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A Unique Storm Spawns Unique Insurance Issues

In Hurricane Matthew's aftermath, lessons from Superstorm Sandy

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While the Southeast United States escaped the worst of feared damage from Hurricane Matthew, the storm did take more than 40 lives in the U.S. and cause extensive power outages, flooded roads and dams, and damage to buildings from Florida to Virginia. It also triggered mass evacuations and closures by order of civil authorities.

In the run-up to a storm, it is customary for insurance executives to appear on newscasts assuring the public that they will take care of things. It is vital for businesses, however, not to assume that their insurance claims will proceed to full recovery without their constant vigilance. Storm-related claims can run into a snarl of unclear policy provisions, sublimits and exclusions, and occasionally obstreperous insurance company adjusters.

Job one for policyholders is to understand the full range of coverage offered by most business property insurance policies – and the nuances of their own policies. As businesses prepare to file claims, they would do well to take note of the coverage issues and disputes that emerged and have been litigated in the wake of Superstorm Sandy, which ravaged the Northeast in October 2012.

The devastation left in the wake of Superstorm Sandy was unprecedented in the region. There were widespread power outages affecting approximately 8.5 million customers. In anticipation of the storm, governors and other officials declared states of emergency and issued mandatory evacuation orders. Major highways, bridges and public transportation were closed in New York, New Jersey and other areas. Sandy has been called the worst disaster in the 108-year history of the New York Metropolitan Transportation Authority.

Insurance coverage litigation over Sandy-related claims frequently hinged on issues like the application of sublimits for floods, windstorms (including storm surges) and named storms; disputes over damage caused by "wind versus water"; and coverage for lost revenue due to orders of civil authority and service interruptions. Four years later, numerous Sandy coverage cases continue to wind their way through the courts. The physical damage and business income losses caused by Matthew may lead to similar coverage disputes regarding these same issues.

The insurance claims arising from Matthew are also likely to include significant losses that trigger extensions of coverage commonly found in most commercial property insurance policies – like business interruption coverage, contingent business coverage, ingress/egress coverage and civil authority coverage. Policyholders that understand the full range of their coverage options – as well as the lessons of Superstorm Sandy – will be best positioned to maximize their insurance recoveries.

> *It's no surprise that a storm as massive and unique as Sandy has given rise to unique and complex insurance coverage issues.*

Knowing Your Sublimits

Following Sandy, many policyholders found themselves in disputes with their insurance companies over sublimits that stood to drastically reduce their coverage for water damage from the storm. Many policyholders with multimillion dollar losses were told by their insurance companies that their losses were capped by a "flood" sublimit, even though a careful review of the entire insurance contract and the facts surrounding the loss revealed that a different sublimit – or no sublimit – applied. For example, some policies make a distinction between losses caused by "flood" and losses caused by "storm surge." From a risk assessment and insurance pricing perspective, this distinction makes sense. Because the weather conditions that result in the overflow of a lake or river (typically, heavy rainfall or rapid snow melt) are very different from the forces that drive storm surge ashore (typically, large coastal windstorms), insurance companies generally model the risks of these different types of losses separately and set premium rates based on these separate assessments. Consistent with this underwriting approach, many commercial property insurance policies include separate definitions of "flood" and "windstorm," with "storm surge" included in either one or the other definition.

Often, the sublimits for flood losses are much lower than the sublimits for windstorm losses. So, when Sandy's storm surge inundated many commercial properties, policyholders whose policies clearly categorized the loss as

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a "windstorm" loss generally fared better than those whose policies defined "flood" to include "storm surge." See *Public Service Enterprise Group, Inc. v. ACE American Ins. Co., et al.*, No. ESX-L-4951-13, 2015 N.J. Super. Unpub. LEXIS 620 (N.J. Law Div. Mar. 23, 2015); see also *Pinnacle Entertainment, Inc. v. Allianz Global Risks U.S. Ins. Co.*, 2:06-CV-00935-BES-PAL, 2008 U.S. Dist. LEXIS 108583 (D. Nev. Mar. 26, 2008). "Other Sandy storm surge victims had policies with 'flood' definitions that did not include 'storm surge' or 'wind-driven water' but still had the loss characterized as a 'flood' – subject to a flood sublimit." See *National R.R. Passenger Corp. v. Arch Specialty Ins. Co., et al.*, 124 F. Supp. 3d 264 (S.D.N.Y. 2016); see also *In re Katrina Canal Breaches Litig.*, 495 F.3d 191 (5th Cir. 2007); *Leonard v. Nationwide Mut. Ins. Co.*, 499 F.3d 419 (5th Cir. 2007). Accordingly, a careful review of all policy provisions and potentially applicable sublimits and definitions is critical when evaluating losses caused by storm surge – like the coastal losses caused by Matthew.

Civil Authority Coverage

Many businesses that did not suffer property damage at their insured locations due to Superstorm Sandy did nonetheless suffer a loss of business income as a result of the storm. While "standard" business interruption coverage would not apply under such circumstances, other time element coverages, such as "civil authority" coverage, may apply. Civil authority coverage typically is triggered where access to the insured premises is prohibited, prevented or impaired by the action/order of a civil authority, such as a city's mayor. While direct physical loss or damage due to a covered cause of loss is still required in order to trigger civil authority coverage, that loss or damage can occur away from the insured premises, and the damaged property need not be owned by the insured. However, policyholders who do not have flood coverage may not be able to take advantage of an order of civil authority if the order to vacate was related solely to flooding and not also to concerns about wind damage. Nonspecific orders can lead to coverage disputes.

Executive orders in New York City have given rise to some disputes regarding the period of time for which insurance companies will cover civil authority losses. Some insurance companies have argued that coverage should be terminated at the time of former Mayor Bloomberg's Executive Order 165, which permitted reoccupation of premises in Lower Manhattan only after the Buildings Department certified it was safe to do so. In many cases, however, policyholders were not permitted to reoccupy their premises for weeks and even months after Executive Order 165 was issued. The theoretical time in which such policyholders could have reoccupied their premises had the Buildings Department allowed it should have little bearing on the insurance companies' obligations to pay civil authority claims for the actual period those policyholders were forced to vacate their premises (as long as the order was related to a covered cause of loss).

In other cities, evacuated policyholders are facing challenges proving orders of evacuation. In those areas, local police made rounds forcing those in harm's way to evacuate. With no written record of the evacuation order, policyholders are resorting to obtaining affidavits from local authorities concerning the forced evacuations in order to trigger civil authority coverage.

Matthew also resulted in widespread evacuation orders up and down the Southeastern Seaboard. Businesses of all sorts that suffered lost revenue from such orders would be wise to review their insurance policies to assess the coverage provided for such losses under the civil authority coverage provisions.

Service Interruption Coverage

Another form of "off premises" time element coverage relied on by many businesses in the wake of Superstorm Sandy is known as service interruption coverage. This covers business interruption losses resulting from damage to personal property of a utility necessary for supplying the insured premises with things such as power, water, communication, natural gas, sewage and Internet access. Typically, the property damage at the utility must be caused by a covered cause of loss under the policy.

In some areas of New York City and other locations affected by Sandy, certain utilities preemptively shut down power in order to preserve the integrity of the electrical system during the storm. While there is little authority on the subject, there is some support that a shutdown of this nature constitutes a covered event under a property insurance policy. See *Wakefern Food Corp. v. LibertyMut. Fire Ins. Co.*, 406 N.J. Super. 524, 540, 968 A.2d 724, 734 (App. Div. 2009) (a blackout case holding that a power plant's inability to perform its essential function of providing electricity constitutes "physical loss or damage" for purposes of coverage under a property insurance policy). Some insurance companies, however, challenged coverage. Similar fights may be in store for policyholders as they attempt to recover from Matthew. Certainly, where power outages and other service interruptions caused lost business income, service interruption coverage should be considered and pursued by policyholders as part of their post-Matthew recovery plan.

Business Interruption and Contingent Business Interruption

Business interruption (BI) coverage covers businesses for losses stemming from unavoidable interruptions in their daily operations. BI coverage may be triggered by circumstances including a forced shutdown, a downturn in business due to damage to the premises, or a substantial impairment in access to a business's plant or premises.

Businesses that are not themselves forced to close may be able to use contingent business interruption coverage, triggered when policyholders do not themselves suffer physical damage but still lose revenue after a property loss sidelines a major supplier or customer base. Contingent BI is a standard provision in many property insurance policies, though many small businesses are not aware of it.

Calculating the full range of business income loss from property damage, disruption to the surrounding area, and closures by order of civil authority is a complex task. The more thorough the documentation, the more likely the policyholder is to win full or near-full acceptance of the claim from the insurance company – or, if necessary, to push back against the insurance company's more limited estimates or even denial of the claim. To that purpose, the services of a public adjuster, skilled in the ways insurance companies calculate loss, can be invaluable.

It should hardly come as a surprise that a storm as massive and unique as Sandy has given rise to unique and complex insurance coverage issues. Some claimants negotiated these issues behind the scenes and out of the courts, while other claimants, typically those with more substantial losses, have been forced to bring suit to have these and other issues resolved. Policyholders seeking coverage for losses stemming from Hurricane Matthew are well advised to take this history into account and to understand the full range of their coverage options when filing their own claims – and if necessary, when responding to coverage defenses invoked against them by their insurance companies.