When Disaster Strikes: Coverage for Natural Disasters

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Natural disasters can strike anywhere, any time and in a variety of forms. The last several years have witnessed catastrophic impacts from wildfires, tornadoes, hurricanes, and winter storms, from coast to coast and virtually all points in between. Natural disasters do and will continue to implicate many types of insurance coverage. In the commercial context the most important natural disaster coverages are for physical damage and time element (business interruption) losses. With natural disaster claims, the issue isn't so much whether the event is covered, but how much is due.

1) Physical damage and Related Costs:
   - Buildings/Real Property
   - Personal Property (of both the Policyholder and its Officers and Employees)
   - Property of Others in Policyholder's Custody
   - Accounts Receivable
   - Electronic Data/Programs/Software
   - Debris Removal
   - Decontamination Costs/Pollutant Removal
   - Demolition/Construction Costs
   - Valuable Papers/Records
   - Professional Fees (excluding attorneys, public adjusters)

2) Time Element Coverage

   - Business Interruption (BI) - Business Interruption Coverage covers actual loss of income/earnings due to suspension of operations caused by covered loss. Coverage continues through the period of restoration of operations (including Extended Coverage Period, if provided).

   - Contingent BI - Contingent Business Interruption Claims coverage is triggered where covered damage to suppliers, customers or "attractor properties" negatively affects the policyholder's business operations, even where policyholder's own property is not damaged. Covered Losses include: (1) additional expenses incurred to obtain supplies and raw materials; (2) diminished revenue because of losses suffered by customers; and (3) other expenses due to damage to suppliers or customers.

- Extra Expense - Covers necessary additional expenses incurred: (1) to avoid or minimize the interruption of business; and (2) to repair or replace property, systems, lost information or damaged valuable papers.

- Civil Authority

- Ingress/Egress - Applies when access to and exit from a policyholder's premises are blocked. Applies even if the policyholder's property has not been physically damaged but typically requires damage of the type covered under the policy to non-insured locations.

- Service Interruption - Covers loss of income or extra expense resulting from interruption of utility services (water, communications, power, gas and sewage) both on and off premises.

Although this paper focuses on commercial coverage, it is important to note that there are significant differences between homeowners and commercial policies. For instance, homeowners insurance generally excludes flooding and earthquakes, whereas some larger commercial policyholders purchase earthquake and flood coverage. However, in commercial coverage particular causes of damage – flooding, earthquake, named storm—typically are subject to specific sub limits. Moreover, there may be specific limits based on the location of the loss; coverage for flooding is less expansive in areas where flooding is common and coverage for named storms or hurricanes can be reduced in the states most often hit, such as Florida, or excluded altogether.

Several important issues arise regarding insurance for natural disasters, particularly under property and business income coverage:

I. Policy Interpretation Considerations

   a. General Considerations

   b. Causation and Anti-Concurrent Causation Language

II. Property Damage Considerations

    a. Number of Events or Occurrences

    b. Cost to Repair/Replace

III. Time Element Considerations

    a. Period of Restoration

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    d. Law and Ordinance Exclusion

IV. Practical Considerations for the Coverage Litigator

We consider each in turn.

I. Policy Interpretation Considerations

a. General Policy Interpretation Considerations

Policy language drives what policyholders may recover. Interpretation is a matter of state law, and differs, rendering choice of law important. Courts review the language and context of the policy, and in many jurisdictions ambiguity in policy language is construed in favor of the policyholder. *See, e.g.*, *Pierce v. Allstate Ins. Co*., 542 F. Supp.2d 495, 498 (E.D. La. 2008) ("When this provision is read in the context of the entire policy, … the endorsement issued by the Defendant is clear and unambiguous and must be enforced as written.") Policy language varies by insurer and policy, and many policies include manuscript language. Where standard language is used, it is frequently modified. Definitions, the use of language such as "directly and indirectly," or causation language create coverage issues, and are rife for arguments by both sides. Courts interpret insurance policies to determine if the language is ambiguous, and if not, they apply the

plain language rule, looking to definitions within the policy and, when those fail, to definitions in dictionaries—legal and otherwise—as well as definitions used by other courts. *See, e.g., Northrop Grumman Corp. v. Factory Mut. Ins. Co*., 563 F.3d 777, 784 (9th Cir. 2009) (finding the flood exclusion barred coverage based on the "plain language of the contract" and dictionary definitions).

Many of the best arguments attorneys on either side can make are based on the policy language. First and foremost, what does the policy say? Is the language clear and unambiguous? If there is ambiguity, frequently found when more than one definition exists, is extrinsic evidence involving the drafting and negotiation of policy relevant? If ambiguity exists, who prevails—keeping in mind that most courts will find in favor of coverage where there is ambiguity? Even when the language is clear, seemingly slight variations can affect coverage depending on the facts. Other arguments involve the policyholder's reasonable expectations, the existence of anti-concurrent causation language (addressed below), the specific facts of the losses, and how to characterize those losses. Loss categorization is one important way to determine if specific damage is covered or not and may drastically alter the amounts paid by the insurer.[1] Other common arguments revolve around other causes of loss that may be excluded: pollutants enter structures following natural disasters; mold may grow following water; theft and looting may occur following major storms; and the policyholder's own negligence regarding maintenance and mitigation.

[1] No coverage where the policyholders "conceded that they could not offer any evidence of entry through openings in the roof or walls caused by Hurricane Irene." *Florida Windstorm Underwriting v. Gajwani*, 934 So.2d 501, 506-507 (Fla. 3d DCA 2005).

b. Causation and Anti-Concurrent Causation Language

The policyholder bears the burden of proof on damages and their cause. *E.g. Loyola University v. Sun Underwriters Ins. Co. of New York*, 93 F. Supp. 186 (E.D. La. 1952) aff'd, 196 F. 2d 169 (5th Cir. 1952); *Tuepker v. State Farm Fire & Cas. Co.,* 507 F.3d 346 (5th Cir. 2001) (applying Mississippi law). There may be multiple coverages from different causes: (1) property damage; (2) business interruption; (3) contingent business interruption; (4) ingress/egress; and (5) service interruption. For each different allocations, deductibles and sublimits likely apply.

The state court's views of causation also create varying results. Some of the principle approaches are: concurrent causation; efficient proximate cause; and proximate or immediate cause. Concurrent causation broadly means that when damage is caused by covered and non-covered causes, all damage is covered. *See Sebo v. American Home Ins. Co*., 208 So. 3d 694 (Fla. 2016) ("it would not be feasible to apply the Efficient Proximate Cause doctrine because no efficient cause can be determined"; "'[w]here weather perils combine with human negligence to cause a loss, it seems logical and reasonable to find the loss covered by an all-risk policy even if one of the causes is excluded from coverage" (internal citation omitted)); *State Farm Fire & Casualty Co. v. Slade*, 747 So. 2d 293 (Ala. 1999). In many states, the efficient proximate cause rule is applied, which requires that if the insured peril is the dominant cause of the loss that sets other causes in motion coverage exists for the entire loss – other perils are not considered. *Garvey v. State Farm Fire and Cas. Co.*, 48 Cal.3d 395 (1989); *Flomerfelt v.* Cardiello, 202 N.J. 432 (N.J. 2010); Julian *v. Hartford Underwriters Ins. Co*., 35 Cal.4th 747 (2005); *Glen Falls Ins. Co. of Glen Falls, N.Y. v. Linwood Elevator*, 130 So.2d 262, 270 (1961). Some states take a conservative view of causation, finding no coverage when an excluded cause combines with a covered cause

to produce a loss, requiring the policyholder either to prove the entire loss was caused by a covered cause or specifically prove which damages resulted from that covered cause. *E.g. Travelers Indemnity Co. v. McKillip*, 469 S.W.2d 160, 162 (Tex. Sup. 1971) (holding that under the policy, when the insurer pled an exclusion, the burden was placed on the insured to establish either that the loss was not caused to any extent by the excluded peril, or to segregate the loss caused by windstorm, the covered peril, from the loss caused by the excluded peril, snow, and to secure a jury finding on the amount of damage caused by the windstorm); *Hahn v. United Fire & Cas. Co*., No. 6:15-CV-00218, 2017 WL 1289024 (W.D. Tex. Apr. 6, 2017); *Amish Connection, Inc. v. State Farm Fire & Cas. Co*., 861 N.W.2d 230 (Iowa 2015). Some courts use proximate/immediate causation to identify the single proximate or immediate cause of the loss and proceed from there without looking at any earlier cause that may have set the chain of events in motion. *Chemstrand Corp. v. Maryland Casualty Co.*, 98 So.2d 1, 5 (Ala. 1957) (recovery is allowed where an insured risk is the last step in the chain of causation set in motion by an uninsured peril).

Insurers responded to the growth of both efficient proximate cause and pure concurrent causation by inserting anti-concurrent causation clauses into the policy to avoid the need to determine which of several different governs. Anti-concurrent causation clauses generally provide that no portion of a loss caused by a combination of covered and uncovered causes is covered—even when a covered cause of loss contributes concurrently or in any sequence. The majority of courts enforce anti-concurrent causation clauses. *See JAW The Pointe, L.L.C. v. Lexington Ins. Co*., 460 S.W.3d 597, 608 (Tex. 2015); *Boazova v. Safety Ins. Co*., 462 Mass. 346 (Mass. 2012); *Lombardi v. Universal N. Am. Ins. Co*., 2015 Conn. Super. LEXIS 138 (Conn. Super.

Ct. Jan. 21, 2015) (collecting cases and finding an anti-concurrent causation clause enforceable in a dispute arising from Tropical Storm Irene); *Corban v. United Servs. Auto. Ass'n*, 20 So.3d 601 (Miss. 2009) (holding in a dispute arising due to damage from Hurricane Katrina that the clause applies only if two or more causes occur simultaneously to cause loss).

A smaller number of jurisdictions, led by California, have rejected this application. *Howell v. State Farm Fire & Cas. Co.*, 267 Cal.Rptr. 708 (Cal. App. 1990) (anti-concurrent causation language contrary to Cal. Ins. Code §§ 530 and 532); *Safeco Ins. Co. v. Hirschmann*, 773 P. 2d 413 (Wash. 1999) (*en banc*) (against public policy to contract around efficient proximate cause doctrine); *Murray v. State Farm Fire & Casualty Co.*, 203 W. Va. 477, 492, 509 S.E.2d 1, 16 (W. Va. 1998). Many of the cases which followed *Howell*, which is a statutory interpretation case, came from jurisdictions such as Washington and West Virginia that did not have a statute comparable to the California statutes interpreted in *Howell*. Those decisions (*Hirschman* and *Murray*) represent judicially created public policy, which may explain why the unenforceability view remains the minority view.

In some cases, damage stemming from natural disasters is caused by some combination of covered and uncovered causes. When this occurs, anti-concurrent causation language is implicated (at least where it exists). This causes significant issues when the cause cannot be separated. Policyholders, unsurprisingly, advocate that the damage was caused solely by a covered cause of loss, with no damage due to an uncovered cause. Insurers, on the other hand, may emphasize the loss from the excluded cause and rely on the anti-concurrent causation language.

For property damage, several issues arise: cause of loss; betterments; labor and material costs; and replacement cost vs. actual value. Coverage attorneys must first determine whether concurrent causation or a different rule applies. Next, they must consider how issues of causation will affect the outcome when there are two causes of loss one covered and one not. Some courts find there is coverage for all the damage, others find nothing is covered, and yet others find there is coverage for the loss arising from covered causes but no coverage for loss caused by causes excluded from the policy, placing the onus on the policyholder to prove the amount of damage resulting from a covered cause of loss. Even where the cause of loss is not excluded, often the policyholder must determine the amount of loss caused by each force because of the categories and sublimits in a policy.

V. Property Damage Considerations

a. Number of Events or Occurrences

The number of events or occurrences can be difficult to determine when a natural disaster hits. This arises particularly in the context of storms which make landfall in the same area more than once. Does the storm constitute a single event or occurrence because it results from the same storm or is it multiple occurrences because the storm made landfall, went back out to sea, and then returned? *SEACOR Holdings, Inc. v. Commonwealth Ins. Co*., 635 F.3d 675, 682-683 (5th Cir. 2011) (Louisiana law) ("An occurrence is defined as 'any one loss, disaster or casualty or series of losses, disasters or casualties arising out of one event.' Thus, each series of losses, even those stemming from different perils, arising from one event is adjusted separately. SEACOR may have experienced different casualties from Katrina's two perils, wind and rain, but under the policy, those losses arose out of one event — Katrina — and warrant only one deductible. … Katrina was

a single event requiring only the Named Windstorm deductible, even if the storm included multiple 'acts' of rain and wind."); *The Lynd Co. v. RSUI Indemnity Co*., 399 S.W.3d 197, 200 (Tex. App.-San Antonio 2012) ("It is undisputed that fifteen of Lynd's properties sustained damage from the same 'occurrence.' … 'a result of the single hurricane "occurrence."'") (citations omitted).

Complicating coverage issues is that some policies cover damage happening within a 72-hour period following a storm, and often the policyholder has the right to choose the start time. *The Lynd Co. v. RSUI Indemnity Co*., 399 S.W.3d 197, 200 (Tex. App.-San Antonio 2012) ("When the term "occurrence" applies to a loss or series of losses from the perils of tornado, cyclone, hurricane, windstorm, hail, flood, earthquake, volcanic eruption, riot, riot attending a strike, civil commotion and vandalism and malicious mischief, one event shall be construed to be all losses arising during a continuous period of 72 hours."); *ARM Props. Mgmt. Grp. v. RSUI Indem. Co.*, No. A–07–CA–718–SS, 2008 WL 5973220, *2 (W.D. Tex. Aug. 22, 2008) ("in the case of a hurricane, 'one event shall be construed to be all losses arising during a continuous period of 72 hours.' It is undisputed that each of the nine properties policyholder under this policy is a 'scheduled item of property.' The term 'loss' is defined as 'a loss or series of losses arising out of one event or occurrence.'")

Turning to the issue of multiple occurrences, must a policyholder exhaust its deductible for each occurrence before coverage is triggered? How do the limits on the number of occurrences affect coverage? This issue has arisen recently with Hurricanes Irma and Harvey. Generally, hurricanes hit an area once, then move on. Harvey, however, made several landfalls in the same locations, with breaks in between as it went out to sea. *ARM Props. Mgmt. Grp.*, No.

A–07–CA–718–SS, 2008 WL 5973220 ("It is undisputed that each of the nine properties policyholder under this policy is a 'scheduled item of property.' The term 'loss' is defined as 'a loss or series of losses arising out of one event or occurrence.'") Named storm coverage may have the 72-hour period time limit, but flood insurance generally has no such time limit. Hurricane Irma hit several islands, where policyholders owned multiple properties on different islands, all of which were covered by the same policy. Is this one occurrence or many? Does the 72-hour time limit apply? Different sublimits and deductibles?

b. Cost to Repair or Replace

A common issue in property damage coverage involves the scope of replacement cost coverage for older structures. It is common for policies to provide for replacement cost coverage, upon actual replacement, namely, paying the cost in excess of actual cash value that it actually costs to replace the policyholder property. Not all policies provide coverage for governmentally mandated upgrades to meet current building standards.

While a detailed discussion of the nuances of what is "replacement cost" under particular policy language and under the laws of various jurisdictions is beyond the scope of this paper, practitioners on either side need to be prepared to address the impact of Ordinance and Law exclusions (generally intended to eliminate coverage for governmentally mandated improvements, aka "code upgrades") and Ordinance and Law extensions of coverage (reversing those exclusions, but generally providing a limited additional amount of insurance, either within or in excess of the policy's limit of liability).

c. Ordinance and Law Exclusions

Given the catastrophic nature of natural disasters, many states enact laws and ordinances regarding methods of construction, material type, and various types of reinforcements to limit future damage caused by the more common natural disasters in their area, policyholder may want to strongly consider purchasing such coverage in an adequate amount. An issue can arise as to the scope of Ordinance and Law coverage as the Ordinance or Law exclusion can play a large role in coverage for natural disasters, impacting both the Period of Restoration and the Valuation following policyholder damage to property, leaving policyholders with no coverage for any code upgrades. Arguments regarding the Ordinance and Law exclusion often revolve around the appropriate period of restoration (for instance, the insurer arguing that all time for a permitting process is excluded and the policyholder claiming that permitting time is not excluded when other factors caused delay) and the definition of "enforcement" and "compliance."); *State Farm Fire & Casualty Co. v. Metro. Dade County*, 639 So. 2d 63, 66 (Fla. 3d DCA 1994) ("Enforcement is 'the act of enforcing: as a: compulsion especially by physical violence b: forcible urging or argument ... c: the compelling of the fulfillment (as of a law or order).' *Webster's Third New International Dictionary, Unabridged*, 751 (1986). … The threat of enforcement is the driving force behind compliance with building and construction codes and ordinances. Permits are required before construction and repairs commence. Failure to comply results in failure to receive necessary permits for further construction or occupancy."); *Haas v. Audubon Indemnity Co.*, 722 So. 2d 1022, 1029 (La. App. 3d Cir. 1998) ("compliance is not enforcement." "[I]t was the vandalism that caused damage to the Haas' building, not the enforcement of any ordinance or law. The costs of asbestos abatement were necessary because of the flooding which arose out of

the vandalism to the building."); *Hampton Foods, Inc. v. Aetna Cas. & Sur. Co.*, 787 F.2d 349, 353 (8th Cir. 1986) ("The condemnation decree did not cause or increase that loss. Construing the exclusion clause to preclude recovery here would violate the reasonable expectations of the layman who purchased the policy. … one would reasonably expect that if a building was severely damaged by a windstorm or snowstorm, rendering its collapse imminent and making access to the building extremely dangerous, this would constitute a loss not due to a subsequent condemnation of the structure.")

III. Time Element/Loss of Business Income

Generally, Business Income coverage is intended to compensate the policyholder for its actual loss of income during the "period of restoration." In the context of catastrophes, two issues are common: (1) the duration of the "period of restoration"; and (2) the degree to which wide scale disaster-induced economic changes are material to the calculation of the actual loss of business income.

a. Period of Restoration

Under most standard-form policies, the period of restoration is measured by the time it would take to repair or replace the policyholder property with reasonable diligence. This is a hypothetical period of time not necessarily governed by how long it actually takes the policyholder to repair or replace its property. *Hampton Foods, Inc. v. Aetna Cas. and Sur. Co.*, 843 F.2d 1140 (8th Cir. 1988); *Beautytuft, Inc. v. Factory Ins. Ass'n.*, 431 F.2d 1122 (6th Cir. 1970).

Major disasters, of course, can wreak havoc on construction efforts. Many insurers recognize this and take into account supply and demand issues for both contractors and building materials in calculating periods of restorations. Some jurisdictions, such as California, statutorily mandate

extensions for time element claims in personal lines policies for declared disasters. Cal. Ins. Code § 2051.5 (effective 2019).

b. Loss of Market Exclusion

Some Insurers may argue that there is no business income loss or reduced business income loss because business in the area ground to a halt due to disaster, triggering the "loss of market" exclusion found in some policies. Other policies contain express provisions intended to address the situation where there is a reduction in some types of commercial activity coupled with a surge in other types of commercial activity (such as contracting and insurance adjusting).

Courts are extremely reluctant to apply loss of market exclusions to circumstances where the cause of the market decline is the same casualty which caused the policyholder property damage. See, *Boyd Motors, Inc. v. Employers Ins. of Wausau*, 880 F.2d 270, 274 (10th Cir. 1989) ("taking the equation of 'loss of market' with 'loss of market value' to its logical conclusion would lead to the absurd result of the exclusion swallowing coverage whole. Since, as written, the loss of market exclusion is not qualified in any way so as to restrict its application solely to post-repair depreciation, accepting the identity of the two terms in question would appear to entail adoption of the indefensible position that all loss in value to the policyholder property (i.e., the entire covered risk) is excluded from coverage under the policy. "); *Duane Reade, Inc. v. St. Paul Fire & Marine Ins. Co*., 279 F. Supp. 2d 235 (S.D.N.Y. 2003); aff'd as modified, 411 F.3d 384, 398-399 (2d Cir. 2005) ("The loss of market exclusion relates to losses resulting from economic changes occasioned by, e.g., competition, shifts in demand, or the like; it does not bar recovery for loss of ordinary business caused by a physical destruction or other covered perils.")

c. Civil Authority Provisions

Civil authority provisions require access be prohibited due to a covered loss. It is often limited to a certain time period and specific geographic area. Often the prohibition of access must be specific to the policyholder's location (or a larger area encompassing the policyholder's location). Civil Authority Coverage for Business Interruption Claims may provide coverage when a government act prohibits access to covered property due to covered damage including closures, curfews and travel restrictions. This may be true even when there is no formal order. *Narricot Industries, Inc. v. Fireman's Fund Ins. Co*., 2002 WL 31247972, *4 (E.D. Pa. 2002) (holding that a Civil Authority Clause did not require a formal order or even a written order); *Kean, Miller, Hawthorne, D'Armond McCowan & Jarman, LLP v. Natl. Fire Ins. Co. of Hartford*, 2007 WL 2489711, *3 (M.D. La. Aug. 29, 2007) (the fact that the Governor declared a state of emergency and government officials asked and encouraged residents to stay off the streets "could be considered an 'action of civil authority' that would not have been given but for Hurricane Katrina."). However, Civil Authority coverage does require that access be prohibited due to property damage. *Kean*, 2007 WL 2489711, *3 (coverage not triggered where "the advisories and recommendations given did not actually 'prohibit access' to the policyholder premises.")

The specific prohibition element has been interpreted to preclude coverage where some general restriction on access elsewhere resulted in a reduction of business at a location outside the restricted area or where the restriction was less than total. Two examples are a reduction in business at a theater chain due to curfews imposed after the Rodney King riots in 1992 (*Syufy Enterprises v. Home Ins. Co. of Indiana*, 1995 WL 129229 (N.D. Cal. 1995)) and where vehicular, but not pedestrian, access to a building in lower Manhattan was restricted after 9/11. *Abner,*

Herrman & Brock, Inc. v. Great Northern Ins. Co., 308 F.Supp.2d 331 (S.D.N.Y. 2004)). Another example is where civil authority eliminated one of several modes of access (such as the grounding of all non-government aircraft for several days after 9/11) which resulted in a reduction of business for the policyholder hotel properties outside of New York. *Southern Hospitality, Inc. v. Zurich American Ins. Co.*, 393 F.3d 1137 (10th Cir. 2004) and *730 Bienville Partners, Ltd. v. Assurance Co. of America*, 2002 WL 31996014 (E.D. La. 2002)).

A government mandated evacuation may mean Business Income loss is not covered. *Dickie Brennan & Co., Inc. v. Lexington Ins. Co.*, 636 F.3d 683 (5th Cir. 2011) (holding that a mandatory evacuation ordered in anticipation of Hurricane Gustav did not trigger business income coverage because there was no nexus between the evacuation order and damage to property, "other than at the described premises," as required for coverage under the policy's civil authority provision.); *Jones, Walker, Waechter, Poitevent, Carrere & Denegre, LLP v. Chubb Corp*., CIV.A. 09-6057, 2010 WL 4026375, *3 (E.D. La. Oct. 11, 2010) (the prohibition of access "as a 'direct result of physical loss or damage to the property,'" requires a "direct nexus between the damage sustained and the [resultant] order.")

When anti-concurrent causation language is present, coverage may be barred when levees break or when a civil authority decides to open a dam to prevent further damage to one area but causes flooding in another.

IV. Practical Considerations for the Coverage Litigator

Coverage and bad faith litigation following a disaster arises in circumstances which counsel, whether for the policyholder or the insurer, ignores at the client's peril. First, even for business policyholders, there is a strong sense of victimization, which is often shared by the jury

pool in the jurisdiction. Second, the policyholder's conduct did not cause the loss – the policyholder simply was in the wrong place at the wrong time. Third, the insurer's claims handling resources are often stretched to or past their breaking point, depending on the scope of the catastrophe thereby possibly impacting the handling of the policyholder's claim. Fourth, government regulators (usually the state's Department of Insurance) are far more involved than they are in ordinary circumstances.[2] All of these circumstances need to be taken into account by counsel on both sides.

[2] For example consider the actions of California's elected Insurance Commissioners. http://www.insurance.ca.gov/01-consumers/140-catastrophes/WildfireResources.cfm