

## **Ninth Circuit to Oregon: A Liability Policy's Known Loss Provision Does Not Bar Coverage for Damage that Occurs After Negligent Repair**

April, 2017

On April 20, 2017, the United States Court of Appeals for the Ninth Circuit issued another in a string of recent decisions from the appellate court that rejected insurers' coverage defenses based on the contractual known loss provision. In *Alkemade v. Quanta Indem. Co.*, No. 14-35605, 2017 WL 1404708 (9th Cir. Apr. 20, 2017), the court held that "a plausible and reasonable interpretation of the insurance contracts permits the conclusion that damage caused by a first negligent act does not continue, change or resume when later damage is sustained after a repair that would have fixed the problem absent a second negligent act."

The case facts are straightforward. The plaintiffs' home was improperly constructed. After receiving notice of the damage that occurred over a number of years, the contractor performed repairs that would have prevented the same damage to the home in the future if the repairs were done correctly. You guessed it, they were not.

Two of the contractor's insurers declined the duty to defend. They argued that the contractor's knowledge of damage caused by the original defective construction, including knowledge of the risk that the same damage could occur again, prevented coverage under the policies' known loss provision. The plaintiffs countered that damage caused by the contractor's negligent repair is not a continuation, change, or resumption of the original damage. While the court found the insurers' interpretation of the known loss provision to be reasonable, it concluded that under Oregon law (*i.e.*, the *Hoffman* analysis) the plaintiffs' equally reasonable interpretation meant that the insurers owed a duty to defend and possibly (on remand) a duty to indemnify.

Unfortunately, the court gave short shrift to the *Hoffman* analysis. The court described an insured's task under Oregon law to offer a competing, plausible interpretation as a "low bar." However, for a policy term to be ambiguous—and therefore interpreted in favor of the insured—the Oregon Supreme Court held that "there needs to be more than a showing of two plausible interpretations." According to the Oregon Supreme Court, "competing plausible interpretations simply establish ambiguity that will require some interpretive act by the court. This triggers a series of analytical steps, any one of which may resolve the ambiguity [before the policy is construed against the insurer]."

The *Alkemade* court confined its analysis to whether the plaintiffs' interpretation of the known loss provision was plausible and reasonable. Although the known loss provision applies to "continuation, change or resumption" of known damage, the court held that "it is plausible to conclude that damage sustained after a repair that would have fixed the problem absent new negligence is not a 'continuation, change or resumption' of previously known damage."

The court concluded that a duty to defend exists, but the case was remanded to resolve the duty to indemnify. The plaintiffs' win on appeal might turn out to be a Pyrrhic victory. On remand, the insurer may be able to argue that "new" damage caused by negligent repairs is subject to other policy exclusions for faulty work.