



# NATURAL DISASTERS & INVERSE CONDEMNATION

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# OVERVIEW

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- ▶ Inverse Condemnation
- ▶ Natural Disaster Inverse Claims
- ▶ Cost Recovery at CPUC
- ▶ Legislation
- ▶ Insurance Solutions

# INVERSE CONDEMNATION

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- ▶ California Constitution, Article I, Section 19, reads:  
*“Private property may be taken or damaged for a public use and only when just compensation ...has first been paid to...the owner.”*
- ▶ If a public agency damages property *“for a public use,”* then it owes the owner compensation (damages).
- ▶ Also applies to private & municipal utilities.

# INVERSE CONDEMNATION *(continued)*

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- ▶ **Strict Liability**

A public entity is liable for property damage substantially caused by a public improvement, regardless of foreseeability or fault.

- ▶ **Policy**

These public improvement costs should be spread among those benefited (taxpayers) rather than allocated to a single community member – the claimant or property owner.

# CALIFORNIA vs OTHER STATES

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- ▶ California is one of the only states in which courts have applied inverse condemnation to events caused by utility equipment.
- ▶ If a utility's equipment is found to have been a substantial cause of the damage – even if the utility has followed established inspection and safety rules – the utility may still be liable.

# CAUSATION – The Only (Narrow) Defense

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- ▶ Claimant must show public improvement was a “*substantial cause*” of damage.
- ▶ Public improvement is not a substantial cause where damage would have occurred even it had operated perfectly.
- ▶ Even where an independent force (e.g., wildfire) contributes to the damage, liability exists if the injury occurred in substantial part because the public improvement failed to function as it was intended.

# OTHER POSSIBLE DEFENSES

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- ▶ Statutory (government) immunities from liability generally not applicable in inverse condemnation claims.
- ▶ The CPUC's safe harbor against liability for water utilities that meet its water quality and other standards (known as Hartwell) has not been tested in an inverse condemnation case.

# RECOVERABLE DAMAGES

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- ▶ Present & prospective damages
  - Cost of repairs
  - Loss of use of real & personal property
  - Lost profits & prospective profits
  - Increased operating expenses
- ▶ Claimant's attorneys' fees, expert fees & other litigation costs



# NATURAL DISASTER INVERSE CLAIMS

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- ▶ In one superior court case (not citable / published), a water utility was found liable in inverse condemnation where its water pumping station failed to operate properly and resulted in fire fighters being unable to prevent several homes from being damaged.
- ▶ Other water utilities being sued for failure of hydrants due to low water pressure (no backup power generators) in California fires.
- ▶ Liability exception for flood control situations.

# COST RECOVERY at CPUC

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- ▶ Court finding of inverse condemnation liability is not controlling as to whether CPUC allows a private utility to recover its costs from customers.
- ▶ Private utilities' recovery of legal and other operational costs subject to CPUC reasonableness review.
- ▶ Municipal utilities pass these costs on to customers in higher rates without any such review.

## COST RECOVERY at CPUC *(continued)*

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- ▶ CPUC disallowed SDG&E \$379 million in costs from 2007 fires.
- ▶ Reasoning was that SDG&E failed to establish that it reasonably managed and operated its facilities prior to fires.
- ▶ SDG&E lost in Court.
- ▶ Implications for other private utilities.

## LEGISLATION – Senate Bill 901 Signed into Law 9/21/18

- ▶ More flexible CPUC standard for recovery of future (2019) wildfire costs by private electric utilities.
- ▶ Private electric utilities may potentially issue bonds to finance 2017 wildfire liability costs over time (to be paid by customers).
- ▶ Increased penalties for all private utilities for violating CPUC orders or rules (\$100k/day).
- ▶ Additional funding to CalFire for wildfire mitigation.

# LEGISLATION – Concepts

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- ▶ No deliberate design & construction to combat wildfires.
- ▶ No inverse liability if:
  - Water utility unable to provide sufficient water supply / pressure to combat wildfire or facilities damaged due to wildfire.
  - Water utility meets flood control reasonableness standard.

# INSURANCE SOLUTIONS

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- ▶ Are takings insurable?
  - Yes = inverse condemnation
  - No = eminent domain
- ▶ Which policy is best equipped to cover inverse condemnation?
  - General Liability or
  - Directors & Officers Liability
- ▶ What are the differences?
  - General Liability: negligence via property damage
  - Directors & Officers Liability: wrongful acts via economic injury

# INSURANCE SOLUTIONS *(continued)*

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## ▶ Takings Recap

- Inverse condemnation is a constitutional violation of the federal and state takings clause
- Unlawful takings are deemed wrongful acts based on the powers, policies & decisions of governing body
- An unlawful taking without just compensation is economic injury and not property damage

## ▶ Policy Answer

- Directors & Officers Liability
- Covers wrongful acts of governing body
- Economic injury is the damage trigger
- Inverse condemnation requires coverage affirmation

# PLACEMENT CONSIDERATIONS

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- ▶ Importance of written affirmation
  - Conflicting policy exclusions
  - Overlapping causes of action
  - Codifies insurance provider intent
  - Silence does not equate to coverage
  
- ▶ Impact of policy provisions
  - Limits & defense costs
  - Loss trigger
  - Manifestation
  - Occurrence or claims made



# PLACEMENT CONSIDERATIONS *(continued)*

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- ▶ Coverage restrictions to avoid
  - Negligence only
  - Property damage only
  - No attachment of claimant's attorneys' fees, expert fees & other litigation costs
  - No deliberate takings
  
- ▶ Insurance provider selection
  - Legal theory fluency
  - Experienced defense panel
  - Articulation of coverage starting & stopping points
  - Water utility track record

# INSURANCE TAKEAWAYS

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- ▶ Directors & Officers Liability can be structured to include inverse condemnation coverage.
- ▶ Requires written affirmation of inverse condemnation in policy to confirm insurance provider intent.
- ▶ Secure clarification of all coverage restrictions.
- ▶ Understand your policy provisions.
- ▶ Select an insurance provider with demonstrable legal theory fluency, segment expertise & knowledgeable defense panel.

# QUESTIONS?

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