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Insurance Coverage

Tsunami-Related Financial Losses: Checklist Of Selected Insurance Coverage Considerations

The tsunami that swept through the Indian Ocean on December 26 has caused widespread loss of life, suffering and damage to livelihood, and sympathies are extended to all those affected. The disastrous tsunami also has caused substantial economic damage to various businesses; among the hardest hit are the hotels and resorts located throughout Thailand, including the otherwise bustling tourist destinations of Phuket, Phi Phi, Krabi and Trang, Malaysia's Langkawi and Penang, Sri Lanka, Maldives, Indonesia, and India, among other areas. Aside from the obvious business interruptions caused by complete destruction of property, many businesses have suffered a significant loss of revenue and related expenses due to (i) partial damage to hotel rooms, restaurants and swimming pools; (ii) lack of water, power supply or sewer services; (iii) lack of access to property because of, among other things, unavailable flights, inaccessible roads, and civil orders by governmental authorities; and (iv) voluminous cancellations of hotel bookings and travel excursions. For some of these businesses, the financial impact will be felt for years.

Given these losses, the availability of insurance, and in particular the role of business interruption insurance, will be a key consideration for affected businesses insofar as economic damages are concerned. Although it has been widely reported that the insurance industry does not view itself as having significant exposure for various reasons, many hotels and resorts – particularly those owned by companies that operate properties throughout the world – may well have been issued broadly worded policies that cover the types of business interruption losses arising from the tsunami disaster. Some of the relevant insurance policy provisions are relatively obscure as

they are not frequently implicated, and some have timing issues associated with them that could affect an insured's ability to procure coverage.

Of course, there are likely to be a variety of issues that arise out of tsunami-related claims for lost revenue and related expenses depending on an insured's individual circumstances. The following checklist of business interruption considerations is a general overview of selected issues that may be relevant to such claims:

IDENTIFYING POSSIBLE COVERAGE

Business interruption coverage typically is included as part of the first-party property insurance covering the assets of the insured entity and is often written in sweeping terms. While there are standard insurance industry forms for the coverage, some insurers have issued tailored policies to meet an insured's particular risk scenarios. Business interruption coverage generally covers the insured's loss of earnings or revenue resulting from property damage caused by an insured peril. Importantly, in addition to insuring lost earnings or revenue, such coverage also often includes, among other things:

- "extra expense" coverage, which generally promises coverage for certain extra expenses the insured incurred as a result of an insured event.
- "civil authority" coverage, which generally promises coverage for losses arising from an order of a governmental authority that interferes with normal business operations.
- "defense" coverage, which generally promises coverage for defense costs incurred with respect to claims alleging that the insured is responsible for damage to covered property of others.

- “ingress and egress” coverage, which generally promises coverage when access to a business premises is blocked for a time.
- “service interruption” coverage, which generally promises coverage when electric or other power supplies and services are interrupted.
- “claim preparation” coverage, which generally promises coverage for the costs associated with compiling and certifying a claim.

PRESENTING A CLAIM

Most policies purport to identify specific procedures that should be followed in presenting a business interruption claim (notice, proof of loss, suit limitation, etc.), and some of these procedures may have timing deadlines associated with them. Accordingly, an insured experiencing a loss potentially covered by a business interruption policy should promptly collect its loss information, evaluate the information in light of the policy wording (with counsel if necessary) and present it to the insurer in a timely and coverage-promoting manner. It is sometimes advisable to retain forensic accountants to assist in preparing and certifying a claim, and the costs associated with such an effort often are covered. If purported deadlines have passed, the insured’s pursuit of an insurance claim is not necessarily foreclosed. It may be that the insurer must show that it was prejudiced by an insured’s failure to meet a timing deadline before coverage will be forfeited on this basis.

COMMON INSURER RESPONSES

Insurers may raise any number of issues in response to a business interruption claim submitted by a policyholder. Issues raised by insurers may include the following:

- Did the alleged loss of income or extra expense arise out of damage to “insured property”? It is not always necessary that the relevant “property damage” occurred to property belonging to the insured. Many policies explicitly or implicitly also promise coverage when a supplier or, depending on the policy language, any other entity incurs property damage that results in an interruption of the insured’s business. Such coverage is sometimes known as “contingent business interruption” coverage and is often very broad. Similarly, there may be arguments for coverage where travel cancellations were due to civil orders, inaccessible roads and closed airports, as opposed to property damage to the hotel property itself.

- Was the damage to insured property caused by an “insured peril”? Many first-party property policies are written on an “all risk” basis, meaning that virtually any cause of property damage is within the scope of the policy, except those causes that are specifically and unambiguously enumerated in exclusions. Policies also sometimes contain particular provisions promising coverage for particular events (including orders of civil authority). Accordingly, although some policies may expressly exclude damage caused by “flood,” some broadly worded policies may nonetheless provide avenues to coverage through, for example, “civil authority” and “ingress/egress” coverage. There also could be disputes about whether the damage was a result of “earthquake” or “earth movement,” which may or may not be covered under certain first-party policies.

- Did an “interruption” of business result? While insurers sometimes take a narrow view of what may constitute an “interruption,” generally an insured may have a claim, depending on the circumstances, any time its income is adversely affected by an insured event.
- Was the interruption necessary? In many cases, this is not a controversial issue. In some cases, the insurer could question whether the claimed interruption is the result of a routine business decision as opposed to a “necessary” interruption under the circumstances.
- Does the loss meet any requirements the policy may have regarding duration of the interruption? Some policies have language limiting coverage to interruptions that extend for longer than a specified period of time. An insured should consider whether any such time frame specified in its policy is appropriate in light of its business.
- How long is the allowed “recovery period”? Policies sometimes include provisions specifying that the policy will only cover loss of income and related expenses for a specified period of time after an insured event occurs. This time frame typically should be tied to the time it would take the insured, employing reasonable mitigation efforts, to resume normal business operations under the circumstances.
- How many “occurrences” are implicated by the alleged loss? Many policies have “per occurrence” deductibles or other self-insurance features that may reduce the amount of coverage available

depending on how the “number of occurrences” issue is addressed. This issue can also impact the amount of per-occurrence policy limits that may be available to the insured.

- In the case of a claim resulting from loss of income or extra expenses associated with loss of electrical power or other services, did the interruption result from damage by an insured peril to property of the provider of the service? Some policies purport to exclude business interruption coverage arising from interruptions in electrical service (assuming the interruption is the controlling “cause” of the loss). Other policies have language explicitly promising time element coverage for losses arising out of service interruptions (including service interruptions to suppliers of the insured) but purport to require that the interruption resulted from damage to property of the service provider. In such a case, the circumstances and cause of the interruption, including whether the circumstances and cause can be characterized as resulting from damage to property of the service provider, may be critical to the availability of coverage. Policy language in this context varies considerably, however, and an insured must review carefully its own policy to assess the availability of time element coverage arising out of service interruption.

EVALUATING AND CHALLENGING INSURER POSITIONS

The validity of any defenses to coverage raised by insurers may well vary from state to state or country to country, as the courts of each state and many countries have developed differing approaches to coverage issues presented by business interruption claims. It is not always clear which state’s or country’s law will apply to a coverage dispute (in the absence of a specific choice-of-law provision, possibilities include, among other locations, the headquarters location of the insured or the insurer, the place where the insurance contract was issued or delivered, or the location of the damaged property). Moreover, the applicability of these potential defenses will also depend a great deal on the specific language used in the policy. Experienced insurance coverage counsel may be able to assist an insured in assessing the viability and strength of its potential claim. Sometimes insurers seek to limit an insured’s right to challenge an insurer’s coverage determination in court by specifying an appraisal and arbitration procedure in the policy.

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