AKO POLICYHOLDER ADVISOR

The Policyholder Law Firm

Volume 10 Number 2 www.andersonkill.com February 2001

Insurance Coverage For Power Interruptions— In California and Elsewhere

Rhonda D. Orin
Michele A. Gallagher
Robert M. Horkovich

Power interruptions could impact you wherever you are. As California's utilities hover on the brink of bankruptcy, California businesses in particular face rolling blackouts, brownouts and other "service interruptions." These power disruptions, occurring with at most a one-half hour warning, may spell serious problems for many businesses in California and elsewhere. Imagine, for example, that you're a large dairy with thousands of gallons of milk needing constant refrigeration. Or that you're a semiconductor manufacturer with hundreds of silicon wafers in mid-production in your "clean room." If the electric utilities flip the switch on you, you stand to lose and to lose big. That's the bad news.

The good news is that you already may have insurance to cover your losses. Your property insurance, specifically your business interruption insurance, should provide coverage.

Your Property Insurance Policies May Cover Your Loss

Property policies can cover policyholders for damages suffered as a result of damage to both tangible and intangible property. Tangible property runs the gamut from items in production to inventory to business records. Intangible property includes anticipated profits and income.

Under most property policies, the insurance company promises to pay for financial loss caused by direct physical damage to insured property or loss of use of insured property. Most property policies cover losses to inventory that businesses suffer as a result of power interruptions.

Your Business Interruption Insurance Is A Likely Source of Coverage

One specific type of property insurance likely to afford coverage to businesses affected by power interruptions is "Business Interruption" insurance. Business Interruption, or BI, insurance is designed to protect policyholders who have to suspend their business or production, resulting in lost sales and loss of profits. It also should reimburse policyholders for expenses that continue despite the cessation of income, such as salaries, taxes, rent, professional fees, certain utility charges and insurance premiums. BI insurance is intended to do financially for the policyholder just what the business would have done had the interruption not occurred.

While specific policies differ, BI insurance generally provides coverage when there is: (1) loss; (2) resulting from business interruption; (3) caused by direct physical loss of, or damage to, property or loss of use of insured property; (4) caused by a covered peril. BI insurance should cover business interruption losses caused by the power interruptions in California and elsewhere.

Indeed, a federal court in Arizona recently confirmed business interruption insurance coverage where a power outage caused a policyholder's mainframe computers to lose information. The court recognized coverage for the substantial lost business. *Am. Guar. & Liab. Ins. Co. v. Ingram Micro Inc.*, 2000 WL 726789 (D. Ariz. Apr. 18, 2000), *appeal dism'd*, No. 00-80913 (9th Cir. Aug. 14, 2000). The court rejected the insurance company's argument that there was no "physical damage" to the policyholder's property because the computers could be reprogrammed and functionality restored. The court ruled that loss of use and functionality of the computer system for a period of time constituted covered "physical damage" under the policy.

In addition to coverage for loss of inventory or loss of use, business interruption insurance often provides coverage for "Extra Expenses", defined as:

> The excess of the total cost during the policy period of restoration of the damaged property chargeable to the operation of the Insured's business over and above the total cost that would normally have been incurred to conduct the business during the same period had no loss occurred.

This provides coverage for all necessary emergency expenses incurred, over and above ordinary fixed operating costs, to continue as nearly as possible the normal conduct of the policyholder's business. Among other things, these expenses may include the cost of paying for emergency generators or alternative power sources, extra compensation to employees, additional rent at a temporary location, and other miscellaneous costs in connection with the reopening of business.

One critical caveat—policyholders entitled to coverage under their business interruption insurance might have to take steps to minimize their losses. Business interruption policies sometimes expressly provide:

It is a condition of this insurance that if the Insured could reduce the loss resulting from the interruption of business.

A. by complete or partial resumption of operation of property herein described, whether damaged or not, or

B. by making use of merchandise or other property, at the location(s) described herein or elsewhere,

Such reduction shall be take into account in arriving at the amount of loss hereunder.

If the policy contains this express condition, a policyholder's recovery may be reduced if the policyholder fails to reduce its losses.

What You Should Do if An Energy Interruption Causes You A Loss:

1. Take Immediate Steps To Minimize Your Damages. As noted, your insurance policies might expressly condition your recovery on your taking steps to minimize your loss.

2. Locate and Read Your Policies. Getting your coverage depends on knowing your coverage. Many different types of property insurance policies contain coverage for your loss. Know your coverage and know who sold it to you.

3. Give Notice of Your Claim or Loss As Soon As Possible. Timely notice is a requirement under most insurance policies. Too frequently, policyholders forget to notify their insurance companies. If you have a loss, notify your insurance agent or broker and your insurance company as soon as possible.

4. When You Make A Claim, Don't Take "No" for An Answer. Insurance companies routinely deny claims, even if they ultimately have no basis for doing so. Be persistent—the difference between coverage and non-coverage often is directly related to the determination and persistence of the policyholder. ■

THE WRITERS ARE FROM ANDERSON KILL & OLICK, A NATIONAL FIRM REPRESENTING POLICYHOLDERS IN INSURANCE COVERAGE DISPUTES. RHONDA ORIN IS A PARTNER AND MICHELE GALLAGHER IS AN ASSOCIATE IN THE WASHINGTON, D.C. OFFICE. ROBERT HORKOVICH IS A PARTNER IN THE NEW YORK OFFICE. RHONDA ORIN CAN BE REACHED AT (202) 218-0049 OR **rorin@andersonkill.com**. MICHELE GALLAGHER CAN BE REACHED AT: (202) 218-0046 OR **mgallagher@andersonkill.com**. ROBERT HORKOVICH CAN BE REACHED AT: (212) 278-1322 OR **rhorkovich@andersonkill.com**.