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NY Court Backs TransCanada's $58M Coverage Win

By **Jeff Sistrunk**

Law360, Los Angeles (September 19, 2017, 8:13 PM EDT) -- TransCanada Energy USA Inc. is entitled to nearly $58 million in coverage for its costs for property damage and business interruption stemming from the breakdown and temporary loss of a faulty turbine, a New York appellate court affirmed on Tuesday.

In a brief opinion, a panel of the state Appellate Division's First Department spurned Arch Insurance Co. and Ace INA Insurance Co.'s bid to overturn a lower court's ruling granting summary judgment to TransCanada and two subsidiaries. Like the trial court, the appellate panel rejected the insurers' contentions that they had no coverage obligations because the damage to the turbine resulted from a crack that existed prior to the policy's inception date and TransCanada didn't experience any business interruption losses until after the turbine was repaired.

Arch, Ace and a third insurer, Factory Mutual Insurance Co. — which didn't appeal the lower court's ruling — had disputed a claim TransCanada made under a policy that went into effect after the power company acquired the Ravenswood Generating Station in Long Island City, New York, in 2008.

Three days after its acquisition of the Ravenswood plant, on Sept. 12, 2008, TransCanada allegedly first noticed excessive vibrations in a generator named Ravenswood Unit 30. These vibrations increased over a number of days until Unit 30 was shut down, and a subsequent inspection revealed severe cracking around the exciter end of the generator rotor, according to court papers.

The turbine was out of service for eight months until repairs were completed in May 2009, according to court documents. TransCanada claimed it had suffered about $7 million in property damage and $50.8 million in business interruption losses, including $48 million in lost sales.

In a March 2016 decision, New York Supreme Court Judge Barbara Jaffe pointed out that TransCanada's policy insured against "all risks of physical loss or damage" to property during the policy period, which spanned from August 2008 to June 2009. It is undisputed that the turbine sustained damage when the policy was in effect, and there is no provision excluding physical loss or damage originating from before the commencement of the policy period, the judge wrote.

The judge agreed with TransCanada that the fact that a crack existed in the turbine before the policy was in place is irrelevant. The insurers' reliance on an "injury in fact" test, which makes coverage dependent on when the damaging act occurred, is misplaced, Judge Jaffe wrote.

TransCanada's business interruption losses were almost wholly constituted of lost sales, in the form of payments from the New York Independent System Operator to generate electricity, according to court documents. However, most of those lost sales weren't realized until auctions occurring after the turbine went back online in May 2009, because the NYISO looks back to rolling averages and generation capacity periods to calculate the amount of sales, TransCanada argued.

The insurers, meanwhile, said the lost capacity sales realized after the date the turbine went back into use aren't covered.

Judge Jaffe found that TransCanada is entitled to coverage for lost sales outside of the period of liability when the turbine was out of commission, because capacity produced during that period wasn't sold at auction until after the turbine was restored to use. The lost sales were directly attributable to the fact that the turbine was not operational for those months, the judge said.

Arch and Ace sought appellate review of Judge Jaffe's decision, but the First Department panel was unswayed by the insurers' arguments. On the question of property damage, the panel found that the insurers' obligations were triggered because the crack in the generator's rotor indisputably worsened during the policy period.

"Therefore, the loss occurred on Sept. 12, 2008 — the discrete event of physical loss or damage triggering the time element coverage when the unit was taken out of operation due to the excessive vibrations, and TransCanada's property sustained a physical loss or damage during the policy period," the appellate panel wrote. "Since there is no provision in the policy that excludes physical loss or damage originating prior to the commencement of the policy period, the policy covers the loss."

The panel also found that the method by which TransCanada calculated its business interruption losses was reasonable, and that a policy exclusion for payments awarded "for attaining or exceeding certain production levels" did not apply.

"It is undisputed that TransCanada is a regulated entity that sells at actual production capacity, not when it attains or exceeds specified production levels," the panel wrote.

Pamela D. Hans of Anderson Kill PC, who represents TransCanada, said in an emailed statement that the decision is important for policyholders on two fronts.

"First, both the Supreme Court and the Appellate Division rejected the insurance companies’ attempt to write into the insurance policy an exclusion for loss or damage that originated — unbeknownst to the policyholder — prior to the commencement of the policy period," Hans said. "Second, in assessing the business interruption claim, both courts focused squarely on losses plainly attributable to the period of liability."

Hans also noted that both the lower and appellate courts rejected the insurers' attempts to rely on cases involving retail stores, which she said "would require disregarding the revenue model prevalent in the energy industry and policy language that accommodates that difference."

An attorney for the insurers did not immediately respond to a request for comment.

Judges David Friedman, Judith J. Gische, Richard T. Andrias and Troy K. Webber sat on the appellate panel.

The appellants are represented by Thomas B. Orlando of Foran Glennon Palandech Ponzi & Rudloff PC.

TransCanada is represented by Pamela D. Hans, John M. O'Connor and Finley Harckham of Anderson Kill PC.

The cases are National Union Fire Insurance Co. of Pittsburgh, Pa., et al. v. TransCanada Energy USA Inc. et al., case number 650515/2010; and TC Ravenswood LLC v. National Union Fire Insurance Co. of Pittsburgh, Pa., et al., case number 400759/2011, in the Supreme Court of the State of New York, Appellate Division, First Department.

--Editing by Aaron Pelc.
