Hunton & Williams

Client Alert

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Hurricane Irma: Insurance May Help Weather the Storm

On the heels of Harvey, Irma left her mark on Florida and is now spinning off into Georgia. Irma lived up to expectations, regaining strength to Category 4 before slicing through the Keys enroute to Florida's Gulf Coast. Beaten to the punch by Harvey, Irma was now the second Category 3+ storm (in as many weeks) to make landfall in the United States since Hurricane Wilma hit South Florida in October 2005.

As the winds diminish and floodwaters recede, significant damage to property and resulting interruptions to businesses are expected. Loss can be expected in areas affected directly and indirectly by the storm. And, the devastation is expected to be extraordinary. For example, the last time a hurricane of this magnitude (other than Harvey) hit the United States, the National Hurricane Center estimated that property damage alone exceeded $20 billion. *See* Tropical Cyclone Report, Hurricane Wilma (12 January 2006), http://www.nhc.noaa.gov/data/tcr/AL252005_Wilma.pdf. Those damage estimates pale in comparison to Harvey, whose damage estimates are in excess $180 billion. *See* Hurricane Harvey Damages Could Cost up to $180 Billion (*Fortune*, 03 Sept. 2017).

Structural damage from Irma will run the gamut, from water damage caused by storm surge, floodwaters and/or wind-driven rain; to broken windows and damaged and missing roofs caused by wind and/or blowing or falling debris; to, in many instances, total destruction of property caused by storm surge, floodwaters and/or the storm's 145+ MPH winds.

These physical losses will in turn, result in business interruptions and, consequently, lost earnings. Damage and destruction to property will in many cases lead to losses in business revenue and event cancellations. Damage to supply chains, vendors, customers and markets may lead to production slowdowns and delays. And damage to physical property may lead to increased building costs due to continually evolving building codes.

With damage and lost income estimates running into the billions, policyholders should review their insurance policies to determine whether or not their losses will be covered.

Types of Weather-Related Losses for Which Insurance May Be Available

Different businesses are affected differently by the same storm, and even the same physical damage. For instance, a physical loss to a part supplier caused by flooding or a lost roof might impact that business as a physical property loss and as a consequential loss of business income. That same event might also indirectly impact a product manufacturer that relies on the part supplier for components to its product. Likewise, the event might also affect a supplier of raw materials used by the part supplier, since the parts supplier's need for raw materials will be diminished during the time it takes to repair the physical damage. Companies supplying transportation, logistics and other essential support services also might be impacted, even though none has suffered physical damage.

Insurance is a resource to pay for these losses. Today's commercial property policies often contain a number of specialized coverages. Depending on the facts of the loss, one or more of those coverages may apply:

- Physical Loss or Damage to Insured Property: There is generally coverage for the cost to repair, replace or rebuild property that suffers physical loss or damage. Covered premises are usually listed or scheduled in the policy and may include not only buildings but also equipment and business personal property such as furniture, machinery and stock.

- Wind v. Flood: Many property policies contain substantially reduced sublimits, or exclusions, for flood damage. Commercial property policies in coastal regions may also exclude windstorm or provide a sublimit applicable to windstorm damage. Some businesses may have separate windstorm-specific policies that complement their commercial property insurance program. Thus, it is important that policyholders carefully examine the "cause" of their loss, and evaluate whether there are multiple causes, before submitting a claim.

- Debris Removal: Many commercial property policies provide coverage for the costs incurred in the removal of debris of covered property damaged by an insured peril such as windstorm. The maximum policy benefit for this coverage is usually expressed as a percentage of the total loss.

- Water Damage Caused by Burst Pipes and Water Mains: In general, water damage from a burst pipe inside a business will be covered. If an outside pipe or main bursts and causes damage, that also should be covered. It may be necessary, however, to demonstrate that the damage did indeed result from the burst pipe. If the insurer concludes that poor drainage—which is often a noncovered maintenance problem—caused the break or resulting damage, coverage may be denied. A claim also might be denied if policyholder negligence, such as leaving a vacant building without heat, caused the break. Further, even if the insurer does pay for the water damage, it may refuse to pay to repair the pipe itself, contending that the pipe was damaged by "wear and tear," which is often an excluded peril.

- Expenses Incurred in Attempting to Mitigate or Stop the Damage: Property policies typically cover expenses incurred in taking preventative measures to avoid loss or, where some loss has already occurred, further loss. In fact, many policies say the policyholder must take steps to safeguard the property and prevent further damage. A failure to do so could jeopardize coverage.

- Extra Expense Coverage: Repairing or replacing damaged property is not the only expense item when property is damaged. Often the cost of operating the business also goes up during the time when the business is affected by the storm or its aftermath. Extra expense coverage is intended to indemnify the policyholder for above-the-norm expenses caused by the insured event. Examples may include the cost of a generator when electricity is lost or costs incurred to operate at a temporary location.

- Business Interruption Coverage: Business interruption insurance is designed to cover lost income and profits resulting from the suspension of operations due to covered property damage. This would also include operating expenses that must be paid even if the business is not operational. Typically, this coverage does not apply until the expiration of a "waiting period" designated in the policy (typically 72 hours after the property damage occurs).

- Contingent Business Interruption Coverage ("CBI") claims: Contingent business interruption insurance and contingent extra expense coverage are common extensions to other insurance that reimburse lost profits and extra expenses that result from an interruption of business at the premises of a customer or supplier of the insured. In other words, the physical damage is not sustained by the insured. Rather, that damage is sustained by some entity with whom the insured has a business relationship and upon whom the insured relied prior to the loss event for a key aspect of the insured's business. The third party could be a supplier of critical materials or components; a transporter of goods, materials, or resources; or a wholesaler or retailer who purchases or consumes the insured's goods on a regular basis.

- Orders of Civil Authority: Coverage may also be available when business income is lost as a result of governmental directives preventing or restricting access to property. These losses may be recoverable even if the company's own property has not been damaged.

- Ingress/Egress Coverage: Similarly, many policies cover losses when ingress to or egress from a covered property is prevented or hindered by the event. This coverage may come into play in the event of road closures, the closing of mass transportation and other transportation problems.

- Service and Utility Interruptions: Losses and expenses caused by power, water and telecom outages can also have a significant impact on business operations and resulting losses may be covered under property insurance policies.

The precise terms of the insurance policy and applicable law govern the existence and extent of coverage. In addition, policies are often endorsed or contain exclusions that may expand or reduce coverage. Some applicable limitations on policies include sublimits on certain losses that limit the total available insurance for a particular type of damage, exclusions for flood or water damage, earth movement exclusions, government action exclusions that may not permit recovery for interruptions in business where government authorities limit access, etc. The burden is always upon the carrier to prove the terms and applicability of any exclusion of coverage in a policy. Exclusions are read narrowly and, where found to be ambiguous or not sufficiently notorious in the policy, they will be disregarded or construed in the light most favorable to the insured and in favor of coverage.

Policyholders are always best served by a careful analysis of the terms of their policies and the controlling law governing their insurer's obligations, as well as a precise documentation and presentation of their loss during the claim process.

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Hunton & Williams LLP's insurance recovery lawyers assist policyholders secure the full benefits to which they are entitled in the event of any type of loss, including amounts spent to defend or settle large-scale litigation. For more information, please contact the members of the firm's insurance coverage practice group.

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