HOMEOWNERS' SUBROGATION CLAIMS:

A PRACTICUM ON HOW TO MAXIMIZE YOUR RECOVERIES

I. INTRODUCTION

Subrogation claims for personal lines losses generally fall into one of the following categories: electrical; mechanical; careless smoking; negligent or reckless misconduct by household residents or guests; building systems (other than electrical or mechanical); and automobiles. This paper will explore some of the typical scenarios involved in the failure or malfunction of certain equipment and systems, as well as the negligent and careless use of potential sources of ignition. With proper investigation and coordination by subrogation counsel, many of these losses can give rise to a successful subrogation recovery.

II. OVERVIEW

It is important to remember that when dealing with personal lines losses, we are addressing highly protected risks. Typically, a home is the most valuable item of property owned by your insureds, and generally, your insureds are well motivated to protect and take care of their homes. For the most part, the mechanical, electrical and other systems in a home are sufficiently sophisticated that outside contractors are usually brought in to install, maintain and repair the equipment within these systems. Homeowners (your insureds) expect that these contractors will be knowledgeable about applicable industry standards and that their work will comply, if not exceed, these minimum requirements. Your insureds place reliance - and this is a critical concept - upon the contractors who are hired to take care of their home. If the products supplied or work performed are deficient, the context augurs well for a favorable result, including the legal context in which the case will unfold.

Many courts will distinguish personal from commercial losses, and case law frequently provides for enhanced rights of recovery for individuals for personal losses, as

distinguished from business losses for commercial entities. An example of this is an exculpatory or limitation of liability provision contained in a pre-printed warranty which might be supplied with an appliance when purchased. In a personal consumer transaction, such a restrictive term may be deemed to be part of a contract of adhesion, meaning a contract that your insureds did not have the right or ability to negotiate or discuss, because of the unequal bargaining position between your insureds and the manufacturer. Such unilaterally imposed restrictive provisions may be deemed unenforceable to bar or restrict claims for personal lines losses. These provisions generally are enforced by the courts in the context of commercial losses. Thus, the ability to prosecute subrogation claims for personal lines losses represents a significant opportunity to increase your recoveries. However, to maximize this opportunity it is essential that all potential claims should be identified promptly, investigated thoroughly, and pursued aggressively.

III. ELECTRICAL

Electricity typically is provided to a structure from above-ground service entrance cables which are connected at one end to the utility's distribution line, and on the other end to a distribution panel within your insureds' home. Somewhere between these connections is the meter. The point at which the utility company's responsibility ends and your insureds' responsibility begins must be determined by reviewing the utility company's tariff. Conventional wisdom is that everything upstream of the meter belongs to the utility, and everything downstream belongs to the customer, but this frequently is not correct. Often, there is a connection called a "point of delivery" located upstream of the meter. The utility company will argue this connection imposes responsibility on your insureds for the installation and maintenance of all cables downstream of the "point of delivery" connection, including cables leading to and from the meter. However, the utility company generally will inspect the

installation of those cables installed by an electrical contractor before turning on the electrical service. This inspection implies some degree of approval with a commensurate degree of responsibility. Any failure in the cables providing electricity to your insureds' distribution panel needs to be thoroughly investigated from the perspective of ownership, control and responsibility for the failed conductors.

The most common distribution equipment within your insured's home is a panel containing circuit breakers which, for the most part, have replaced fuses in a homeowner setting. Most electrical engineers tell us that while circuit breakers are more convenient, they have significantly greater potential for failure, because of their electro-mechanical design. Circuit breakers can be made with design and manufacturing defects, or their electrical and mechanical components can deteriorate over time. Circuit breakers also can be affected by ambient conditions, such as a moist or corrosive atmosphere.

On the other hand, fuses contain a metal link which reacts simply to the heat generated by the level of current in the conductor cable being monitored. Once the value exceeds the rating of the link, it melts and opens the circuit, thus clearing any fault. A fuse is a much more fail-safe device than a circuit breaker.

The results of a study performed by the United States Consumer Product Safety Commission showed a surprisingly high failure rate of a variety of different brands of molded case circuit breakers. Many of the breakers tested failed to clear faults within the required time under accepted industry standards. When a circuit breaker is slow or fails to clear a fault, it will allow sustained overcurrent at the point of failure in the downstream wiring or in the equipment being protected by that breaker. Often this slowness or failure will lead to electrical arcing and expulsion of hot, molten metal which is sufficient to ignite nearby combustibles.

In many instances, the precise nature of the electrical fault may be undetermined, a viable defendant may not be identified, or the work may be the responsibility of your insureds. In each instance where an electrical failure occurs, close scrutiny should be made of the overcurrent protection system to determine if there was a breakdown in the protective scheme which allowed the electrical fault to persist for a sufficient time to turn a fault into a fire. Frequently, the circuit breaker panel box is situated at a location away from the area of the fire, so that identifying the manufacturer of the suspect circuit breaker can be made easily.

Under these circumstances, it is imperative that all of the physical evidence be preserved, beginning at the instrumentality causing the fire, and continuing upstream to include the circuit breaker and panel box.

Virtually every jurisdiction within the United States has adopted the National Electrical Code as part of the jurisdiction's applicable building code. The NEC has very specific procedures for designing and installing electrical equipment and systems, including overcurrent protection devices. It is important to research and review the applicable provisions of the NEC. Utilities are not governed by the NEC, but must adhere to the National Electric Safety Code, which similarly should be consulted for evaluating potential misconduct on the part of electrical utilities.

Frequently, small appliances must be investigated as potential ignition sources in any homeowners' loss. These appliances, usually purchased for a moderate price, still must comply with accepted standards of engineering design with respect to their critical components: insulation values; connective devices; thermal controls; overcurrent protection; and the use of fire-resistant or non-flammable components. By purchasing an exemplar, it is relatively easy to determine the nature of these components. On the basis of the examination of the exemplar, a

preliminary determination can be made that a substandard design or mechanism was employed. It is relatively easy to examine the fire artifact itself for any signs of failure associated with the substandard components. Also, it is essential to research applicable standards establishing guidelines for the design and manufacture of these appliances, including standards issued by Underwriters Laboratories (UL) and the American Society for the Testing of Materials (ASTM).

IV. MECHANICAL

There are two broad areas to consider: water leaks and related plumbing failures; and the breakdown of electro-mechanical equipment with resulting causation of fires.

For plumbing losses, there typically are numerous connections, many of which are soldered, associated with a domestic plumbing and water system. With plastic piping, it is typical to encounter connections with adhesives or mechanical fasteners. Any failure of these connections must be investigated carefully to determine if installation deficiencies and/or product defects are responsible. In particular, close attention should be paid to connections of dissimilar materials, which frequently will expand and contract at different rates, causing connections to loosen. The supporting mechanism must be analyzed to determine whether the weight of the system was not adequately supported, and/or made vulnerable to external damage or abuse. Any piping which is subject to vibrations, from sources such as motor vehicles or heavy equipment, also is a potential source of failure and a potential basis for a subrogation claim.

Pipe ruptures due to freezing usually result from standing water not properly drained. This type of loss requires an analysis of the potential for clogging or inadequate drainage.

Plumbers typically will use torches to “sweat” or “size” a pipe; however, this procedure is recognized as an extreme fire hazard. It is not unusual for fires of this nature to

begin in such an inconspicuous manner that the plumber may leave the site, allowing the fire to smolder and eventually manifest itself with open, flaming combustion, many minutes or even hours after the plumber has departed the premises.

HVAC systems within a home contain various types of equipment which have the potential to cause fires: boilers, hot water heaters, dehumidifiers, filtering systems and numerous other devices. Applicable NFPA standards acknowledged as industry standards, should be consulted, since they contain very specific guidelines, for the installation, maintenance and repair of HVAC equipment. Frequently, your insured calls a contractor to troubleshoot a situation, or to replace a component part, which entails the contractor to inspect and test the related componentry or the entire assembly. Fires frequently are associated with improper or inadequate venting and exhausting of stack gases and other by-products of combustion. Even though they may be part of the original equipment, the vents have to be evaluated with the performance of combustion tests by the contractor performing the maintenance or repair work. If your insureds have service contracts requiring periodic inspections, start-up and other standard services, the contractor effectively has undertaken the responsibility to evaluate the important components and critical controls of the equipment. If the components and/or controls fail, it is a failure on the part of the contractor which may support a subrogation claim.

There are potential design and manufacturing deficiencies in the automatic controls, regulators, valves and other mechanisms associated with HVAC equipment, all of which have to be evaluated and measured against applicable industry standards.

V. CARELESS SMOKING

The careless discarding of smoking materials and related ignition sources should always be evaluated as a potential source of ignition. Smoking materials can include cigarettes, cigars, matches, candles, incense and other similar items. If the responsible actor is not your

insured, either as a named policyholder or as an additional insured by definition, there is a substantial basis for proceeding against him or her. The potential group of responsible third parties would include house guests, tenants, babysitters, contractors, cleaning service personnel, and even family members who reside elsewhere. Obviously, all members of these groups are on notice that a burning candle, cigarette or match can easily cause a fire, and must be handled and disposed of with great care. When dealing with specialized receptacles for candles, consideration must be given to whether conspicuous and adequate warnings and instructions were provided by the seller. Mechanical devices such as cigarette lighters typically can be purchased for about one dollar, and generally receive about the same amount of engineering consideration. Failure rates of cigarette lighters are alarmingly high, and any lighter-induced fire must be evaluated for a potential malfunction. When investigating household fires, the burn patterns may lead to a trash can or other container which has no potential source of ignition other than carelessly discarded smoking materials. In this manner, all causes of the fire other than the careless use of disposal of smoking materials can be ruled out.

VI. NEGLIGENT OR RECKLESS MISCONDUCT BY HOUSEHOLD RESIDENTS, GUESTS OR OTHER INVITEES

This category covers a wide spectrum of culpable conduct, including fires caused by minors, improper use of household appliances, failure to maintain safe conditions by adjacent property owners, and numerous other fact patterns. In every case, the analysis is the same: was there a duty on the part of the actor which was violated, thereby causing damage to your insured. The existence and nature of a duty always is the paramount consideration. Sometimes it can be established by a written agreement (e.g. lease agreement, service contract), but more often it is necessary to research written standards and codes, and consult with specialized experts, to

develop the applicable standard of care. Case law also should be analyzed to determine if authoritative precedents exist.

Any minor who causes damage will be deemed an additional insured under that minor's parents' homeowners' policy. The question of intentional misconduct, and its implications for potential policy exclusions, must be addressed, but it is not atypical for a minor to lack the required specific intent to bring about the full consequences of his or her thoughtless actions. In other words, the intent to start a fire in a trash container is not the same as intending to burn down the entire house. The same analysis concerning intent-versus-consequences should be applied for other types of reckless or even intentional misconduct.

Every person who enters your insureds' household has a duty, imposed by law, to act with reasonable care to avoid causing foreseeable damage to your insureds' property. Reasonable care is the prism through which the actor's conduct must be viewed. Any deviation from reasonable care, with resulting foreseeable damage, gives rise to a negligence claim.

These scenarios also may involve the use of products, ranging from appliances to solvents to tools. Any instrumentality involved in causing the loss must be evaluated, both with respect to potential design/manufacturing defects, as well as in the context of whether adequate, necessary and conspicuous warnings and instructions were given concerning foreseeable dangers arising from expected use of the product. Where a claim can be developed against both the user of the product, as well as the manufacturer, typically there will be "cross-fire" between these defendants which can only inure to the subrogating carrier's benefit.

There is a legally imposed duty on the part of property owners to maintain their premises in a reasonably safe condition so as to avoid foreseeable damage to adjacent properties. Improper maintenance of the structural components of a building or of a building's systems

which cause a failure with resulting damage to an adjacent structure, create a strong basis for proceeding against the responsible property owner. Moreover, even when there is intervening conduct by a third party — such as juveniles or vandals — this does not necessarily relieve the property owner of responsibility. If the property owner allowed conditions to deteriorate on his or her property, such that it became an attractive nuisance to juveniles or vandals, and/or if such third parties were using the premises with actual or constructive notice to the property owner, there is a solid basis for proceeding against the property owner for failure to stop the improper and frequently dangerous use of the property with the foreseeable risk of harm to adjacent homes.

VII. BUILDING SYSTEMS (OTHER THAN ELECTRICAL OR MECHANICAL)

Roofing systems typically are constructed of a series of layers of roofing materials, adhered or fastened to each other, and ultimately to the roof structure of the home. The roofing materials generally are sold through a distribution network involving manufacturers, wholesalers, retailers and installers. Industry literature contains detailed specifications and instructions concerning appropriate applications and procedures for the use and installation of these materials. Any roofing failure, even those accelerated by a force of nature, must be evaluated to determine whether the roof and roofing components were properly selected and installed in compliance with industry standards, manufacturers' instructions, and applicable building codes.

Fireplaces, by definition, involve potential fire hazards, and must be designed and erected to provide a positive, fail-safe means for the safe exhausting of hot embers and combustion gases from the fire box through the flue and chimney. Common experience demonstrates that embers or ashes from a burning log remain hot, and represent a potential source of ignition, for many hours following the use of the fireplace. The exposure of nearby

construction materials to the heat of a fire, particularly over time, is a recipe for causing pyrolysis, or the drying of combustible materials with a correlated decrease in the ignition temperature of those materials. The nature of the wood itself also must be analyzed: excessive creosote deposits can cause unusually high stack temperatures.

Most building systems will undergo an inspection and approval process by an independent third-party agency. While there may be issues of immunity for governmental entities that perform this role, the inspection activities of all approval agencies must be analyzed from a tort liability perspective.

VIII. AUTOMOBILES

Automobiles, like fireplaces, furnaces, and other similar equipment, contain all of the ingredients necessary to cause a fire: sources of ignition (catalytic converters, spark igniters, batteries, hot conductors and more), a readily ignitable fuel (gasoline, gasoline vapors, wiring insulation, plastics, foam and more), and an ample supply of oxygen. An automobile fire itself, causing damage solely to the automobile, must be evaluated for a potential design/manufacturing defect, or improper servicing. Such fires often involve exposure damage to adjacent carports, garages and houses. As with any fire investigation, an inspection must be done to determine whether the vehicle was within the area or origin. It may be appropriate to focus attention on the vehicle as the most likely source of ignition if there is severe, localized and non-uniform damage within the vehicle.

It is not unusual for the damage to the engine compartment to be so severe as to obliterate the specific defect that gave rise to the fire. Many states provide an enhancement of the circumstantial evidence rule under these circumstances, whereby a successful subrogation case can be built upon proof that the fire was caused by a non-specific malfunction of the automobile which, given the car's age, condition and history, reasonably cannot be attributed to

any source other than a manufacturing defect. Obviously, it is necessary to rule out reasonable secondary causes, such as improper servicing, the activities of the insured, misconduct by a third party, or other ignition sources in the area of origin.

IX. PRACTICE POINTERS

Often the amount of the loss imposes restrictions upon the extent of the investigation that can be conducted. Spoliation of evidence issues dictate that, wherever possible, a potentially responsible third party should be placed on notice as early as is practicable. In addition to precluding spoliation contentions down the road, this often has the additional benefit of enabling the subrogating carrier either to shift to or share with the prospective defendant certain investigation expenses. For instance, it may be necessary to perform x-ray examination or to perform destructive disassembly of a small appliance in order to determine the nature of the defect, or even to confirm the identity of the manufacturer. The manufacturer will have a legitimate interest in having these tests performed, since the result may exculpate the manufacturer from any responsibility. Similarly, the subrogating carrier needs the test results in order to determine whether there is a basis for pursuing a claim against the manufacturer. Under those circumstances, it is reasonable to request the manufacturer to absorb all or part of the cost and associated expenses of performing the test. A similar approach should be made in other contexts, e.g., evaluation of electrical equipment installed by a contractor for evidence of an internal breakdown, metallurgical evaluation of pipes and connections or evidence of fatigue failure, and many similar scenarios.

The subrogating carrier always should determine the nature of any investigation carried out by the public sector authorities. In the event that the findings of the public sector officials corroborate and support those of your privately retained consultants, this should be used as the bedrock for the resulting subrogation claim. Ultimately, if the specially retained experts

cancel each other out, it is the public sector authorities who are left standing, and it is not unreasonable to expect that their determinations will carry the day.

Early investigation of a subrogation claim does not necessarily require taking a written or tape recorded statement from your insureds. In fact, by doing so, you are simply memorializing your insured's recollection for your future opponent's benefit. Early retention of subrogation counsel can enable a detailed interview of your insureds to take place, and allow the investigative process to unfold, all in an appropriate, privileged context.

X. CONCLUSION

It is important to reiterate that consumers are provided with a heightened degree of protection beyond that extended by the law to commercial entities. In addition to rights of recovery under common law principles such as negligence and strict products liability, many states have legislated additional litigation weapons in the form of consumer protection statutes which often provide for doubling or trebling of damages, as well as recovery of attorney's fees and costs. Absent a situation in which your insured is solely responsible for the loss, without involvement of any other actor or potentially defective instrumentality, every homeowner's loss should be investigated promptly, thoroughly and professionally, with supervision and coordination by subrogation counsel to identify all claims, and to maximize the opportunities for subrogation recoveries.

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