



Cosmetic Damage Exclusion and First Party Lawsuits

As more carriers begin to adopt the new American Association of Insurance Services (AAIS) and ISO endorsements governing the cosmetic damage exclusion due to wind and hail, one certainty is that these exclusions will surely result in a series of new lawsuits.

What Constitutes Cosmetic Damage?

The exclusion, available as an optional policy endorsement, will likely exclude coverage for exterior surfacing of most of the structure, including walls, roofs, doors and windows, provided that the wind and hail damage to the surfaces impacts appearance but does not impair those barriers' ability to prevent weather elements from creating havoc. The obvious question is what constitutes cosmetic damage?

It is easy to envision a situation in which a vandal tosses a can of paint onto a house's exterior wall. This is cosmetic damage, and if the insured with the vandalized wall has a cosmetic damage exclusion



in his policy, there would be little debate over whether it should be covered. However, the likelihood that there will be far more nuanced debates over what does and doesn't constitute cosmetic damage seems very high.

Think of roofing shingles being discolored, which some engineers determine constitutes structural damage because the shingles are no longer fully functioning, as the discoloration portends a weakening of the actual shingles.

By Jason Wolf

Or, what about a chip in a home's stucco that does not immediately impact the wall's ability to keep out rain, but over time, is arguably (from an insured's perspective) likely to result in more serious, and permanent damage that could cause structural damage?

Even a crack in foundation can be considered simply cosmetic, causing no unsafe or unsanitary conditions. But if the crack ultimately creates a sloping floor, which has happened in the past, it's a different issue. In that case, the insured and insurer would probably disagree over whether the crack is cosmetic or not.

The Sinkhole Precedent

The state of Florida has already enacted a statute that addresses cosmetic versus structural damage, although it focuses on sinkholes and has no impact on windstorm and daily damage claims. Analyzing the sinkhole statute gives us an apt analogy, because Florida's efforts to limit payments was seen by the policyholder bar as an effort to limit claims and lawsuits over sinkholes.

In 1981, the Florida Legislature enacted Fla. Stat. 627.706, which required insurers to provide coverage for sinkhole losses, which were defined as "structural damage to the building." The statute was revised several times over the years, then in 2011, the legislature included a restrictive and specific definition of "structural damage." I believe, as do many property insurance lawyers, that the state Legislature was compelled to act because of the increase in litigation over what constituted structural damage.

Before the statute was amended to add the full definition of structural damage, Florida courts determined "structural damage" to constitute "damage to the structure." This often resulted in the opposite impact of the exclusion, because harm to any property is thus damage to the property's structure. This subverted the process of the cosmetic damage exclusion; even a can of paint splashed on a wall would be included under this broad definition, because the colored paint causes "damage to the structure," although the property is not "structurally damaged." (Can you see why the statute needed to be clarified and amended?)

When a sinkhole claim is made, sinkhole engineers evaluate the situation by assessing construction defects, thermal expansion, differential settlements, organics, date of loss and an array of other factors to determine whether there is true structural damage. There are also specially trained adjusters who assess structural impairment or loss caused by sinkholes.

With the new wind and hail damage and the cosmetic exclusion for non-sinkhole claims, a similar scenario may ensue.

Will we see engineers who solely assess wind and others that develop expertise in ice damage as occurs in Montana, New Hampshire and Idaho?

These engineers will be tasked to determine whether the damage is cosmetic — rusty eaves, cracked sidewalks — or more serious — snow weight beyond the load-bearing capacity of the roof that invades the home.

A Pandora's box of conflicting perceptions will occur when cosmetic damage is excluded, as policy owners will be eager to over-dramatize the impact to collect. This conflict naturally leads to more lawsuits.

Recently, the first District Court of Appeal in Florida ruled on a sinkhole case stating that property insurers cannot limit sinkhole loss coverage to less than the dwelling coverage limit set by the Office of Insurance Regulation. Where does "loss" enter into the debate between "cosmetic" and "structural?"

The Concept Is Clearly Unclear

Sinkholes are not solely a Florida problem — nor are hurricanes or the myriad of situations that cause property damage. Property damage is often weather-related but can ensue for a number of reasons — vandalism, pure accident, as well as age and neglect. The current cosmetic exclusion is geared toward damage from wind and hail — all climate issues. That, too could change.

The endorsements from the AAIS and ISO governing the cosmetic damage exclusion are still considered optional, so the full picture has yet to be seen.

The resulting situation is ripe for the discussion and certainly provides a wide opening to see a rise in first-party property lawsuits.

About Jason Wolf

Wolf is a shareholder at the Fla.-based firm of Koch Parafinczuk & Wolf. His practice focuses on first-party property insurance defense, and he is the firm's partner overseeing all lawsuits against property insurers.