid and enforceable.1

Moreover, contrary to Ms. Lesure's argument that this issue is somehow unsettled in Washington law, the *Allemand* Court's analysis included a discussion of Washington caselaw dating to 1923 on the issue of a policy's limitation on building code coverage. *Id.* The *Allemand* Court's introduction to the opinion is particularly applicable.

> This case revisits the recurring problem of fire-loss house repairs that must account for changes in building codes since the house was originally constructed, an issue that stretches back across Washington law for nine decades. We conclude that the limitation on losses resulting from building code upgrades in this homeowners policy was effective under long-standing precedent. . .

Allemand, 160 Wn. App. at 365, 366-367, 248 P.3d 111.

The legal issue in this case is well-settled. Farmers paid Ms. Lesure's claim in accordance with the exact terms and conditions of the subject policy and Washington law.

As a result, the Court should conclude that Ms. Lesure is not entitled to any further benefits under the subject policy. The Superior Court should therefore be affirmed.

II. ASSIGNMENTS OF ERROR

1 Farmers objects to Ms. Lesure's footnote indicating what she apparently believes to have been the subsequent procedural history of Allemand following the Court of Appeals decision. That information is not in the record and is based on pure speculation.

A. Assignments of Error

Farmers assigns no error to the rulings of the trial court.

B. Issues Related to Appellants' Assignments of Error

1. The Superior Court correctly applied long-standing Washington law to the undisputed facts of this case and the specific terms and conditions of the Lesure Policy to conclude that no further benefits were due for the subject loss, based on the following:

   a. Farmers' payment of $21,748.25 is undisputedly the amount necessary to repair the damage caused by the fire with "equivalent construction";

   b. Farmers payment of $11,200.00, representing 10% of the Lesure Policy's Dwelling limit, was the full amount that Plaintiff was entitled to recover under the Building and Ordinance Endorsement to her policy.

2. The Superior Court correctly concluded that the terms of the Lesure Policy are not ambiguous under Washington law.

3. The Superior Court correctly concluded that the efficient proximate cause rule is inapplicable and does not alter the

specific terms of the policy, including the limit available for code upgrades.

III. STATEMENT OF THE CASE

A. Background

On or about January 4, 2014, a fire started in a shed located several feet from Ms. Lesure's residence. CP 057-062. The fire spread to the residence, causing partial damage. The residence was not a total loss. See CP 77-96.

The cause of the fire is not disputed. A Port Angeles Fire Department investigation concluded that the fire started while Ms. Lesure's son was extracting THC oils from marijuana plants in the shed. CP 057.

Ms. Lesure tendered a claim to Farmers later that same day and arrangements were made for Farmers to examine the scene. CP 064.

B. Ms. Lesure's Claim and Farmers' Response Thereto

Farmers issued Washington Special Form Homeowners Policy 90923-16-10 to Ms. Lesure with a policy period of January 24, 2013 through January 24, 2014. CP 118-163. CP 119. This policy provides coverage pursuant to its terms and conditions and not otherwise.

The policy issued to Ms. Lesure provides coverage for direct physical loss.

> **Perils Insured Against**
>
> . . .
>
> We insure for accidental ***direct physical loss to property*** described in Coverage A and B, subject to the exclusions and limitations described elsewhere in Section I of this policy, except we do not insure for loss where earth movement, water damage, or nuclear hazard occur, however caused, as further explained in this policy.

CP 127 (emphasis added).

The direct physical loss in this case is the damage caused by the fire.

On January 6, 2014, Farmers issued a reservation of rights to Ms. Lesure, which indicated that Farmers investigation was ongoing. CP 064. On January 9, 2014, Farmers hired investigator Dave Kreg to examine the scene and prepare a report on the damage. CP 067-070. As a result of the fire, the estimate for repairs to the damage of the structure totaled $22,248.25. CP 072-074. Ms. Lesure has never contested this amount as being the amount necessary to repair the damage caused by the fire. She has also never presented her own competing scope of repair or estimate.

Accordingly, on January 27, 2014, Farmers sent Ms. Lesure a letter explaining the loss settlement amount, including an explanation of the actual cash value of the repairs:

> "Actual cash value is an amount less than the full replacement cost of the damaged property, usually by a depreciable amount related to the useful life and condition of the property. You may be entitled to recover all or a

> portion of the depreciation shown above, under the replacement cost portion of your policy."

CP 072.

Attached to the letter was a check for $17,384.47 representing the actual cash value of the repair totals minus depreciation, along with a copy of Farmers' estimate of repairs. CP 072-095. Farmers' letter also specifically advised Ms. Lesure of the following:

> You have the option of not repairing or replacing the covered property. In that case, payment of the actual cash value amount of your claim will be considered final payment.

CP 073.

Ms. Lesure was advised, however, that she could recover the complete cost of repair of the fire damage if she actually conducted the repairs. Farmers' letter specifically advised Ms. Lesure of the following:

> Actual cash value is an amount less than the full replacement cost of the damaged property, usually by a depreciable amount related to the useful life and condition of the property. You may be entitled to recover all or a portion of the depreciation shown above, under the replacement cost portion of your policy. In order to recover the withheld depreciation, please forward a copy of the final replacement invoices, receipts, paid checks or credit card statements to the above captioned address for consideration. We will not reimburse you more than the amount you actually and reasonably spend to repair or replace the lost or damaged property.

CP 072.

With regard to loss settlement, the Policy provides as follows:

Conditions

3. *Loss Settlement.*

a. Except as stated in item b, covered loss to buildings under Coverage A and B will be settled at replacement cost without deduction for depreciation, subject to the following:

(1) Settlement under replacement cost will not be more than ***the smallest of the following***:

(a) the limit of insurance under this policy applying to the building.

(b) the replacement cost of that part of the building damaged for ***equivalent construction*** and use on the same premises.

(c) the amount actually and necessarily spent to repair or replace the building intended for the same occupancy and use.

. . .

(3) At your option, you may make a claim under this policy on an actual cash value basis for loss or damage to buildings. Within 180 days after loss you may make a claim for any additional amount on a replacement cost basis if the property has been repaired or replaced.

CP 131 (emphasis added).

On June 24, 2014, following the tender of the Actual Cash Value payment for the repair of fire damage, Ms. Lesure submitted a demand for payment of the full policy limits for the Dwelling coverage in the amount of $112,000 despite the fact that it was undisputed that the direct physical damage actually caused by the fire was limited to $22,248.25. CP 097. Ms. Lesure's demand for policy limits was based on a letter from the Port Angeles Community & Economic Development Department, which required Ms. Lesure to bring the property into compliance with City of Port Angeles Municipal Code 17.95.030. CP 101-102.

Specifically, the City Code requires a structure that does not comply with zoning and building codes to be demolished and reconstructed to-code if the damage is greater than 75% of the tax assessed value of the structure. CP 102. Ms. Lesure claimed in her demand letter that as a result of the City's position, a complete rebuild would be required, thus entitling her to the full limits under the policy. CP 101-102. Ms. Lesure's demand did not include any reports from any experts or contractors verifying any amounts claimed. CP 101-102.

In response to Ms. Lesure's demand, Farmers issued correspondence to Ms. Lesure dated July 1, 2014, reaffirming its position. CP 104. Farmers continued to investigate the claim, including consultation with coverage counsel. See CP 106. Thereafter, on August 21, 2014,

Farmers issued yet another correspondence to Ms. Lesure, this time detailing Farmers' analysis of the claim, including any potential benefits due as a result of the enforcement of the building code by the City of Port Angeles. CP 106-112. In this letter, Ms. Lesure was specifically advised of the fact that the primary coverage part specifically excluded coverage relating to the enforcement of any ordinance or law.

> **Exclusions**
> ...
> **Applying To Coverage A, B and C**
>
> We do *not* cover direct or indirect loss from:
>
> 1. Enforcement of any ordinance or law regulating construction, repair or demolition of a building or other structure, unless endorsed to this policy.

CP 129.

However, Ms. Lesure was also advised that her Policy included a Building Ordinance or Law Coverage Endorsement, which provides as follows:

> **BUILDING ORDINANCE OR LAW COVERAGE ENDORSEMENT**
>
> Under **Section I - Property, Losses Not Insured or Losses Not Covered**, the following exclusion is deleted:
>
> Enforcement of any ordinance or law regulating construction, repair or demolition of a building or oilier structure, unless endorsed on this policy.

Under **Section I -Property, Additional Coverages**, the following coverage is added:

Building Ordinance or Law Coverage

1. ***Our limit of liability for this coverage will not be more than 10% of the total limit of insurance applying to the covered property under Coverage A*** - Dwelling or Coverage B - Separate Structures, shown in the declarations or premium notice, whichever is most recent at the time of loss. This endorsement applies to all coverages whether in the policy contract or subsequently added by endorsement.

    a. If there is a covered loss and you decide not to repair or replace the damaged building, we shall pay the actual cash value not to exceed the limits of insurance that apply to the damaged portion of the building. You have the option of making a claim within 180 days after the date of the loss for any additional payment on a repair cost basis if you repair or replace the damaged building.

    b. This coverage does not increase the limit of insurance applying to the covered property under Coverage A - Dwelling or Coverage B - Separate Structures.

    ...

3. We will pay for the increased costs you incur due to the enforcement of any ordinance or law in force at the time which requires or regulates:

    a. The construction, demolition, remodeling, renovation, repair, or replacement of that part of a covered building or other structure damaged by a covered accidental direct physical loss.

    b. The demolition and reconstruction of the undamaged part of a covered building or other structure which must be totally

demolished due to damage caused by a covered accidental direct physical loss to another part of the covered building or other structure.

c. The remodeling, renovation, or replacement of the undamaged part of a covered building or other structure necessary to complete the remodeling, renovation, or replacement of that part of the covered building or other structure damaged by a covered accidental physical loss.

d. The legally required modifications to any undamaged portion of the structure which are caused by the enforcement of any building ordinance or law, zoning or land use ordinance if the law enforcement is directly caused by a covered accidental physical loss.

CP 144-145 (emphasis added).

The above extension of coverage provides the insured with additional benefits in the event that a covered loss triggers the enforcement of a regulation or ordinance requiring demolition or reconstruction of covered property. The additional benefits are owed when the insured incurs the code upgrade costs and the coverage is limited to 10% of the "Coverage A – Dwelling" Limit.

Specifically responding to Ms. Lesure's policy limits demand, Farmers advised as follows:

> As in Allemand, Ms. Lesure's insurance policy covers the cost to repair or replace that part of the building damaged for "equivalent construction and use" on the same premises. Coverage for building code compliance and upgrade is

> specifically excluded, except pursuant to the endorsement covering code upgrades. That endorsement provides that the coverage is limited to 10% of the Dwelling limit. Accordingly, Ms. Lesure's policy provides coverage for the estimated costs of repair, plus the building code limit. The policy terms simply do not provide for payment of the Coverage A - Dwelling policy limit under the facts and circumstances of this matter."

CP 111.

It is undisputed that as of the date of Farmers' August 15, 2014 letter, Ms. Lesure had not actually incurred any actual repair costs or any costs associated with code compliance. Regardless, in its letter of that date, Farmers tendered the replacement cost holdback and the code upgrade limit. Farmers letter stated the following:

> It is our understanding that Farmers has already paid Ms. Lesure the actual cash value of the estimated repairs. It is also our understanding that check has not been negotiated, and Farmers recently stopped payment as the check has expired. Although replacement cost coverage is not due and owing until replacement has occurred, as a gesture of good faith, Farmers has decided to pay Ms. Lesure the full replacement cost of the estimated repairs, and the maximum available code upgrade coverage. Enclosed herein are payments in full of Ms. Lesure's claim under Coverage A – Dwelling: $17,384.47 representing actual cash value, $4,363.78 representing withheld depreciation, and $11,200 representing the code upgrade coverage limit.

CP 111-112

Under Washington law, an insurer is not obligated to pay replacement costs under a property policy unless those costs are actually

incurred by the insured in the repair of the subject property. See *Hess v. N. Pac. Ins. Co.,* 122 Wn.2d 180, 188, 859 P.2d 586 (1993), *Dombrosky*, 84 Wn. App. 245, 928 P.2d 1127; See discussion below. The Washington Courts have specifically addressed this issue based on the same policy language at issue in this case. *Id.*

Regardless, the payments tendered by Farmers were issued as a matter of good faith and fair dealing, despite the fact that the depreciation and code upgrade coverage were not owed until replacement had occurred and the expenses were actually incurred by Ms. Lesure. It is Farmers' understanding that Ms. Lesure has not initiated any repairs on the structure.

Despite receiving all benefits owed under the terms of the policy, Plaintiff initiated this lawsuit on October 31, 2014. CP 199-201.

B. Ms. Lesure's Lawsuit

Despite Farmers issuing the above-discussed good faith payments, Ms. Lesure filed this lawsuit on October 31, 2014. CP 197-201. In her Complaint, Ms. Lesure alleges that she is entitled to the policy limits for Coverage - A Dwelling of $112,000 and code upgrade coverage of $11,200, for a total of $123,200. CP 200.

At the time of the filing of the Complaint, several other elements of Ms. Lesure's claim were also unresolved, including her claims under

Coverage B – Separate Structures, Coverage C – Personal Property, Coverage D – Loss of Use, as well as potential benefits under the "Additional Coverages" section of her policy, including the following:

a. Debris Removal;
b. Necessary Repairs;
c. Trees, Shrubs, Plants and Lawns;
d. Fire Department Service Charge;
e. Emergency Removal of Property; and
f. Collapse of a Building.

Although not directly addressed in Plaintiff's Complaint, her lawsuit did seek relief and damages as it pertained to each of the foregoing claims.

Farmers answered Plaintiff's Complaint denying that she was entitled to any of the relief requested therein. CP 188-191. Farmers also asserted appropriate affirmative defenses and asked that Ms. Lesure's Complaint be dismissed in its entirety, with prejudice. CP 190-191.

Thereafter, Farmers filed a Motion for Partial Summary Judgment on the sole coverage issue of whether Ms. Lesure was entitled to any further benefits for the fire loss under Coverage A - Dwelling. CP 167-180. The Motion contained a specific footnote reserving its rights on issues other than the Coverage A – Dwelling claim.

> This motion addresses Plaintiff's contractual claim only. Farmers' conduct with regard to this claim was reasonable at all times. To the extent that Plaintiff makes claims for attorneys' fees or extra-contractual damages, Farmers

> reserves the right to seek summary judgment dismissal of those claims.

CP 168.

Farmers' Motion detailed the coverage issue, including the interplay between the Loss Payment Provision's "equivalent construction" language, the building and ordinance exclusion and Endorsement, and Washington law, particularly as set forth in *Allemand*. CP 167-180.

Ms. Lesure responded to Farmers' motion arguing that the Efficient Proximate Cause rule somehow applies to re-draft to terms of the policy to provide greater coverage than those expressly provided by the unambiguous terms of the policy. CP 40-50. Ms. Lesure's brief, as the Superior Court pointed out, did not address the *Allemand* case. CP 40-50.

> Despite the fact that the *Allemand* case is so closely on point, Ms. Lesure does not mention it in her memorandum. There is no attempt to distinguish the case, presumably because it is almost directly on point.

CP 13.

Ms. Lesure's opposition was based solely on her efficient proximate cause argument. CP 40-50. She did not contest the amounts paid by Farmers for direct physical loss, nor did she present any evidence indicating any dispute with the scope of repair adopted in Farmers' estimate. CP 40-50.

On June 4, 2015, after considering the briefing and hearing oral argument, the Superior Court issued a Memorandum Opinion on the coverage issue. CP 011-014. In that Memorandum Opinion, the Superior Court held the policy is unambiguous and that Farmers has met its coverage obligations. CP 011-014. The Trial Court then entered an Order granting Farmers' Motion for Summary Judgment, which stated that Farmers owes no additional benefits under the Coverage A – Dwelling policy provision. CP 009-010.

Following the Superior Court granting Farmers' Motion for Partial Summary Judgment, in order to secure a final judgment for purposes of triggering the right of appeal, the parties agreed to resolve all of her other claims. As a result, all remaining claims, including the remaining coverage claims and any extra-contractual claims, were resolved. The Superior Court entered Final Judgment on September 8, 2015. CP 005-006.

IV. LEGAL ARGUMENT

A. Standard of Review.

Ms. Lesure's brief does not include any reference to the standard of review for this appeal. Farmers therefore takes the opportunity to do so here.

An appellate court reviewing a summary judgment order must engage in the same inquiry as the trial court. *See Sedwick v. Gwinn,* 73 Wash.App. 879, 884, 873 P.2d 528, 531 (1994), *referencing Marincovich v. Tarabochia*, 114 Wash.2d 271, 274, 787 P.2d 562 (1990). The appellate court reviews the facts and law with respect to summary judgment de novo. *Mountain Park Homeowners Ass'n v. Tydings*, 125 Wash.2d 337, 341, 883 P.2d 1383 (1994).

Summary judgment is appropriate when the pleadings, affidavits, depositions, and admissions indicate that no genuine issue of material fact exists and a party is entitled to judgment as a matter of law. *Young v. Key Pharmaceuticals*, 112 Wn.2d 216, 225, 770 P.2d 182 (1989). In a summary judgment motion, the moving party bears the initial burden of showing the absence of an issue of material fact. *See LaPlante v. State*, 85 Wn.2d 154, 158, 531 P.2d 299 (1975). The trial court should grant the motion for summary judgment if a party "fails to make a showing sufficient to establish the existence of an element essential to that party's case, and on which that party will bear the burden of proof at trial." *Young,* 112 Wn.2d at 225, *quoting Celotex Corp. v. Catrett*, 477 U.S. 317, 322, 91 L. Ed. 2d 265, 106 S. Ct. 2548 (1986).

Farmers' Motion for Summary Judgment was based upon undisputed facts. In fact, Ms. Lesure agrees that "[t]he material facts are

not in dispute." CP 40. As a result, there are no factual issues and this case rests solely on an issue of policy interpretation or construction. Policy interpretation is a question of law. *State Farm General Insurance Company v. Emerson,* 102 Wn.2d 477, 480,687 P.2d 1139 (1984).

B. Principles of Policy Construction Under Washington Law

The interpretation of insurance policy language is a question of law. *State Farm General Insurance Company v. Emerson,* 102 Wn.2d 477, 480,687 P.2d 1139 (1984). A reviewing court examines the policy terms to determine whether or not under the plain meaning of the contract, there is coverage. *Kitsap County v. Allstate Insurance Company,* 136 Wn.2d 567, 575, *964* P.2d 1173 (1998).

If the language is clear and unambiguous, the court must enforce the policy as written and may not modify it or create ambiguity where none exists. *American National Fire Insurance Company v. B & L Trucking and Construction Company,* 134 Wn.2d 413, 428, 951 P.2d 250 (1998). A clause or phrase is only ambiguous when, on its face, it is fairly susceptible of two *different interpretations,* both of which are reasonable. *Weyerhaeuser Company v. Commercial Union Insurance Company,* 142 Wn.2d 654,666, 15 P.3d 115 (2000); *Kitsap County v. Allstate Insurance Company,* 136 Wn.2d 567, 575, 963 P.2d 1171 (1998). Courts may not strain to find an ambiguity in an insurance contract where none exists,

Farmers Home Mutual Insurance Company v. Insurance Company of North America, 20 Wn. App. 815, 820, 583 P.2d 664 (1978), nor can courts create ambiguity or doubt where language of an insurance policy is **not susceptible of more than one reasonable interpretation**, *Truck Insurance Exchange v. Aetna Casualty Insurance,* 13 Wn. App. 775, 778, 538 P.2d 529 (1975) (emphasis added); *Britton v. SAFECO,* 104 Wn.2d 518, 528, 707 P.2d 125 (1985). The rule that contracts of insurance are construed in favor of an insured and most strongly against an insurer should not be permitted to have the effect of making the plain agreement ambiguous, and then construing it in favor of the insured. *West American Insurance Company v. State Farm Mutual Auto Insurance Company,* 80 Wn.2d 38, 44, 491 P.2d 641 (1971).

C. Based on Nine Decades of Legal Precedent, The Superior Court's Ruling Correctly Applied The Language in the Lesure Policy and Concluded that She Was Not Entitled to Further Benefits

The Washington Courts have addressed the exact issue in this case. *See, Allemand v. State Farm Ins. Co.*, 160 Wn. App. 365, 248 P.3d 111 (2011). In fact, the facts in this matter are nearly identical to those in *Allemand.*

> It cost the Allemands $96,669.56 to replace the house under modern building requirements. Their State Farm homeowners policy provided a maximum of $89,866.00 under "Coverage A" to repair or replace the home "with

> similar construction." The policy also excluded "increased costs resulting from enforcement of any ordinance or law" including "construction repair or demolition" from coverage except as provided by optional "Option OL." That optional coverage provided an additional sum, equal to 10 percent of the policy maximum, for costs resulting from building code enforcement. The Allemands had purchased Option OL.
>
> State Farm paid the Allemands $59,663.55, consisting of the estimated repair costs from the fire plus the maximum OL coverage for the code updates. The Allemands then filed an action for declaratory judgment and damages, arguing that State Farm was required to pay the maximum under both Coverage A and Option OL.

Allemand, 160 Wn. App. at 367-68, 248 P.3d 111.

After addressing the well-settled standards under Washington law for the Court's review of an insurance policy, the *Allemand* Court turned to the question of whether insurance coverage extends to the costs necessary to bring a residence into compliance with modern building codes. The Court focused on four modern cases pre-dating its decision, but also acknowledged that historically, insurance was not construed as extending to code upgrades. Discussing a 1927 Washington Supreme Court decision, the *Allemand* court described the following:

> *Gouin* involved a house damaged by fire in Seattle. The owner's insurance covered replacement or repair "of like kind [or] quality." Modern building codes required the house to have a cement or stone foundation and required plaster walls; the previous house had no foundation and had cloth walls. The property owner appealed a jury verdict upholding an appraisal panel's award. Among the issues

> raised by the owner was a contention that the verdict was insufficient because the award did not include the cost to bring the repaired building up to code. The Washington Supreme Court declared that such costs were not contemplated by the parties and the damages were limited to the actual cash value of the property or the cost to repair or replace with "material of like kind." *Id.* at 208-209. In such circumstances, the building code requirements were not covered:
>
> > The requirements of the city went far beyond this. They required the foundations of the building to be entirely reconstructed and of different materials from that originally used; they required the upper parts of the building to be finished in a different manner than that in which it was originally finished; in fine, they required a practically new and more costly building. This, we cannot conclude, was within the contemplation of the contract.

Allemand, 160 Wn. App. at 367-68, 248 P.3d 111, *quoting Gouin v. Nw. Nat'l Ins. CO. of Milwaukee*, 145 Wn. 199, 259 P. 387 (1927).

Nonetheless, the *Allemand* Court turned its attention to its four immediate predecessors, finding that the coverage focuses on the language of the loss payment provisions.

The insured in *Allemand* relied primarily on a Division One decision in *Starczewski v. Unigard Ins. Group*, 61 Wn. App. 267, 810 P.2d 58 (1991). *Starczewski* involved a claim relating to a fire loss to a duplex where the policy provided for loss payments up to the actual cash value or 'the amount necessary to repair or replace" the property. *Id.* at 269, 810 P.2d 58. The *Starczewski* Court found that the "repair or replace" language in the loss payment provision necessarily required payment for

building code compliance. *Id.* at 274, 810 P.2d 58.

Four years later, Division One was once again confronted with this question in a matter entitled *Roberts v. Allied Group Insurance Co.*, 79 Wn. App. 323, 901 P.2d 317 (1995). *Roberts* involved a fire loss to a single family home that was not in compliance with the current codes. Unlike the policy in *Starczewski*, however, the *Roberts* policy provided for loss payments "for like construction". *Id.* at 325, 901 P.2d 317. That policy also specifically defined replacement cost as the costs associated with repairing or replacing property "with new materials of like kind and quality." *Id.* at 325, 901 P.2d 317.

The *Roberts* Court therefore determined that the *Starczewski* dicta relating to code compliance benefits was not applicable, and, relying on *Gouin*, determined that code compliance benefits were not available where the policy contains "like kind and quality" type language. *Id.* at 325, 901 P.2d 317.

The *Allemand* Court also discussed a Division Two case involving this same issue, and in fact discussing it in the context of a Farmers policy with the same language as that at issue in this case. *Dombrosky v. Farmers Ins. Co. of Washington*, 84 Wn. App. 245, 928 P.2d 1127 (1996). In *Dombrosky*, as here, the policy provided for repair or replacement of damaged or destroyed property with "equivalent construction." *Id.* at 257,

928 P.2d 1127. In fact, as is also the case in the instant matter, the *Dombrosky* policy also had a specific exclusion for costs related to the enforcement of building codes or ordinances. *Id.* The *Dombrosky* Court determined that the term "equivalent construction" had the same effect as the term "like kind and quality" in the *Roberts* policy and rejected the arguments of the insureds based on *Starczewski*. Thus, the Court concluded that based on "equivalent construction" language in the loss payment provisions of the Farmers' policy, along with the existing exclusion, there was no coverage available for code compliance.

Finally, the *Allemand* Court discussed a Division 3 case involving a fire loss to a residential structure. *DePhelps v. Safeco Ins. Co. of America*, 116 Wn. App. 441, 65 P.3d 1234 (2003). While the *DePhelps* case also provided for loss payment on an "equivalent construction" basis, the *DePhelps* Court found that the insureds were entitled to coverage for code compliance because the policy there at issue specifically included a clause indicating that losses would be paid "on the basis of any ordinance or law that regulates the construction, repair, or demolition of" the subject property. *Id.* at 449, 65 P.3d 1234. As a result, the *DePhelps* Court distinguished the *Roberts* and *Dombrosky* decisions on the basis that the *DePhelps* policy specifically provided a coverage extension for the cost of code compliance. *Id.*

Having fully addressed the legal standards for the analysis of this issue in the State of Washington, the *Allemand* Court then turned to the case before it, which, like here, involved (1) a loss payment provision similar to the *Roberts* and *Dombrowsky* cases, (2) a building and ordinance exclusion, like that in *Dombrosky*, and (3) a building and ordinance optional insurance endorsement limited to 10% of the Dwelling Limits.

> As all of those cases show, the ultimate controlling language is that found in the policy. The Coverage A language states in part that
>
> a. We will pay the cost to repair or replace with similar construction and for the same use on the premises ... subject to the following:...
>
> (4) we will not pay for increased costs resulting from enforcement of any ordinance or law regulating the construction, repair or demolition of a building or other structure, except as provided under Option OL – Building Ordinance or Law Coverage.

Allemand, 160 Wn. App. at 371, 248 P.3d 111.

Based on this language, the *Allemand* Court concluded that there would generally not be any coverage available to the insured for code compliance costs based on cases such as *Gouin*, *Roberts*, and *Dombrosky*.

> The policy at issue here covers "similar construction" and is the same as the "like" construction at issue in *Gouin* and *Roberts* and the "equivalent" construction in *DePhelps* and *Dombrosky*. Thus, the Coverage A component of this

> policy does not include building code upgrades as the policy in *Starczewski* did.

Allemand, 160 Wn. App. at 372, 248 P.3d 111.

However, the Court also held that because the *Allemand* policy contained the optional coverage for building ordinance and code compliance costs, the case was similar to the *DePhelps* case, but with one key distinguishing feature.

> Unlike that case, however, the policy here expressly limits the code upgrade coverage to 10 percent of the policy maximum.

Allemand, 160 Wn. App. at 372, 248 P.3d 111.

The *Allemand* Court then specifically held that the 10% of Coverage A limit was valid and enforceable.

> In light of the foregoing authority, the policy language is clear and this court is not in a position to find it ambiguous. *Quadrant Corp.*, 154 Wn.2d 165. State Farm's original obligation under Coverage A is to provide "similar construction" in rebuilding the home. Unlike Starczewski, that phrase does not include paying for required code upgrades. Instead, the policy provides for necessary upgrades by Option OL. That coverage is the sole source of the obligation to pay for bringing the remodeled home up to code. But that coverage is limited to the 10 percent of Coverage A that the Allemands purchased. The necessary upgrades required more than that figure and State Farm thus properly tendered its limits under that coverage. ***It was not required to pay more for the upgrades.***

Allemand, 160 Wn. App. at 373, 248 P.3d 111 (emphasis added).

The Court's decision in *Allemand* is directly on point in this

matter.

Ms. Lesure indicates in her briefing to this Court that she "disagrees" with the *Allemand* decision. However, Ms. Lesure's disagreement is based on the fundamental misapprehension of how the policies work under Washington law. Ms. Lesure's entire position is based on the argument that if Ms. Lesure had not purchased the optional coverage, she would have been entitled to payment for all code upgrades. In fact, Ms. Lesure repeats this argument throughout her briefing.

However, this argument ignores the fact that the policy issued to Ms. Lesure provides for loss payment on an "equivalent construction" basis, just as in *Dombrosky*, thereby precluding code upgrade coverage unless Ms. Lesure purchases the coverage separately. Here, Ms. Lesure, like the insured in *Allemand*, did purchase the coverage. However, that specific coverage is subject to a policy sub-limit. Ms. Lesure's complaint is really with the valid and unambiguous limit that applies to that coverage.

Moreover, the *Allemand* decision is not the final word from the Courts of this jurisdiction on this subject. In a July 7, 2015 decision, the United States District Court for the Western District of Washington, Honorable James Robart, summarized Washington law on this subject as follows:

> In interpreting similar policies, Washington courts have consistently held that replacement costs "for like construction and use" of a structure do not include costs of upgrading a structure to meet building codes that it did not previously meet. *See Allemand v. State Farm Ins. Companies*, 160 Wn. App. 365, 248 P.3d 111, 114 (Wash. Ct. App. 2011) (holding that coverage for "similar construction" did not include upgrades to comply with building codes); *Dombrosky v. Farmers Ins. Co. of Wash.*, 84 Wn. App. 245, 928 P.2d 1127, 1135 (Wash. Ct. App. 1996), as amended (Feb. 7, 1997) (holding that coverage for "equivalent construction" did [*12] not include building code upgrades); *Roberts v. Allied Group Insurance Co.*, 79 Wn. App. 323, 326, 901 P.2d 317 (Wash. Ct. App. 1995). (holding that coverage for "like construction" did not include building code upgrades). Therefore, the replacement costs described under subsection (b) do not include costs necessary to bring a formerly nonconforming structure into compliance with existing building codes. (See Policy at 16.)
>
> On the other hand, Washington courts interpreting similar provisions have found that replacement costs in the "necessary amount actually spent to repair or replace the damaged building" do include costs necessary to comply with building codes. See *Starczewski v. Unigard Ins. Grp.*, 61 Wn. App. 267, 810 P.2d 58, 62 (Wash. 1991). Therefore, it appears that the replacement costs described under subsection (c) could include compliance costs. On that basis, Mr. Allen argues that he is automatically entitled to coverage for costs of bringing his dwelling into compliance with modern building codes.

Certain Underwriters at Lloyds, London v. Allen, 2015 U.S. Dist. LEXIS 88141, 11-12 (W.D. Wash. July 7, 2015).

In applying this law to the facts then before him, Judge Robart raised an important distinction given the language at issue in the Loss Payment provision.

> Mr. Allen overlooks the fact that the Loss Settlement provisions provide that Lloyds will only pay the "least of" the three definitions of replacement and repair costs set forth in subsections (a), (b), and (c). (Policy at 16.) Therefore, to the extent the "necessary amount actually spent to repair or replace the damaged building" exceeds "the replacement cost of that part of the building damaged for like construction and use on the same premises," Mr. Allen is entitled to receive only the latter amount. Accordingly, the court holds that subsection (b) of the Loss Settlement provisions does not include coverage for costs necessary to bring a formerly nonconforming structure into compliance with current building codes, and to the extent the costs described under subsection (b) exceed the costs described under subsection (c), Lloyds is only required to pay the lesser amount.

Allen, 2015 U.S. Dist. LEXIS 88141 at 12.

In *Allen*, the insured had argued that because the term "like construction" only appeared in sub-paragraph b. of the loss payment provision, the policy would operate to provide code compliance coverage and would overcome a clear exclusion. *Id.* Judge Robart clearly rejected this argument, holding that Washington law is clear and that the terms of the loss payment provision are controlling. *Id.*

Finally, to the extent that Ms. Lesure is arguing that the limit itself is somehow ambiguous, the *Allemand* Court has also resolved that argument in Farmers' favor.

> The Allemands also argue that the Option OL coverage is ambiguous because it makes reference to the policy limits shown in the "Declarations," but the coverage limits page is not entitled "Declarations" nor is that word used on the

> page. Any confusion they may have had—and there has been no factual finding on that point—does not create an ambiguity. They were aware from Option OL that the coverage was limited. They were also aware from the cover page, even if they did not know what a "Declarations" was, what the limits were. Even if there was subjective confusion on this point, there was no ambiguity. The cover page, however denominated, expressly stated the limits of both Coverage A and Option OL. There was no ambiguity.

Allemand, 160 Wn. App. at 373, 248 P.3d 111 (emphasis added).

This case is quite simple. Ms. Lesure had a fire loss that caused $21,748.25 in damage. She was paid this full amount despite the fact that she never actually repaired the property.

Again, the Washington Courts have made it clear that an insurer is not obligated to pay the replacement cost value of a loss unless and until the insured actually incurs the costs in repairing the property. *Hess v. N. Pac. Ins. Co.,* 122 Wn.2d 180, 188, 859 P.2d 586 (1993), *Dombrosky*, 84 Wn. App. 245, 928 P.2d 1127. The policy language addressed in *Hess* and *Dombrosky* is the same as that at issue in this matter. In this matter, Ms. Lesure was not actually entitled to the replacement cost. Regardless, Farmers tendered that amount. The same issue applies to the Building Law or Ordinance coverage.

Ms. Lesure is required by operation of building codes to pay additional amounts beyond the amount of the direct physical loss – the fire damage – to bring the property into compliance with current building

codes. In accordance with the plain and unambiguous terms of her policy, Ms. Lesure would not be entitled to recovery of any code required expenses but for the fact that she purchased additional coverage. Ms. Lesure has been paid the full limit available under that coverage despite the fact that she has never actually incurred any expenses relating to bringing the property into code compliance.

All first-party property policies have some type of stated policy limits. In fact, property policies contain numerous sub-limits applicable to certain types of loss. For instance, policies typically contain sub-limits for losses to jewelry, for mold damage, and for business property. No Washington Court has ever held that these types of sub-limits are unenforceable.

In fact, the Washington Courts have consistently upheld such limits. For example, in a case applying Washington law, the Ninth Circuit upheld the enforceability of an earthquake sub-limit that reduced available property damage coverage from $5,000,000 to $500,000. *Caliber One Indem. Co. v. Wade Cook Fin. Corp.*, 491 F.3d 1079 (9th Cir. Wash. 2007).

Ms. Lesure's complaint is not that she was inappropriately denied coverage. Rather, her complaint is with the amount of coverage she purchased. This is not a basis under Washington law to alter the terms of

the policy or to somehow void a policy limit.

As a matter of law, Ms. Lesure is not entitled to any further benefits under the policy and the Superior Court should be affirmed.

D. The Efficient Proximate Cause Rule Is Inapplicable and Does Not Operate to Alter the Coverage Available Under the Subject Policy.

Ms. Lesure's sole argument in this case is that the Efficient Proximate Cause rule somehow operates to alter the Building Ordinance or Law coverage in her policy. Ms. Lesure's argument is without merit.

Ms. Lesure fails to set forth any legal authority in support of this position. In fact, Ms. Lesure concedes that the Washington State Supreme Court has not ever addressed the issue of whether the Efficient Proximate Cause Rule can somehow be utilized to change how the policy provides coverage. However, the Washington Courts *have* addressed this argument and it has been specifically rejected.

Ms. Lesure's argument was made and rejected in the *Allemand* case. The *Allemand* Court, rejecting this argument, specifically stated the following:

> This [OL Option] provision recognizes the efficient proximate cause rule; the Allemands' argument that the policy conflicts with that rule is without merit. The policy actually applies the rule and covers building code upgrades that are required when repairing a covered loss.

Allemand, 160 Wn. App. at 373 at fn 2., 248 P.3d 111.

More recently, the United States District Court for the Western District of Washington, Honorable James Robart, also addressed this argument, rejecting the notion that the Efficient Proximate Cause Rule applied to a similar case.

> Second, Mr. Allen argues that the efficient proximate cause rule nonetheless precludes application of the exclusion. "The efficient proximate cause rule operates to permit coverage when an insured peril sets other excluded perils into motion which 'in an unbroken sequence and connection between the act and final loss, produce the result for which recovery is sought.'" Kish, 883 P.2d at 311 (*quoting Graham v. Public Employees Mut. Ins. Co.*, 98 Wn.2d 533, 656 P.2d 1077 (Wash. 1983)). "In such a situation, the insured peril is considered the proximate cause of the entire loss and the loss is covered despite the fact that the other perils contributing to the loss were excluded." Id.
>
> The efficient probable cause rule is inapplicable to the instant situation. The rule "applies only when two or more perils combine in sequence to cause a loss and a covered peril is the predominant or efficient cause of the loss." *Vision One, LLC v. Philadelphia Indem. Ins. Co.*, 519, 174 Wn.2d 501, 276 P.3d 300, 309 (Wash. 2012); see also Kish, 883 P.2d at 312 ("When, however, the evidence shows the loss was in fact occasioned by only a single cause, albeit one susceptible to various characterizations, the efficient proximate cause analysis has no application. An insured may not avoid a contractual exclusion merely by affixing an additional label or separate characterization to the act or event causing the loss."). ***Here, there is only one cause of the loss—the fire. The issue is not what caused the losses, but rather what losses caused by the fire are recoverable.*** As addressed in the preceding paragraph, that issue is governed by the Loss Settlement provisions.

Certain Underwriters at Lloyds, London v. Allen, 2015 U.S. Dist. LEXIS 88141, 13-14 (W.D. Wash. July 7, 2015)(emphasis added).

This is not an Efficient Proximate Cause Case. Once again, the policy in this case provides coverage for direct physical loss. CP 127. In this case, there was one direct physical loss – a fire. The issue before this Court, as it was in the *Allen* case, is not what caused the loss, but what losses caused by the fire are recoverable.

In this case, Ms. Lesure was entitled to the amounts necessary to repair the fire damage as well as the limit available for code compliance coverage. The Efficient Proximate Cause Rule does not alter this result.

Moreover, even if this Court were to engage in an Efficient Proximate Cause analysis, the conclusion would be the same. Under Washington law, the Efficient Proximate Cause Rule applies only to determine coverage where a loss involves multiple causes, some of which are covered, and some of which are specifically excluded. *Graham v. Public Employees Mut. Ins. Co.*, 98 Wn.2d 533, 538, 656 P.2d 1077 (1983).

In order for the Efficient Proximate Cause Rule to apply a covered peril must set into motion an "unbroken sequence" of events, including an uncovered peril, such that the uncovered peril does not operate to preclude coverage for the entire loss. *Graham, supra.* The Efficient Proximate

Cause Rule "does not allow a claimant to focus on one covered cause out of a causal chain." *Wright v. Safeco,* 124 Wn. App. 263, 275, 109 P.3d 1 (2004).

Ms. Lesure's argument is that a covered loss (fire) resulted in the City of Port Angeles enforcing its building codes, which is somehow an unbroken chain implicating the Efficient Proximate Cause Rule. This makes no sense. The decision by the City of Port Angeles Building Department to enforce the building code was a superseding and intervening event. It is not a direct result of the fire, but rather the result of the city ordinance. This caused a break in the sequence of events. *Wright* 124 Wn. App. 263, 109 P.3d 1.

Finally, even accepting Ms. Lesure's argument that the fire and the building code enforcement are somehow two causes within the same "unbroken sequence", the Efficient Proximate Cause Rule does not apply because Ms. Lesure had coverage for the fire loss and was also paid the full limit of her coverage for the building code enforcement.

Once again, Ms. Lesure's complaint is that the building code enforcement coverage has a limit that was not sufficient to cover the cost of a complete rebuild of her residence. Ms. Lesure has not, however, provided any legal authority for the proposition that the Efficient Proximate Cause Rule somehow renders the policy limit inapplicable.

Once again, Ms. Lesure's entire claim is really based on a disagreement with the application of the sub-limit. As is discussed above, the Washington Courts have routinely held that sub-limits in first-party property policies are valid and enforceable. *See, Wade Cook, supra.*

As a result, the Efficient Proximate Cause Rule is inapplicable to the instant case and the Superior Court properly granted summary judgment in Farmers' favor.

V. CONCLUSION

Based on the foregoing, Farmers asks that the Superior Court be affirmed in its entirety and that a Mandate be issued ending this litigation.

DATED this 9 day of March, 2016.

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CERTIFICATE OF SERVICE

The undersigned certifies that on the date below stated they caused the foregoing Respondent's Brief to be served upon the below party(ies) at the address(es) and by the method(s) so indicated.

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