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INSURANCE COVERAGE FOR BP OIL SPILL CLAIMS

BY FINLEY T. HARCKHAM

Many different types of companies and other enterprises have been harmed by the BP oil spill in the Gulf of Mexico, and they have been harmed in a variety of ways.

Most prevalent is the loss of profits suffered by companies that rely directly upon the Gulf waters and beaches for their livelihood; these include businesses in the commercial fishing, energy and tourism industries. The losses suffered in those industries set off chain reactions resulting in damages to their suppliers and customers, locally and across the country.

Other businesses will incur liability or at least legal fees in lawsuits alleging negligence and possibly malfeasance by corporate boards.

The losses and liabilities of many of the entities adversely affected by the spill are covered by property or liability insurance.

However, as explained below, certain conditions and exclusions found in many first-party property policies will present serious and sometimes fatal obstacles to insurance recoveries.

Don't Ignore Insurance

Pursuing claims through the independently administered BP fund or through the courts might fully compensate some businesses for their losses. However, policyholders should act now, if they have not done so already, to protect their rights to insurance coverage in case it is needed.

All insurance policies require prompt notice of losses suffered by and claims asserted against a policyholder. Although courts will often excuse that requirement if the late notice has not prejudiced the insurance company, policyholders should strive to avoid a potential problem by notifying their insurers as soon as possible and by documenting and preserving evidence of their losses as fully as possible.

Also, most property insurance policies contain contractual limitations on the time in which any suit against the insurer must be brought for nonpayment of a claim. Those periods can be as short as six months from the date of loss, though many states have statutorily mandated longer periods that supersede the contractual provisions.

Policyholders must check their policies carefully for such provisions and protect their interests, preferably by obtaining written agreement from the insurer to extend the suit deadline and allow sufficient time to resolve a claim or, if necessary, by filing a protective lawsuit.

Property Damage and Lost Profits

Coverage for damage to a company's property and loss of profits is found in its own first-party property insurance policies and perhaps in the property policies of other entities if it is named as an additional insured.

In addition to coverage for property loss, most of these policies insure against lost profits under a number of "time element" coverages for business interruption, contingent business interruption and orders of civil authority.

Business Interruption

Most property insurance policies pay for lost business income resulting from damage to covered property. This type of coverage is often referred to as business interruption insurance.

Many policies also provide so-called contingent business interruption coverage for losses stemming from damage to the property of a supplier or customer.

Both types of insurance require, as a predicate to coverage, that there be damage to property and profit loss from that damage.

The property damage requirement might preclude coverage for businesses that suffer losses simply because an offshore oil slick scared tourists away, because the Gulf waters are not the property of the policyholder or its customers or suppliers.

However, many businesses will be able to meet the property damage requirement if oil reaches their beaches, docks or industrial facilities, or fouls their boats or other equipment.

Also, companies that have licenses to use the Gulf waters and seabed for fishing, oil, and gas exploration and extraction or for other purposes may be able to establish coverage for contingent business interruption caused by damage to the property of a "supplier" (i.e., the government entity that has licensed its business activities in the Gulf).

For example, fishing companies that have business licenses to fish in certain waters may well be able to argue that property in which they have an insurable interest has been damaged.

Moreover, companies far away from the Gulf may have covered claims for contingent business interruption because of lost orders from companies that suffered physical damage.

Coverage for Civil Authority Orders

Coverage might also be provided for some companies under their insurance for business interruption resulting from orders of civil authority that prevent access to their property. An example was the order given by the mayor of New Orleans to evacuate the city when Hurricane Katrina was approaching in 2005.

Like business interruption insurance, coverage for orders of civil authority is typically tied to property damage, though it can be anyone's property, not just that of the policyholder or its suppliers or customers.

It is likely that many thorny issues will arise over coverage for business interruption caused by advisories against swimming, fishing and boating in contaminated areas and by denial of access to areas licensed for energy exploration or extraction.

Exclusions in Property Policy Coverage

If the requirements for coverage for business interruption or orders of civil authority can be met, policyholders may still have to contend with exclusions in their insurance policies. Perhaps most problematic will be the so-called pollution exclusions.

Many such exclusions are broadly worded, and they clearly include oil spills in certain circumstances. However, many pollution exclusions contain an exception for contamination that results from a "hostile fire."

A very good argument can be made that the current disaster resulted from a hostile fire, but insurance companies will likely contest that issue.

Many property policies also contain exclusions for damage to "land." Undoubtedly, insurers will rely upon that exclusion to deny coverage for claims based upon fouled beaches and fishing beds.

However, beaches that are groomed and developed may fall outside the exclusion, and damage to natural resources such as fish should not be considered "land."

Liability Insurance

Companies facing liabilities for alleged harm resulting from property damage or bodily injury can look for defense and indemnity from their liability insurance coverage.

Both general liability insurance policies and pollution liability insurance policies may cover such claims.

Companies (including any captive insurance companies) facing lawsuits should give notice under all primary, umbrella and excess liability policies in their insurance program despite a present \$75 million cap on liability. Legislation to eliminate caps on liability has been proposed.

A prudent policyholder facing oil spill liability claims ought to provide notice now rather than wait to see what happens with such legislative initiatives.

Directors and Officers Insurance

Derivative actions against directors and officers of companies involved in the Gulf of Mexico oil spill already have been filed in court. Dozens of such lawsuits are sure to follow. D&O insurance should be tapped to provide defense and indemnity of directors and officers facing such claims.

D&O insurance is written on a "claims made" basis, and it is extremely important to give immediate notice of claims or suits under those policies.

Protecting and Pursuing Rights to Coverage

The following steps can help to ensure that a company's rights to coverage are preserved, and they increase the likelihood of successfully resolving claims.

Provide prompt notice. Identify and provide notice under all policies that might provide coverage, and do so as promptly after losses are suffered or liability claims are asserted.

Comply with time deadlines. In addition to contractual statutes of limitation, property policies often set deadlines for the submission of proofs of loss and notice of intent to replace or actual replacement of damaged property. Identify and comply with all such deadlines or obtain written agreements extending the time to do so.

Assemble a claim team with all the skills needed to maximize the recovery. Although most policyholders only communicate with an adjuster, the insurance company has a team of attorneys, accountants and in-house claims personnel who are working hard to minimize the payment of your claim through coverage defenses and the calculation of the loss.

The policyholder's knowledge of its own business goes a long way to leveling the playing field but many arcane coverage issues and claims-adjustment practices require special expertise.

Keep a written record of everything that transpires with respect to the claim in correspondence to the insurer. This record may deter dilatory claims handling by putting the insurer on notice that its actions -- or inaction -- are being preserved for a possible bad-faith claim later on.

Insist the insurer pay all undisputed amounts before negotiating over the contested portion of a claim. Typically, the insurer will make a "good faith" partial payment and then pay little or nothing more until a final negotiation over all the open issues.

This partial payment allows the insurer to hold onto funds that should be paid out for undisputed portions of the claim and increases its leverage for later negotiations. Counter this strategy by forcing the insurance company to commit to a position on coverage and to pay the amounts due under its own analysis of the claim. Start by demanding a coverage determination.

Typically, insurers issue vague letters on the reservation of rights that quote numerous policy provisions without explaining how those clauses apply to the claim. Such a letter is intended to protect the insurance company from a waiver of defenses, but it does not fulfill its obligation to provide a timely coverage determination.

Respond to the letter on the reservation of rights with a demand for a detailed and specific coverage determination, reminding the insurer that its failure to do so may constitute bad faith. Also, demand payment of the undisputed amount of each element of the claim.

For example, a dispute over the period of restoration for business interruption coverage should not delay payment for property loss. If the insurance company will not agree to make partial payments, submit partial proofs of loss, which will trigger the deadlines for payment under unfair claims-handling statutes in most states.

Do not be shy about claiming losses that result from an insurer's dilatory handling of the claim. Under Louisiana law and that of other states, the period of restoration for a business interruption loss may be extended by the insurer's untimely payment of the property loss.

Business interruption coverage is provided for a hypothetical period of time that is reasonably necessary to restore the damaged property, but it should take into account the reality faced by the policyholder, including the delayed payment of insurance proceeds.

The insurance company may also be liable for consequential damages flowing from its breach by failing to make timely payments. Those damages might include lost profits or extra expenses that exceed the limits of coverage and lost value of the enterprise if it could not resume operations because the insurance company improperly withheld or delayed payment.

If a claim cannot be resolved through negotiation, you may have a choice of proceeding either to appraisal or litigation. Either party can demand appraisal, a form of arbitration provided for under many insurance policies, to resolve disputes over the amount of the loss. It can be a quick and inexpensive way to quantify the claim.

However, appraisal is not required and may not be appropriate when there are coverage issues to be resolved. For example, if the parties disagree over the amount of a business interruption loss because of a dispute over whether market conditions after the occurrence should be considered when calculating damages, the policyholder would be entitled to have that coverage issue decided in court. Appraisers, who typically are in the building trades, generally are not qualified to address such issues.

Also, bad-faith claims fall outside the scope of an appraisal clause and will have much greater value if placed before a jury. Thus, the policyholder must carefully consider its options and not necessarily feel compelled to agree to an appraisal simply because the amount of damages is one issue in dispute.

Conclusion

A key to the satisfactory resolution of insurance claims is for policyholders to take control of the process to the extent possible and to demonstrate a resolve to secure the coverage for which they paid. Now is the time to push Gulf oil spill claims to resolution.

About the Author

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