

'Experience is the name we give to our mistakes!' – Oscar Wilde

Sewer Backup Coverage: The case for risk aversion and restraint

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Editor's Note: This topic will be among sessions offered at the upcoming Midwinter Conference in Lincoln, Feb. 23-24.

Peter Senge's internationally best-selling business book, *The Fifth Discipline*, contains an illustration about systems thinking entitled "The Beer Game," which graphically illustrates a complicated chain of interactions involving brewing, warehousing, shipping and selling beer. Senge says the Beer Game "shows how rational individuals that are part of a system but that act in isolation can get trapped in problems related to their own thinking and behaviors." At any place in the relational chain, such isolation can disrupt efficient, on-time delivery of beer to customers. The Beer Game is an appropriate metaphor for other complex systems, including just about any public function that involves facilities, staffing, customer service, billing, or maintenance, where any interruption in system workings can upset customers.

Old collection systems

For instance, not unlike the beer buyer who simply purchases a favorite beverage without thinking of prior manufacturing and distribution, typical municipal sewer customers seldom consider collection and treatment processes that occur subsequently to



Dennis Watts, Sewer/Water Director, City of Norfolk

flushing the toilet. In many small municipalities, collection systems are old and defective; sewer maintenance is nonexistent, therefore, insurance underwriting is inexact. Sewers installed many years ago were clay pipe or cast iron.

Replaced with PVC

As these sewers have worn out, utilities have replaced many of them with PVC. Old remaining pipes in many instances are vulnerable to inflow and infiltration problems, which during rain accumulations, can result in sewer backups. These are reasons commercial and homeowner insurers normally provide coverage with low coverage limits and high deductibles.

Inflow and infiltration are not only problematic for an affected municipality and insurer; when multiple



Mike Forster, Executive, Michigan Municipal League Liability and Property Pool

communities cooperate interlocally by contracting with a regional wastewater treatment facility, deferred maintenance in upstream collection systems can converge into the downstream interceptor sewers and accentuate possible backups and potential litigation. If weather patterns are erratic and rainfall is intense, the regional wastewater treatment provider and its insurer can become susceptible to "deep pocket" liability that may result.

Poster child

The Michigan Municipal League Liability and Property Pool is inarguably the poster child for such litigation. Historically, the pool had provided full insurance limits, including sewer backup coverage up to \$10 million. The pool experienced on-average 150

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to 200 minor claims annually and denied coverage successfully in most cases. Total incurred losses averaged typically \$250,000 to \$300,000 per year. Then between 1996 and 2000, recurrent rain inundations upended the continuity and provoked multiple class action lawsuits by hundreds of residents of several suburban communities near Detroit.

During that interval, the consequences to the Michigan pool were anything but foreseeable. Sewer backup claims exceeded \$25 million. Municipal leaders and judges susceptible to judicial retention often advocated for plaintiffs. Pool investigative and defense costs became exorbitant. Determining dates of loss and whether storms were a single occurrence or multiple events were often challenging. Flooding claims tended to cause fraud. Sewer coverage created adverse selection quarrels from members who had not purchased sewer coverage and were annoyed at having to defend and pay claims of members who had obtained coverage.

Class action suites

Within a few years, according to pool executive Mike Forster, class action suits threatened to force the Michigan Pool into insolvency. The pool dropped from \$17 million in surplus on \$25 million in annual premium to almost zero. Recounts Forster, "The problem was that the courts were not going to dismiss these claims, no matter what the law said (regarding negligence), no matter the circumstances. If it was a 500 year storm – it didn't matter. The courts were not going to dismiss those claims; they were going to at least allow them to get to

a jury.... We were forced to limiting coverage or go insolvent."

The Michigan Pool responded effectively to the grim situation by lowering coverage limits to a maximum of \$100,000 per occurrence (and aggregate), with a zero deductible. Sewer back up coverage is now provided only to members who pre-qualify with underwriting and premiums must pay for losses. The pool, however, provides claims advice on handling, regardless of coverage and attempts to pay claims involving individual homeowners or when legal responsibility is unclear.

Extraordinarily successful

Mike Forster says that the results have been extraordinarily successful. Class action and multiple claimant lawsuits have decreased dramatically from reduced availability to access insurance dollars. The vast majority of new sewer backup claims are covered by the new sublimit, and pool members as a whole are satisfied that they are not paying increased premiums

to cover ongoing sewer problems of a small number of other municipalities. Nearly all other Michigan carriers and insurers have copied the Michigan Pool's decision by limiting their sewer coverage to varying degrees.

Rates have stabilized

"Since 2000," Forster says, "pool surplus has grown to \$54 million on \$19 million in premium, rates have stabilized and over \$10 million in dividends have been returned to members."

Notwithstanding the Michigan Pool's successful corrective strategy, the trial lawyers who represented the class action plaintiffs continue today to market themselves as legal experts for "victims" of sewer backup. Their website is telling. (See this link: <http://mldclassaction.com/why-do-sewage-backups-happen/#sthash.kU94awnm.dpu>) Noting that sewer backups are typically caused by either inflow and infiltration, utility pump failures,

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City of Norfolk sewer jet vacuum truck

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debris and improper maintenance, these litigators observe, “To ensure that such maintenance issues do not arise, it is important that the governmental agency charged with operating the sewer system engages in regular cleaning and/or maintenance of the sewer system. Unfortunately, most governmental agencies do not even have written procedures regulating the maintenance of their sewer system.”

Vulnerability criteria

In other words, lack of written procedures and documented maintenance are among vulnerability criteria used by these attorneys when conducting discovery against municipal sewer providers. The plaintiff attorneys conclude: *(M)ost governmental agencies faced with a claim of damages arising from a sewage backup will state that the backup occurred due to unforeseen circumstances such as an unusual rain event, pump failure or some form of obstruction. These claims do not automatically relieve the defendant of liability.... Governmental entities faced with claims for damages arising from sewage backups typically respond to such claims by issuance of a form letter outlining the severity of the rain event and the complexity of the sewer system.... These letters are submitted in an attempt to bully and/or intimidate the victim of a sewage backup into accepting the governmental agency's assertion that it is not responsible for the sewage backup and/or it would be too difficult for the homeowner to prevail. Do not be intimidated by these letters. Feel free to contact us for a free consultation regarding any such claim. In most cases litigated by this office, common sense ultimately prevails. Putting aside the law, from a common sense point of view, should a homeowner ... in the United States of America be required*

to accept the presence of raw, untreated sewage in his home. The answer is clearly no. Throughout Michigan's ordeal LARM's Board and staff were paying attention. Several Board members expressed concern about the number of LARM sewer claims and discussed ways to reduce them through exclusion of coverage and loss control, including education about backflow preventers, riders on home insurance policies and deductibles for members who wanted sewer backup coverage.

Coverage excluded

On April 16, 2004, the LARM Board excluded coverage of all backups from sanitary sewers, storm sewers and rises in ground water level, excluded inverse condemnation, and provided members with lower limits of sewer backup coverage for an additional charge and minimum deductible. Coverage was made conditional on the member implementing a written maintenance policy acceptable to the underwriter. LARM's current sanitary sewer backup endorsement was approved by the Board, effective Oct. 1, 2004. LARM's two coverage options with limits of liability for bodily injury and property damage arising from the backing up of sanitary sewers and any loss related thereto, are (1) \$5,000 per building and \$25,000 per occurrence or (2) \$15,000 and \$75,000 per occurrence. Between 2004 and 2014, LARM's revised sewer backup coverage created the following remarkable results:

Withdrawn claim	1	
Dismissed claims	1	
Denied claims	42	
Paid claims	7	\$52,467
Settled claims	2	\$19,500

On several past occasions during bidding competition, LARM's private insurance contestants alleged to elected officials that private insurers provide their customers with better sewer backup coverage than LARM. LARM representatives responded, “The real proof is whether our competitors pay or deny claims!” Customarily, when the private insurers were challenged to disclose particular claims information, the information was not forthcoming, and the outcome of the bidding was not affected by any differences in sewer coverage.

Recent rain storm

During a recent rain storm impacting one of LARM's member communities, a private contractor working on a state construction project attempted to deny a claim that involved a sewer backup. The private contractor was insured by one of LARM's competitors who initially contended that the contractor had not been negligent. However, photographs taken during the flooding by homeowners and municipal employees were later provided to LARM's adjusters and the competing insurer's adjusters. The photos proved that during the storm, the private contractor had neglected to cover manholes properly; therefore the competing insurer relented and paid the claim. In conversations between LARM and the private insurer representatives, the word “subrogation” was used, which may have been a motivating factor in payment of the claim.

All the foregoing said, LARM implemented the strategy of lower limits with a higher deductible to protect LARM members at large from the unpredictability of severe sewer backups affecting

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a few members. LARM continues to encourage and recognize the importance of good loss control with effective sewer maintenance. One of LARM's customers sets the bar for best practices in sewer maintenance.

Maintenance program

Norfolk's Water and Sewer Maintenance Director Dennis Watts indicates that Norfolk's annual sewer maintenance program includes all residential sewers and interceptors. Between April and November sewers are cleaned with a high pressure jet and vacuum combination truck, which is jointly purchased with the Street Division and is also used for storm sewer maintenance.

Each of Norfolk's sanitary sewer sections is flushed from manhole to manhole. Once enough material is collected in the manhole, maintenance crews vacuum the material out. Footage cleaned between manholes, the date and operator, and any deficiencies are recorded. Certain low areas of the collection system are inspected quarterly, monthly and weekly, and the inspections are recorded. Water and sewer crews have purchased inexpensive camera systems that are affixed to Styrofoam floats and used to inspect and video the sewer mains when needed. Norfolk's 14 lift stations are physically inspected, Monday and Thursday of each week. Operation of the pumps, stations alarms and system controls are checked for proper operation. Two portable generators are available to use at the lift stations in the event of a power outage.

Norfolk has adopted the International Code Council's model building code that requires backflow prevention technology in all new construc-

tion. If a structure needs to replace the existing sewer service line, owners are required to install a backflow protection device. Norfolk encourages existing homeowners to retrofit the technology in their residences.

Drain campaign

Additionally, Norfolk recently developed a "Drain Campaign" to inform citizens to not clog drains with paper, objects or grease. The program involves press releases, public posters, as well as staff presentations to public and parochial school children, parents and civic groups about how grease, paper towels, wipes, feminine products, prescription drugs and leftover cleaning supplies can plug sewers and the consequential cost to homeowners and the municipality.

Norfolk's sewer maintenance program represents exceptional attention-to-detail that defense attorneys value because good management is always the best mitigation against lawsuits.

While smaller municipalities may be unable to fund their own equipment and staff for sewer maintenance and code enforcement, many private contractors are available throughout Nebraska to provide these services to small communities. Also, the Interlocal Cooperation Act is an additional option that authorizes smaller municipalities to contract with other local government subdivisions for these services.

Good risk management

Good risk management is fundamentally about good management. By excluding sewer backups from general liability coverage and affording coverage by endorsement at low limits and high deductibles, the LARM Board understood that the effect would be to foster good management of sewer collection systems and maintenance. Accordingly, improved loss control reduced claims and premium savings have resulted. ■



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