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FREEZING AND EXPANSION PERILS EXCLUDED IN CAUSAL LANGUAGE ALL RISKS POLICY

Richards Buell Sutton Insurance Newsletter

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At issue in *Wynward Insurance Group v. MS Developments Inc.*, 2015 BCSC 324 was the enforceability of specific exclusions in an all-risk policy covering commercial premises damaged by frost heave. The heave occurred after the failure of a freezer drainage system in a restaurant. The heave caused extensive damage to floors, walls and ceiling in the restaurant as well as consequent business interruption and other losses.

THE FACTS

The insureds owned the subject premises in Kelowna, BC and operated a restaurant and bar on the premises. The restaurant had a large walk in freezer which naturally created condensation through its operations. The condensation was drained from the premises by a drain pipe. To prevent freezing, the drain pipe was wrapped in tape containing electrical heating elements. This tape is commonly known as heat wrap or heat tape. In late 2013, the heat tape failed causing the drain pipe to freeze and burst. Water migrated from the broken drain pipe through the freezer wall and onto and through the freezer floor slab. Water accumulated under the freezer floor slab and restaurant walls where it froze. This freezing caused the ground around the freezer and restaurant walls to heave and damage floor tiles, walls, doors and even the ceiling in the vicinity of the freezer. The insured sought indemnity for property damage and business losses under its all-risks property policy.

THE POSITION OF THE PARTIES

The insurer denied coverage, and then petitioned the court for a declaration that the losses were caused, either directly or indirectly, by three excluded perils: “freezing”, “earth movement” and “settling, expansion, contraction, moving, shifting or cracking”. The insured, on the other hand, argued that all of the exclusion clauses in issue were ambiguous, and therefore ought to be construed narrowly and *contra preferentum* against the insurer. In particular, the insured argued that the clauses were ambiguous in not distinguishing whether they were limited to naturally occurring events or included man-made causes.

THE RULING

The court ruled that two of the three exclusions applied and accordingly granted a declaration that the insurer was not obliged to indemnify for the loss. The court considered first the "freezing" exclusion. This clause provided that coverage would not be extended where the loss or damage was caused "directly or indirectly" by "changes in or extremes of temperature, heating or freezing". The court easily concluded that the damage flowed "indirectly" from the phenomenon of freezing, both at the drain pipe and ground, and that coverage was therefore excluded by an unambiguous exclusion.

The "earth movement" exclusion required greater consideration from the court due to a line of established case authority favouring the insured, including the decision in *Strata Plan NW2580 v. Canadian Northern Shield Insurance Co.*, 2006 BCSC 330 (CanLII). In that case, following earlier appellate authority, the B.C. Supreme Court found ambiguity in a near identical "earth movement" clause. The ambiguity arose from the fact that the clause in issue could be interpreted as including both naturally occurring phenomenon and man-made events. Therefore, because the earth movement at issue had a man-made cause, resolving the ambiguity in favour of the insured meant reading the clause narrowly to exclude only coverage for damage caused by naturally occurring phenomena. The court in *Wynward* followed this approach, and extended coverage.

The third exclusion was based on "expansion". The clause excluded loss and damage occurring by "settling, expansion, contraction, moving, shifting or cracking". Here again, the notion of natural vs. man-made causes was the thrust of the insured's plea for ambiguity. And here again, the court looked to guidance from the 2006 decision in *Strata Plan NW2580*, but – interestingly – with a different result than with the "earth movement" exclusion. In *Strata Plan NW2580*, a very similar clause excluding "expansion" was held to encompass both natural and unnatural events, thereby avoiding the ambiguity that afflicted the earth movement exclusion. Note the insured in *Wynward* argued also that the expansion clause was ambiguous in that it did not state what material was meant to settle, expand, etc. The court disagreed, stating that it was "clear on the face of the clause" that the material at issue was the ground. Finally, the court rejected case authority from the Alberta Court of Appeal that arguably favoured the insured, on the basis that it was not binding in B.C.

PRACTICAL CONSIDERATIONS FOR INSURERS

This case is a useful reminder of certain policy interpretation fundamentals:

- There can be a significant difference in the interpretation of "causal based" exclusions, such as those at issue in *Wynward*, as compared to "damage based" exclusions;
- Causal based exclusion clauses require evidence, usually expert, on the cause of loss. In *Wynward*

the insurer's and insureds' experts agreed on the cause of the loss thus allowing the parties to have the policy interpretation done by way of petition and without need of a trial. Insurers are well advised to employ competent adjusters and obtain early expert opinion when addressing losses under policies containing causal based exclusions;

- The failure to specify if an exclusion applies regardless of whether it occurs from natural or man-made sources may, in the context of certain exclusions, result in an ambiguity which will likely be resolved in favour of the insured; and
- Courts in different jurisdictions may treat similar exclusions in an opposite manner. Insurers must be aware of how the subject jurisdiction has treated the relevant exclusion(s) before making a coverage determination.