

Answers to Frequently Asked Insurance Questions in the Wake of September 11



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Given the staggering human and emotional toll left in the wake of the terrorist attack on the World Trade Center on September 11, 2001, it may seem too soon to focus on economic issues. Unfortunately, almost all businesses in New York City, and many elsewhere, suffered dislocation of their operations, with consequent losses, and insurance law often punishes even small delays in reporting such losses with forfeiture of any right to collect. This is especially true in New York. Further complicating this situation, property insurance policies are frequently nearly incomprehensible, even for experienced business persons. Therefore, affected companies, some still operating under heavy emotional burdens, must locate insurance policies, parse confusing insurance language, decipher its meaning, and give notice—all in a short period of time. This issue of the Policyholder Advisor is designed to give business people answers to some of the common questions they may have.

What type of insurance coverage is implicated?

Most businesses affected by the attack will look to first-party insurance policies, or policies that promise to protect policyholders from losses they suffer to their own property or expectations of profit. These policies are generally referred to as “property” insurance policies, but they come under other names, such as “inland marine,” “fire” or “multi-peril” insurance policies. Some businesses, if sued by people charging that negligence caused or enhanced injury, may call upon their third-

party insurance policies, which promise to pay policyholders for the costs of defending, and paying judgments or settlements in, lawsuits against them. These policies are generally referred to as “liability” policies, but may be labeled as “catastrophe” or “commercial” insurance policies.

What type of property coverage is implicated?

Property insurance policies contain three basic types of coverage: property damage, business income and extra expense.

- Property damage coverage is designed to pay for physical loss or damage to business property—machinery, equipment, inventory, raw materials—as well as property of others in the policyholder’s control or on the property of the policyholder.
- Business income coverage (sometimes referred to as business interruption coverage) is designed to pay for the policyholder’s loss of profit, and the policyholder’s unavoidable continuing expenses (for instance, insurance premiums or salaries of management but not raw materials because they are not needed by an inactive operation) during the period in which the policyholder is out of business because of property damage.
- Extra expense coverage pays for both the policyholder’s costs in minimizing or avoiding a business income loss (for instance, costs incurred in relocating temporarily) and those costs the policyholder would not have incurred but for the loss (for instance, security guards to prevent looting).

There are also various other types of coverage that may be implicated, like that for accounts receivable, computer equipment or valuable records. Insurance coverage may also be found under *contingent business income* and *contingent extra expense* coverage as well as *civil authority* coverage. These coverages provide insurance coverage to businesses which did not suffer physical damage to their property, but have suffered loss on account of damage to other property or acts by civil authority. These coverages are discussed below.

Will the War Risk Exclusion apply?

Many insurance companies have publicly stated that they will not apply war risk exclusions. Such statements, however, are not unanimous, as war risk exclusions should not apply. The leading case on this issue is *Pan American World Airways, Inc. v. Aetna Casualty & Surety Co.*, 505 F.2d 989 (2d Cir. 1974) (applying New York law), which addressed whether various “war risk” exclusions precluded coverage for damages stemming from the hijacking and subsequent destruction of a Boeing 747. The United States Court of Appeals for the Second Circuit found that “war” refers to the use of force between governments or entities essentially like governments, and that the hijacking terrorists were not representatives of a government or government policy:

The loss of the Pan American 747 was not caused by any act that is recognized as a war-like act. The hijackers did not wear insignia. They did not openly carry arms. Their acts had criminal rather than military overtones. They were the agents of a radical political group, rather than a sovereign government.

Id. at 1015. Other cases, including some in New York, have followed this reasoning, which should apply to the terrorist acts of September 11, 2001.

Will insurance companies nonetheless assert the War Risk exclusion?

Despite the statements by domestic insurance companies that they will not apply the War Risk exclusion, the decision may not be entirely theirs. Most domestic property and casualty insurance companies reinsure great

percentages of their portfolios with reinsurance companies located in the Caribbean and in Europe. Those reinsurance companies are not under the same pressures as domestic insurance companies to accept coverage for losses from the terror attack, and may refuse to pay claims for reinsurance by domestic insurance companies based upon the War Risk exclusion. If this occurs, look for domestic insurance companies to revisit their promises not to apply the War Risk exclusion.

Do I have a property claim if my business did not suffer property damage?

Businesses that suffered business losses from the attack unrelated to any physical damage to their property may still have coverage under property insurance policies. The first coverage for which to look is *contingent business income* coverage, designed to cover a policyholder for loss of income caused by damage to or destruction of property owned by others. An example would be coverage purchased by a car maker to protect it if its sole supplier of a key component suffers destruction of its factory, and the car maker suffers a business income loss from its inability to complete manufacture of cars. Accordingly, a business which had an close relationship with a company physically located in a destroyed building may be able to recover for losses suffered in the wake of the destruction of that company’s physical plant.

Similarly, businesses can look to *contingent extra expense* coverage to pay for increased costs incurred after the disaster to minimize or avoid a contingent business income loss. Accordingly, if a business incurred additional expenses in order to avoid or minimize a contingent business income loss—for instance, by using a service provider located in New Jersey, rather than at the World Trade Center, or by purchasing cell phones for its employees—it may have coverage for those costs under contingent extra expense coverage.

Another potential coverage is provided by the *civil authority* clause, often listed as an “additional coverage” in property insurance policies. This clause is designed to provide coverage for business income losses incurred as a result of an order by a civil authority preventing access to the policyholder’s place of business. Obviously,

businesses in lower Manhattan may have coverage under such clauses—given that access to their premises was prohibited for a number of days after the attack and for some areas is still prohibited—but businesses located throughout the New York metropolitan area may also be able to make claims for business income losses if they can demonstrate that these losses stemmed from the inability of clients to get to their premises because of the orders of civil authorities.

Finally, affected businesses should also look to service interruption coverage, designed to provide coverage for business income losses attributable to dislocation of utility or telecommunications service. There are businesses in New York that still do not have telephone or internet service. Income losses from such dislocations should be covered under most property insurance policies. A business's costs in avoiding or minimizing service interruption losses—again, for instance, by purchasing cell phones for its employees—should also be covered, under contingent extra expense coverage, or under provisions in the policy promising to pay for a policyholder's efforts to avoid or minimize loss. Such clauses—which come in many varieties, including “sue and labor” and “expense to reduce loss” provisions—simply reinforce the established “loss mitigation” rule of insurance law, which holds that a policyholder's costs in avoiding or mitigating covered losses are themselves covered.

Can I trust insurance company promises to “pay” property insurance claims?

Insurance company assurances that property claims will be “paid” concede little. Property insurance disputes tend to be about *amounts of coverage* and not *coverage* itself. Given public sentiment in the immediate aftermath of the disaster, insurance companies could do little other than promise that they would “pay” claims; the value of those promises will only be fully known when the checks are cut. Note that insurance companies made similar promises after the 1993 bombing of the World Trade Center, and many policyholders who made claims after that disaster have not yet received full payment. Indeed, we are already hearing from affected retailers that insurance company adjusters are taking commercially unreason-

able positions regarding inventory damage. It is too soon to tell whether the insurance companies themselves will back down or fight with their policyholders.

How do I make a claim?

If you have not done so already, you must give notice of your claim, preferably by instructing your broker to give notice under all policies that conceivably could be implicated, and to copy you on the letter. If they fail to do so, send notice to your insurance company directly, preferably “Return Receipt Requested.”

When do I make a claim?

Immediately! If you feel there is any possibility that you may have a claim, you should give notice NOW. New York law is extremely unforgiving of “late” notice, and frequently finds that policyholders who wait even a few days to give notice have waived all rights under their policies. Give notice even if you do not have a handle on all the particulars of your claim; you can always supplement the notice later. Although we are seeking legislative relief from New York's common law rules on notice, there is no guarantee that it will be forthcoming.

Do I need help in pressing my claim?

If your claim involves the complex issues of business interruption or inventory valuation, you should consider hiring a public adjuster and/or an accounting firm that specializes in property insurance coverage accounting. The insurance company will almost certainly hire an “independent” adjuster, and one or more accounting firms that specialize in representing insurance companies; it will also probably hire, and conceal the hiring of, a law firm. If the insurance company presents an adjuster or accounting firm as “your” or an “independent” accountant, do not hesitate to do a little research on that firm. Insurance companies typically hire one of five or six accounting firms that specialize in representing insurance companies in property insurance disputes (that group may be expanding due to the size of this loss). Your insurance company's engagement of such a firm may give you an early indication of how it is treating your claim. Further, an insurance company may suggest that you should not

hire accountants, adjusters or law firms. You should try to get the insurance company to put such improper suggestions in writing.

What do I do if my insurance company says no?

Insurance companies frequently resort to the tactic of “rationing by hassle.” They deny claims and do all they can to discourage policyholders, finally paying only the persistent policyholders who do not take “no” for an answer. Accordingly, you should do everything in your power to demonstrate to the insurance company that you will not simply go away. For instance, write letters and demand information and positions on, and explanations of, coverage. If unanswered, write further letters incorporating all previous requests for information and demanding immediate responses.

Further, try to force your insurance company to commit its positions to writing. Insurance company claims handlers and adjusters frequently will try to change positions they have taken as the parameters of the loss become more clear. For instance, an insurance company may take the position that a policyholder’s business income loss from the destruction of one factory should be examined by looking at the performance of all the policyholder’s factories, because the insurance company assumes the other factories would pick up the business lost by the destroyed factory. Later, after determining that the other factories also suffered business income losses due to collateral effects of the loss, the insurance company may argue that only the income stream of the destroyed factory is relevant. To protect against such shifting positions, and to take full advantage of them if the claim is litigated, you should try to make the insurance company commit in writing to every position it takes.

As a last resort, if tenacity alone is insufficient to compel the insurance company to pay a claim, policyholders should consider legal avenues to secure their rights under their insurance policies. ■

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