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Advanced Business Interruption Time Element Coverages

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Remember that time is money.¹

— Ben Franklin

I. INTRODUCTION

Perhaps now more than ever, companies face a host of risks that can impact their business. When they occur, some of these events do no more than slight damage, with minimal impact. Others do more, resulting in substantial impairment. Occasionally, such events may even cause a complete cessation of business, either temporarily or permanently. Of these risks, some are natural disasters such as floods, hurricanes, or earthquakes and others are the consequence of human activity, such as terrorism, arson, theft, or even simple negligence. Lastly, some losses involve a combination of both, such as a loss caused by a hurricane but exacerbated by inadequate or defective construction methods.

II. BUSINESS INTERRUPTION AND TIME ELEMENT COVERAGES – THE BASICS

This paper, along with the accompanying presentation, will attempt to provide a basic overview of some of the key insurance issues concerning coverage for business interruption and time element losses. To adequately cover these topics in-depth would require a multi-volume treatise.² Nevertheless, it can hopefully serve as a useful starting point on a handful of these complex issues. Accordingly, what follows below is designed to provide a basic treatment of various subjects concerning coverage for time element losses, and where possible, an attempt is made to illustrate some of these concepts with cases from Texas and other jurisdictions as well.

There are numerous types of policies that provide protection to businesses. To begin with, a commercial property policy is usually a good starting point for protecting the real and personal property used by the insured in its business activities, as well as the revenue streams generated by those assets.³ In addition to the basic insuring agreements, such policies often contain “extensions of coverage” that provide coverage for specific items, such as valuable papers, debris removal, expediting expense, and other soft costs. As the scope of coverage can vary from one policy to the next, insureds should carefully examine potential policies for

¹ Benjamin Franklin, *Advice to a Young Tradesman* (1748).

² Fortunately, several such treatises already exist. Although many include treatment of various topics of property coverage, two in particular are cited here as references of first resort on such issues. For a treatise focusing exclusively on property insurance, see STEPHEN A. COZEN, *INSURING REAL PROPERTY* (2d ed. 2002). Of course, for sheer breadth of subject matter on all matters of insurance coverage, it is difficult to find an equal to LEE R. RUSS & THOMAS F. SEGALLA, *COUCH ON INSURANCE* (3d ed. 2000). This characterization holds true with respect to the property context as well, as the property coverage sections of *COUCH* encompass more than fifteen chapters spread among three volumes. Finally, a new treatise focusing exclusively on insurance for natural and man-made catastrophes exists. See JOHN K. DIMUGNO, ET AL., *CAT CLAIMS: INSURANCE COVERAGE FOR NATURAL & MAN-MADE DISASTERS* (1st ed. 2008).

³ But this is often just a starting point, and standing alone, it may not provide complete protection for the insured. Other more specialized forms of coverage may also be necessary in order to obtain more comprehensive coverage of risks to the insured’s business. Depending on the individual circumstances, an insured might need other forms of coverage to protect certain assets such as ships, aircraft or other less common forms of property.

individualized risks. Time element coverage is so important that, depending on the facts, having adequate protection might mean the difference between a (relatively) smooth resumption of operations and no resumption at all. Before moving on, however, it is worthwhile to consider the words of one court:

Few generalizations about business interruption endorsements can be made, however, because the nature of the coverage varies widely. In any given case, the particular terms and conditions of the policy in question must be examined to determine whether a specific business interruption loss falls within the scope of the coverage.⁴

Not only is this useful advice for the practitioner, it also explains why business interruption cases often turn on nothing more than an analysis of the policy language, with little or no citation to other case law in support of a given holding.⁵

A. Business Interruption Coverage

Apart from protecting against losses to the insured's property, protection against impairment of the company's income is also vitally important. Known as "business interruption" coverage, this type of coverage does not protect against physical damage to any property. Rather, it is designed to provide protection to the insured from disruptions in business due to other covered perils that damage the insured's property.⁶ In effect, this coverage supplements the insured's lost income while its property is being repaired, rebuilt or replaced. Stated differently:

[T]he purpose of a business interruption policy is to indemnify the insured for loss caused by the interruption of a going business due to the destruction of the building, plant or parts thereof.⁷

Although actual policy language can vary, mere "slowdown" in productivity is typically not enough to trigger business interruption losses. For example, the policy in *Quality Oilfield* provided coverage for:

[L]oss resulting directly from the necessary interruption of business caused by damage to or destruction of real or personal property. . . ."⁸

The insured suffered a theft loss of critical data and engineering drawings that reduced its ability to perform its operations. Because the policy did not define "interruption of business," the court had to determine whether a mere "work slowdown" was enough or if an actual "suspension of

⁴ *Prot. Mut. Ins. Co. v. Mitsubishi Silicon Am. Corp.*, 992 P.2d 479, 481 (Or. Ct. App. 1999).

⁵ See, e.g. *Snelling & Snelling, Inc. v. Fed. Ins. Co.*, 2005 WL 2767610 (N.D. Tex. Oct. 25, 2005)(citing only cases for the summary judgment standard, choice of law, and the rules of contract construction).

⁶ Or property central to the insured's business, even if it is not directly owned by the insured. This issue will be discussed in greater detail below.

⁷ *Quality Oilfield Prods., Inc. v. Michigan Mut. Ins. Co.*, 971 S.W.2d 635, 638 (Tex. App.—Houston [14th Dist.] 1998, no pet.)(citation omitted).

⁸ *Id.* at 637.

operations” was required. After stating that it was an issue of first impression for the Texas courts, the court looked to other jurisdictions and ultimately concluded:

[A]fter considering the policy as a whole and persuasive authority from other jurisdictions, we find that “interruption of business” is an unambiguous term meaning “cessation or suspension of business.” Therefore, Quality was not entitled to business interruption coverage for the work slowdown it experienced and we find the trial court did not err in granting Michigan’s motion for summary judgment.⁹

An insured may suffer a loss of income from an event, such as a hurricane, but the loss of income may not be tied to property damage. Business interruption provisions often require a causal connection between the company’s loss of income and covered physical loss or damage. The provision in *Quality Oilfield* is illustrative. It specifically limits coverage for business income loss *caused by damage to or destruction of property*. The “caused by” language creates the requirement that ties the loss of the insured’s income to the damage to property.

The causal connection requirement is particularly important when an event affecting an overall community has a corresponding effect on the insured’s business. For example, in *Southern Hotels Limited Partnership v. Lloyd’s Underwriters at London*,¹⁰ in the wake of Hurricane Andrew and the lack of customers, an insured hotel owner made a claim for loss of income and for damage to air conditioning units, a pool pump, and the telephone system. The insured claimed that the damage made its hotel rooms unavailable for rent. But the insured never turned away a single customer due to the damage allegedly resulting from the hurricane.

The *Southern Hotels* court specifically noted that there was no evidence that “*causally connects* the damage in the rooms to the loss of revenue,” since client demand never exceeded the availability of undamaged rooms.¹¹ It went on to explain that, “[to] state a triable issue for business interruption damages, the plaintiff must show that it lost revenue as a result of damages caused by Hurricane Andrew.”¹² Specifically, the insured must prove “a *causal nexus*” between the damage caused by the hurricane and the business interruption loss.¹³ Because this causation was lacking, no business interruption coverage was found.

⁹ *Id.* at 639. *But see Evans v. LaFayette Ins. Co.*, Civ. No. 06-6783, 2007 WL 4545883 (E.D. La. Dec. 18, 2007) (finding coverage when lawyers from the New Orleans office continued to provide legal services (and produce revenue) at alternative locations following Hurricane Katrina because there was a “complete cessation” of business at the New Orleans office due to damage arising out of Hurricane Katrina).

¹⁰ Civ. A. No. 95-2739, 1996 WL 592732 (E.D. La. Oct. 11, 1996).

¹¹ *Id.* at *2 (emphasis added).

¹² *Id.* at *3

¹³ *Id.* at *4 (emphasis added) (see also *Kean, Miller, Hawthorne, D’Armond McCowan & Jarman, LLP v. Nat’l Fire Ins. Co. of Hartford*, 06-770-C, 2007 WL 2489711 (M.D.La. Aug. 29, 2007) (holding that a direct nexus must exist between the action of the civil authority and the prohibition of access to the insured premises)).

Valuation of business interruption losses are also often the subject of dispute. One recent Texas case illustrates this point. In *Finger Furn. Co., Inc. v. Commonwealth Ins. Co.*,¹⁴ the insured was unable to open several of its furniture stores in the aftermath of Tropical Storm Allison. After the flood, the company re-opened its stores and slashed prices the following weekend, causing a surge in business.¹⁵ The company also filed a business interruption claim for the days while the stores were closed. Using a stipulated value from the prior year's sales for the same period, the dispute turned on whether the insurer could offset the losses against the post-storm surge in sales.¹⁶ Noting that the policy language required that due consideration be given to the "experience of the business before the date of the damage . . . and to the probable experience thereafter had no loss occurred," the court held that the post-storm sales could not be used to determine whether the insured actually suffered a loss. Accordingly, the insured was awarded the full value of its stipulated loss, with no offset against the subsequent sales.¹⁷

There can also be disputes concerning the "period of restoration" of the covered premises. One example of this can be found in *Lava Trading, Inc. v. Hartford Fire Ins. Co.*,¹⁸ where the insured was a tenant of the World Trade Center at the time of the September 11th terrorist attacks. Lava Trading sold computer software programs to facilitate electronic trading. Its primary offices, along with a functioning data center, were on the 83rd floor of One World Trade Center. Approximately one month later, the insured had operational offices at another location. The policy's "period of restoration" was:

[T]he period of time that:

- (a) begins with the date of direct physical loss or damage caused by or resulting from any Covered Cause of Loss at the described premises, and
- (b) ends on the date when the property at the described premises should be repaired, rebuilt or replaced with reasonable speed and similar quality.¹⁹

The main issue was the point at which the "period of restoration" was complete – the insured's replacement of suitable operational space, or the rebuilding of the World Trade Center.²⁰ The court held that the "period of restoration" ended when the insured's property "should have been repaired, rebuilt or replaced with reasonable speed and similar quality." Thus, the date when the

¹⁴ 404 F.3d 312 (5th Cir. 2005). *But cf. Rimkus Consulting Group, Inc. v. Hartford Casualty Ins. Co.*, 552 F.Supp.2d 637 (S.D. Tex. 2007) (holding that post-loss sales increases could be taken into account in determining whether a business interruption loss existed under the particular policy language at issue, discussed further below in section H, *infra*).

¹⁵ *Id.* at 313.

¹⁶ *Id.*

¹⁷ *Id.*

¹⁸ 365 F. Supp. 2d 434 (S.D.N.Y. 2005).

¹⁹ *Id.* at 439.

²⁰ Actually, this case is much more complex than the space constraints of this paper allow. It is therefore suggested that interested readers study the case in more detail to gain a complete understanding of this decision.

insured's offices were functionally replaced marked the end of the restoration period, and not when the World Trade Center's rebuilding is actually complete.²¹

B. Contingent Business Interruption Coverage

When the insured's property is not damaged, but its income is affected by property damage at key suppliers or customers, "contingent business interruption" coverage is crucial. As the Seventh Circuit noted:

Regular business-interruption insurance replaces profits lost as a result of physical damage to the insured's plant or other equipment; contingent business-interruption coverage goes further, protecting the insured against the consequences of suppliers' problems. Regular business-interruption coverage did [Archer Daniels Midland Company] little good in 1993, for the flood largely spared its plants, but contingent business-interruption coverage was just the ticket.²²

A fairly typical contingent business interruption clause states:

This policy covers against loss of earnings and necessary extra expense resulting from necessary interruption of business of the insured caused by damage to or destruction of real or personal property, by the perils insured against under this policy, of any supplier of goods or services which results in the inability of such supplier to supply an insured locations [sic].²³

Note that there is a causation element tying the loss to a covered peril, even though the insured need not have an insurable interest in the property that is damaged. This is a common feature in most time-element coverages because it avoids the problem of theoretically limitless coverage by installing a causative requirement in order for coverage to attach.

C. Extra Expense

It is usually the case that insureds incur extra costs following significant losses. This is where "Extra Expense" coverage comes into play. One example of this coverage is as follows:

²¹ *Id.* at 440-43. See also *In re Cosmetics Plus Group, Ltd.*, 379 B.R. 464, 472, n.7 (S.D. N.Y. 2007) (discussing the numerous cases arising out of 9/11 that discuss period of restoration and its correlation to replacement of the insured's property, rather than property of others).

²² *Archer Daniels Midland Co. v. Hartford Fire Ins. Co.*, 243 F.3d 369, 371 (7th Cir. 2001). Unfortunately for ADM, it later found out that it did not have contingent business interruption coverage for the 1993 flood in the upper Mississippi River basin that inundated approximately eight million acres of farmland and was the single largest flood in the nation's history. The court noted that the company's desire to save \$19,000 in premiums by switching carriers cost ADM \$50 million in uncovered losses, because the replacement insurance it purchased did not cover the contingent business interruption losses ADM sustained as a result of the flood. *Archer Daniels Midland Co.*, 243 F.3d at 370-71.

²³ *Archer-Daniels-Midland Co. v. Phoenix Assur. Co. of New York*, 936 F. Supp. 534, 540 (S.D. Ill. 1996).

This “policy” . . . covers the necessary Extra Expense incurred by the Insured during the “period of restoration” in order to continue as nearly as practicable the “normal” operations of the Insured’s business following a “covered property damage loss.”

In the above policy, “Extra Expense” is defined as:

[T]he excess (if any) of the total cost incurred during the “period of restoration” 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 or damage occurred.

*Travelers Indem. Co. v. Pollard Friendly Ford Co.*²⁴ is a good example of how a Texas court has looked at extra expense coverage. There, the insured suffered damages from a tornado, resulting in a thirteen-day interruption of the insured’s normal business activities.²⁵ The trial court awarded the insured with extra expenses for security, debris removal, employee wages and meals, and temporary storage facilities.²⁶ The Court of Appeals held:

In this case, normal business being impossible for thirteen days, cleaning up the debris, preserving the remains of the operation, and making preparations for reopening for business would appear to be acts “in order to continue as nearly as practicable the normal conduct of insured’s business.”²⁷

Notably, extra expenses must also be tied to specific damage at the insured’s property. In *Lavoi Corp. v. National Fire Ins. of Hartford*,²⁸ a fire destroyed the insured’s newly built Dallas, Texas location. The location was not open at the time of the fire, but its scheduled opening was imminent and the insured had taken orders from Dallas customers. Because the location was not in operation at the time of the fire, the insured did not purchase coverage for business interruption or extra expense at that location. Following the fire, the insured incurred extra costs at its Georgia and Arizona locations including costs for excess freight charges to ship products to the Dallas clients and excess overtime to employ workers in Georgia and Arizona to meet the Dallas clients’ demands. The court found that the policy unambiguously excluded coverage for business interruption and extra expense losses at the Dallas location. Because the insured’s extra expense claim arose from damage at the Dallas location, the court concluded that the insured could not recover damages for expenses incurred at the Georgia and Arizona plants to supply product that could not be produced at the Dallas plant.

²⁴ 512 S.W.2d 375 (Tex. Civ. App.—Amarillo 1974, no writ).

²⁵ *Id.* at 379.

²⁶ *Id.* at 377.

²⁷ *Id.* at 379-80.

²⁸ 666 S.E.2d 387 (Ga. 2008).

D. Civil Authority

Occasionally, governmental authorities prohibit access to certain areas even though not all buildings in the area were damaged. Two recent tragedies are prime examples – the shut-down of lower Manhattan following September 11th, and the evacuation of New Orleans following Hurricane Katrina. “Civil Authority” coverage is designed to protect against losses arising out of orders like these. A typical provision might read something like the following:

The insurance provided . . . is extended to cover the actual loss sustained by the Insured during the length of time . . . when access to “covered locations” is specifically prohibited by order of civil authority, provided such order is a direct result of actual loss or damage from a [covered] peril to property in the vicinity of the “covered locations” to which access is prohibited.

Importantly, this clause has a geographical limitation to the “vicinity of the ‘covered locations.’” Other clauses, however, are broader. In *730 Bienville Partners, Ltd. v. Assurance Co. of Am.*,²⁹ the policy provided:

We will pay for the actual loss of “business income” you sustain and necessary “extra expense” caused by action of civil authority that prohibits access to your premises due to direct physical loss of or damage to property, other than at the “covered premises,” caused by or resulting from any Covered Cause of Loss. This coverage will apply for a period of up to 4 consecutive weeks from the date of that action.³⁰

The insured operated two hotels in New Orleans and sought coverage for business interruption losses under the “Civil Authority” provisions of its policy due to the FAA’s closure of the nation’s airports after September 11. In other words, the insured argued that the lack of flights kept guests from being able to travel to New Orleans and stay in its hotels. The court rejected this argument, concluding:

While the FAA’s closure of the airports and cancellation of flights may have prevented many guests from getting to New Orleans and ultimately to plaintiff’s hotels, the FAA hardly “prohibited” access to the hotels.³¹

Similarly, courts will not enforce Civil Authority provisions when the order precedes property damage or is merely precautionary. For example, in *South Texas Medical Clinics v. CNA Financial Corp.*,³² officials ordered a mandatory evacuation because Hurricane Rita was projected to land in an area near Galveston, Texas. The insured’s medical clinics in Galveston were closed while the evacuation was in effect.

²⁹ 2002 WL 31996014 (E.D. La. Sept. 30, 2002).

³⁰ *Id.* at *2.

³¹ *Id.*

³² Civ. A. No. H-06-4041, 2008 WL 450012 (S.D. Tex. Feb. 15, 2008).

Hurricane Rita took a different path and Galveston was not damaged as a result. The insured's property was therefore unscathed. Nevertheless, the insured sought coverage for the business income lost during the period of the evacuation order. The insured's policy provided:

We will pay for the actual loss of Business Income you sustain and actual Extra Expense caused by action of civil authority that prohibits access to the described premises due to direct physical loss of or damage to property, other than at the described premises, caused by or resulting from any Covered Cause of Loss.³³

The parties agreed that Hurricane Rita actually caused damage to property in Florida and to oil rigs in the Gulf of Mexico. The insurer denied coverage, however, alleging that the evacuation order was not "due to" property damage. Rather, the insurer argued that the evacuation order was issued as a precautionary measure in anticipation of damage in Galveston.

The court focused on the "due to" language in the Civil Authority provision and embarked on a causation analysis. It concluded that if "there is no causal relationship between the physical damage to other property and the civil authority order,"³⁴ then there is no coverage. The court therefore implicitly recognized a requirement for damage in the proximity of the insured's property. Since the evacuation order was issued due to the anticipated threat of damage to Galveston, rather than due to the physical damage in Florida (several hundreds of miles away), the court concluded that the policy did not provide coverage.³⁵

Disputes for coverage under civil authority provisions also arise in the context of length of the period of restoration,³⁶ complete prevention of access,³⁷ and mandatory vs. advisory orders.³⁸ In fact, most case law addressing business interruption claims arising out of Hurricane Katrina involve civil authority claims. Accordingly, in the context of hurricanes and other catastrophic events, the civil authority provision will play an important role in your analysis.

³³ *Id.* at *2.

³⁴ *Id.* at *9.

³⁵ See also *United Air Lines, Inc. v. Ins. Co. of PA.*, 439 F.3d 128 (2nd Cir. 2006) (holding that when the civil authority order is caused by fear of future harm to the area where the insured property is located, but not the actual physical damage inflicted on other property, there is not causal relationship between the civil authority order and damage to other property as required for coverage).

³⁶ See e.g. *Abner, Herrman & Brock, Inc. v. Great Northern Insurance Co.*, 308 F.Supp.2d 331,336-337 (S.D. N.Y. 2004) (limiting coverage to the specific period of time that civil authorities prohibited access to the insured's property, despite any confusion or difficulties to reach the property following the lifting of the order).

³⁷ See e.g. *Mercury Ins. Co. v. Magnolia Lady, Inc.*, 1999 WL 33537191, at *3 (N.D.Miss. Nov.4, 1999) (no coverage when state authorities hampered access to claimant's casino-hotel by closing damaged bridge, because "casino-hotel was accessible during the period of time the bridge was under repair");

³⁸ See e.g. *Kean, Miller, Hawthorne, D'Armond, McCowan & Jarman, LLP v. Nat'l Fire Ins. Co. of Hartford*, Civ. A. No. 06-770-C, 2007 WL 2489711, at *4 (M.D. La. Aug. 29, 2007) (holding that a law firm's voluntary closure of its Baton Rouge office based on the authorities' recommendation in the wake of Hurricane Katrina did not trigger coverage under the policy because access to the property was not actually prohibited).

E. Service Interruption

Catastrophic events (both man-made and natural) often result in disruption to utility service providers and their customers, such as downed power lines following storms or broken water mains following earthquakes. “Service Interruption” coverage is available for such losses. The language at issue in one case dealing with this coverage read:

In consideration of additional premium, the Time Element [*i.e.*, business interruption] coverage of this Policy is extended to cover the actual loss sustained caused directly by the interruption of the specified incoming services during a Period of Service Interruption, or if applicable, during the Restoration of Normal Operations

* * * * *

Coverage is provided for loss resulting from interruption of the following specified incoming services: Gas, Water, Electricity, Telephone[,] by reason of any accidental [occurrence] to the facilities of the following suppliers: Any Public Utility[,] that immediately prevents in whole or in part the delivery of useable services specified³⁹

In this case, the city of Salem, Oregon suffered severe flooding, leading its water utility to temporarily shut down operations. During this period, the insured had to purchase water from an outside supplier, and it continued doing so until the purity of the city’s water supply returned to normal.⁴⁰ Thus, the court noted:

Here, Siltec’s business operations were impaired because utility service was interrupted, not because its insured property was physically damaged by the flood.⁴¹

This fact, along with the foregoing policy language, led the court to conclude initially that the insured’s loss was covered. However, the “Service Interruption” endorsement also contained specific exclusions for flood and contamination. Due to these exclusions, the court ruled that there was ultimately no coverage for the loss.⁴² This case illustrates how “Service Interruption” coverage works, even though there was no coverage in this instance.

F. Ingress/Egress

Sometimes, access to an insured’s property is impaired. The resulting loss of business can be covered under “Ingress/Egress” coverage. Here is one example of this coverage:

³⁹ *Prot. Mut. Ins. Co. v. Mitsubishi Silicon Am. Corp.*, 992 P.2d 479, 483 (Or. Ct. App. 1999).

⁴⁰ *Id.* at 482.

⁴¹ *Id.* at 483.

⁴² *Id.* at 483-84.

Loss of Ingress or Egress: This policy covers loss sustained during the period of time when, as a direct result of a peril not excluded, ingress to or egress from real and personal property not excluded hereunder, is thereby prevented.⁴³

In *Fountain Powerboat*, the only road leading to the insured's facility was flooded for days following Hurricane Floyd.⁴⁴ Thus, the insured sought coverage under its "Ingress/Egress" coverage for the business interruption losses it sustained as a result of the inaccessibility. The court began by noting:

The court cannot find, and neither party has provided, any case in any jurisdiction that interprets an ingress/egress clause in the business interruption loss section of an insurance policy.⁴⁵

Looking then only to the policy language, the court concluded:

Loss sustained due to the inability to access the Fountain facility and resulting from a hurricane is a covered event with no physical damage to the property required.

....

Therefore, the court finds that no requirement for physical loss to the property is required under the contract of insurance in order to trigger business interruption coverage under the ingress/egress clause.⁴⁶

G. Border Wars

Occasionally, business interruption losses can fall on the border between direct "business interruption" coverage and "contingent business interruption" coverage. *Zurich Am. Ins. Co. v. ABM Indus., Inc.*,⁴⁷ provides just such an example. As it is both interesting and complex, an extended discussion is necessary to fully understand the court's reasoning.

ABM Industries ("ABM") provided an array of janitorial and engineering services at the World Trade Center ("WTC") complex.⁴⁸ It operated the WTC's heating, ventilating, and air-conditioning ("HVAC") systems, virtually running the physical plant. In addition, ABM serviced the common areas of the buildings and had contracts to provide janitorial services to some ninety-seven percent of the WTC's tenants. To perform these duties, ABM maintained a

⁴³ *Fountain Powerboat Indus., Inc. v. Reliance Ins. Co.*, 119 F. Supp. 2d 552, 556 (E.D.N.C. 2000).

⁴⁴ *Id.* at 554.

⁴⁵ *Id.* at 556-57.

⁴⁶ *Id.* at 556. On an unrelated note, *Fountain Powerboat* is also of independent significance in that it is an example of a court disregarding the rule of *contra proferentem*. The court observed that "when the parties to the insurance agreement are sophisticated and jointly negotiate the policy, there is no need to construe ambiguities against the insurance company." *Id.* at 555.

⁴⁷ 397 F.3d 158 (2d Cir. 2005).

⁴⁸ *Id.* at 161.

significant presence at the WTC. Employing 800 people at the site, it had office and storage space in the complex, as well as full access to custodial closets and sinks on each floor.⁴⁹ Outside of normal business hours, ABM had exclusive use of the freight elevators. It created and staffed a call center that dispatched appropriate personnel to handle problems reported by tenants. Finally, ABM even developed a sophisticated maintenance program for the WTC complex that was designed to fix problems before they happened.⁵⁰

To cover its operations across North America, ABM obtained a policy from Zurich with a blanket limit of \$127,396,375, subject to certain sublimits.⁵¹ Like most property policies, it provided a number of different coverages. To begin with, §7.A(1) of the policy covered loss or damage to “real and personal property, including but not limited to property owned, controlled, used, leased, or intended for use by the Insured.” §7.B(1), the business interruption (“BI”) coverage, insured against “loss resulting directly from the necessary interruption of business caused by direct physical loss or damage . . . to insured property at an insured location.” There was no sublimit for BI coverage, thus making the policy’s full blanket limit of \$127,396,375 available for covered BI losses. The Extra Expense provision covered up to \$50,000,000 of extra expenses “resulting from loss, damage, or destruction covered herein . . . to real or personal property described in [§7.A(1)].” “Extra Expense” was defined as the “total cost 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 had no loss or damage occurred.”

Other coverages were also relevant. The contingent business interruption (“CBI”) provision provided coverage for up to \$10,000,000 in actual losses sustained from the necessary interruption of business because of direct physical loss or damage from a covered peril “to properties not operated by the Insured” that wholly or partially prevented the insured’s direct customers from receiving ABM’s services.⁵² Finally, the policy contained a “Leader Property” provision that provided coverage for losses arising out of damage to a property that attracted business to the insured, and a “Civil Authority” provision that provided coverage for losses sustained by a lack of access resulting from the order or action of a civil or military authority.

The insured brought claims under the policy for the loss of income it derived from its operations at the WTC, resulting from the destruction of its equipment, offices and storage spaces, the call center, the freight elevators and janitorial closets, the common areas of the WTC, and the tenant spaces where ABM provided services. ABM also brought claims for more than \$20,000,000 in extra expenses resulting from union negotiations, increased employee termination costs and unemployment expenses, other wage expenses, and claim preparation fees.⁵³ Finally, ABM asserted claims for losses stemming from police orders that prevented it from servicing some 34 other locations in lower Manhattan during the aftermath of September 11.

⁴⁹ *Id.*

⁵⁰ *Id.* at 161-62.

⁵¹ *Id.* at 162.

⁵² *Id.*

⁵³ *Id.* at 162-63.

Zurich filed a declaratory judgment action in the Southern District of New York to determine the extent of its liability under the policy.⁵⁴ After the district court found that the policy was “ambiguous in several pertinent respects,” the parties engaged in discovery concerning the ambiguities. Both sides then filed cross-motions for partial summary judgment. ABM contended that its lost income fell under the BI or Leader Property provisions, and Zurich maintained that (a) most of ABM’s losses fell under the policy’s CBI coverage, which had a \$10,000,000 sublimit; and (b) that there was no coverage under the BI, Extra Expense, Leader Property and Civil Authority provisions. The trial court sided with Zurich, and ABM appealed.⁵⁵

A two-judge panel of the Second Circuit reversed the district court’s rulings on the key coverage issue, remanded on the other coverage issues, and affirmed on an evidentiary point. It began by addressing ABM’s BI claims, noting again that the policy language defined the scope of coverage as “[t]he interest of the Insured in all real and personal property, including but not limited to property owned, controlled, used, leased, or intended for use by the Insured.”⁵⁶ The dispute between the carrier and the insured centered on the nature of involvement an insured must have with a piece of property in order to recover on a business interruption claim. Zurich argued that a legally recognized property interest, such as ownership or tenancy, was necessary for coverage to attach. Relying on the rules of construction, the court disagreed and noted that Zurich’s approach would require it “to ignore the phrase ‘but not limited to’ as well as the disjunctive ‘or’ in the provision.” Further, if a property interest were required by the policy, then the words “controlled,” “used,” and “intended for use” would be rendered meaningless. Thus, it held that the policy required only an “insurable interest,” and not the higher standard of a “property interest” that was urged by Zurich.⁵⁷

To further explain its holding, the court analyzed each component of ABM’s BI claim. First, as to the common areas, tenants’ premises and the HVAC systems of the WTC complex, it noted that since ABM did not “own” or “lease” these areas, the relevant inquiry under the policy was whether it “controlled,” “used,” or “intended to use” them. Applying the district court’s definition of “use,” the Second Circuit held that the plain meaning of the word unambiguously included coverage for this case. Observing the reality of ABM’s business purpose, the court ruled that these areas “were the means by which ABM derived its income and were as essential to that function as ABM’s cleaning tools.” Additionally, the court recognized that a contrary rule would discriminate against service providers that focus on physical tasks rather than intellectual ones, because companies such as ABM generate income largely by working in spaces other than the ones they occupy for their own business needs. Stated differently, the WTC tenants were paying ABM to clean and maintain their offices, not ABM’s. As to the spaces ABM did occupy, the court held that it “used” and “controlled” those areas as well. On causation, the court also disagreed with the district judge and held that the “ruination of the WTC, *including* the property at issue, was the cause of ABM’s business interruption.” (emphasis original). Finally, the court concluded this part of the opinion by revisiting the “insurable

⁵⁴ *Id.* at 163.

⁵⁵ A more thorough analysis of the district court’s opinion can be found in Michael Sean Quinn & Pamella A. Hopper, *Extra Expenses & Business Interruption Coverages*, 26:3 INS. LITIG. REP. 97 (February 2004).

⁵⁶ *Id.* at 165.

⁵⁷ *Id.*

interest” versus “property interest” distinction, holding that the district court’s imposition of the “legally cognizable ‘interest’ in the property” requirement was an “impermissible hurdle to insurance coverage, contemplated by neither the parties nor the New York legislature.”⁵⁸ In light of the insured’s business model, it ruled that ABM satisfied New York’s “insurable interest” requirement. Since it also satisfied the requirements of the policy, the insured was entitled to recover for its business interruption losses.

Based largely on its conclusions regarding the BI claims, the court rejected Zurich’s arguments that the insured’s claim was limited to the \$10,000,000 available for contingent business interruption losses. As noted above, the express terms of the policy limited CBI coverage to losses sustained from the necessary interruption of business because of direct physical loss or damage “to properties not operated by the Insured.” Given the extensive level of ABM’s activities at the WTC, the court concluded that it “operated” the physical spaces it occupied as well as those of other tenants and the common areas. Accordingly, it held that the policy’s CBI coverage was inapplicable on these facts.

Because the Extra Expense coverage was also linked to the “insurable interest” provision in §7.A(1), the court held that summary judgment in Zurich’s favor was improper on this claim for the same reasons as the BI claim.⁵⁹ But this issue was remanded to the trial court to determine whether causation was satisfied. As for ABM’s Civil Authority claim regarding non-WTC properties in lower Manhattan, the Second Circuit rejected the district court’s holding and instead ruled that the insured might have coverage under this provision because the WTC’s destruction would not have resulted in lack of access to the other properties absent orders by the governing authorities. It also held, however, that a fact question existed as to whether it was these orders, or ABM’s own policies, that impaired access to the surrounding properties. Lastly, the court rejected coverage under the “Leader Property” provision because the language of the insuring agreement made it applicable only to “properties not owned or operated by the insured.” This conclusion was consistent with the court’s previous holdings on the other coverages.⁶⁰

The Second Circuit reached the result on the key issue in this case by focusing on the nature of ABM’s business generally and its extensive role at the WTC complex in particular, as well as the policy’s language and New York law.

On remand, the district court determined that the appropriate period of recovery for ABM’s claim was “the hypothetical length of time required to rebuild the WTC.”⁶¹ This ruling was a departure from other 9/11 cases addressing period of restoration. In most 9/11 cases, the court refused to tie an insured’s claim for lost income to the period of time to rebuild the WTC. Instead, courts tied the insured’s period of restoration to the period of time it would take to build property that is functionally equivalent to the *insured’s* lost property, rather than property of

⁵⁸ *Id.* at 167-68.

⁵⁹ *Id.* at 170.

⁶⁰ Procedurally, the court affirmed the trial judge’s exclusion of ABM’s evidence in support of a two-occurrence claim, but it contained no discussion of the trial court’s decision to deny ABM’s motion to amend its pleadings to assert a bad faith counterclaim based on Zurich’s conduct both prior to *and* after the commencement of litigation.

⁶¹ *Zurich Am. Ins. Co. v. ABM Indus., Inc.*, No. 01 Civ. 11200, 2006 WL 1293360, at *3 (S.D. N.Y. May 11, 2006).

others.⁶² But the *ABM* court distinguished those cases on the basis that, as a service provider for the WTC, “the nature of ABM’s business is fundamentally different...ABM cannot simply relocate to another building and carry on its business...restoration of the WTC itself is ‘necessary for ABM to resume’ its operations.”⁶³ The court recognized that other factors influenced rebuilding the WTC and therefore limited the restoration period to the theoretical period of time to rebuild the WTC.

H. Business Interruption Loss Measurement

Although an insured may suffer property damage and an interruption of business, it does not always follow that the insured actually sustains a recoverable loss. Other factors affecting the insured’s business may impact the measurement of the insured’s claim. For example, if the insured is operating at a loss prior to the property damage, and actually *saves* operating costs following property damage, courts have found that the insured does not sustain a business income loss.⁶⁴ Similarly, courts have sometimes found that payments from other sources, such as government grants, may reduce an insured’s loss. For example, in *PMA Capital Ins. Co. v. US Airways, Inc.*,⁶⁵ the court found that payments that the insured airline received from the federal government constituted “recoveries” as defined by the policy, and therefore reduced the insured’s business income loss.

One tactic that insurers often take following a loss is an attempt to reduce an insured’s business income claim by calculating increased sales following an event in the measurement of the insured’s loss. This is illustrated by *Rimkus Consulting Group, Inc. v. Hartford Casualty Ins. Co.*⁶⁶ Hurricane Katrina forced Rimkus to close its damaged New Orleans office. But Rimkus continued to provide consulting and engineering services by working out of temporary offices.

Because Rimkus provides independent adjustment services, its business following Hurricane Katrina increased exponentially. In fact, Hartford introduced evidence that Rimkus’ actual revenues during the Period of Restoration were nearly four times the projected revenue for that period. Nevertheless, Rimkus sought business interruption coverage from Hartford, claiming it suffered lost revenues from its “regular, ‘pre-storm’ clientele.”⁶⁷ Hartford, on the other hand, argued that the distinction between pre-storm and post-storm income is meaningless because Rimkus continued to provide engineering and consulting services to the same industry following Katrina.

⁶² See e.g. *Retail Brand Alliance, Inc. v. Factory Mutual Ins. Co.*, 489 F.Supp.2d 326, 332 (S.D. N.Y. 2007) (distinguishing the *ABM* case and holding that the period of liability is tied to the restoration of the insured’s building and equipment, and not to the original location of that building or the surrounding sales environment).

⁶³ *ABM*, 2006 WL 1293360, at *2.

⁶⁴ *Dictiomatic, Inc. v. U.S. Fidelity & Guar. Co.*, 958 F. Supp. 594, 602 (S.D. Fl. 1997) (holding that the insurer must demonstrate “that there was an actual loss of business income during the period of time necessary to restore the business and that the loss of income was caused by the interruption of business and not some other factor or factors.”)

⁶⁵ 626 S.E.2d 369 (Va. 2006).

⁶⁶ 552 F.Supp.2d 637 (S.D. Tex. 2007).

⁶⁷ *Id.* at 642.

The court found that Rimkus’ “operations, the provision of engineering and consulting services, continued after Katrina and it received income for those services.”⁶⁸ Because its income actually increased, the court concluded that Rimkus did not suffer a recoverable business income loss. In reaching this conclusion, the court relied on specific policy language that allowed Hartford to reduce amounts payable “to the extent that the reduction in volume of business income from the affected income channel is offset by an increase in the volume of business from other income channels.”⁶⁹

The court’s analysis in *Rimkus* demonstrates that the specific facts of the case, in conjunction with the policy language, determine the measurement and extent of business income coverage. Therefore, it behooves attorneys to closely examine policy language and distinguish cases when that language differs.

III. CONCLUSION

Due to the complexity of business interruption and time element losses, lawyers must give particular attention to the policy language and the relatively limited universe of relevant cases. Regardless of whether a lawyer is acting for an insurer or an insured, taking a disciplined approach to handling these issues is a critical step to a successful resolution.

⁶⁸ *Id.* at 645.

⁶⁹ *Id.* at 640.