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Exploring Insurance Recovery Paths After Major Disasters

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First-party property insurance policies sold to commercial policyholders often contain coverage extensions beyond the traditional property damage and business interruption coverages. While many businesses understandably focus on their traditional coverages, common extensions to these coverages may provide additional paths to recovery for storm losses from Harvey and Irma. These coverage extensions include "extra expense," "service interruption," "preservation of property," "civil authority" and "ingress/egress," and "electronic data processing" coverages.

Extra Expense and Contingent Extra Expense

Businesses that sustained major property damage from Harvey or Irma may incur substantial cleanup, repair, and/or replacement costs as they attempt to resume normal operations. "Extra expense" coverage (often purchased in or with standard form commercial property policies) covers expenses that exceed normal operating costs.[1] Insurers typically expect those extra expenses to facilitate ongoing operations while the policyholder's premises are being restored.

Examples of "extra expense" include the costs of moving and hauling equipment, purchasing backup generators, and hiring temporary labor. In storm-ravaged areas in Texas and Florida, extra expenses also likely include the costs of securing temporary facilities, equipment or services to operate the business while repairs to the insured's own property are ongoing. One potential area of dispute concerns coverage for the increased costs from a real estate shortage in affected areas as a result of numerous businesses seeking temporary quarters.[2]

"Contingent business interruption" and "contingent extra expense" provisions may also cover lost profits and extra expenses resulting from a business interruption at the premises of the policyholder's customer or supplier. For example, Harvey-related damage to manufacturing plants in Houston may force businesses that purchase supplies or components from those plants to incur extra expenses to secure substitutes. Those expenses may be considered "contingent extra expense."

Similarly, "contingent business interruption" coverage may permit recovery for business slowdowns due to problems suffered by direct and indirect suppliers or customers. Where the policy does not specifically limit coverage to those direct suppliers or customers, disputes frequently arise over whether losses arising from damage to indirect suppliers or customers may be covered. Also, some policies offer "interdependency" coverage to protect the policyholder against the risk that damage to a subsidiary may result in disruptions to the supply chain.

Service Interruption

Harvey and Irma resulted in widespread utility outages that affected millions of individuals and countless businesses. Losses arising from power disruptions may be covered under "service interruption" insurance. Under this coverage extension, policyholders typically can recover for property damage and business income losses arising from the disruption of utility services (such as electric, gas or water) to the insured premises. Steps taken by policyholders to minimize loss associated with a power outage, such as purchasing backup generators or utilizing alternative power sources, can help facilitate insurance recovery.

Notably, "service interruption" coverage may require damage to the property of the policyholder's utility supplier, or may require the damage to occur within a certain distance of the policyholder's own premises. Some commercial property policies exclude loss or damage due to utility failures that originated outside the insured premises. However, policies that contain "off-premises" utility coverage may respond to losses arising from lack of services that was caused by damage to utility services located away from the insured's premises. Because such coverages often exist in an intricate array of forms, endorsements and superseding endorsements, policyholders may want to seek guidance in analyzing such provisions.

Preservation of Property

Many businesses were aware that Harvey and Irma were approaching and took measures to protect their property. Those types of preventative measures are often covered under a "preservation of property" clause, which is also known as "sue and labor" protection. Post-loss mitigation or remedial measures, such as drying facilities damaged by water to prevent further loss, may also be covered.

Efforts to protect property in imminent danger should be compensable even if the property is ultimately spared from damage. Nor must protection or preservation efforts be successful in order to be insured. In addition, costs associated with protection and preservation of property are often not subject to deductibles or sublimits.

Still, insurers may attempt to reduce their liability or avoid coverage by contending that a business failed to adequately protect and preserve its property. In reality, policyholders are not required to take all possible measures to protect their property. The reasonableness of their efforts is measured on a case-by-case basis.

Civil Authority and Ingress/Egress

Business income losses resulting from governmental orders and restricted access to premises may fall within coverage provisions known as "civil authority" and "ingress/egress," respectively. "Civil authority" coverage generally applies to business income losses sustained when a governmental authority prohibits or impairs access to the policyholder's premises. For example, businesses that lost profits due to mandatory evacuations that were ordered in some Houston-area counties may be covered under the "civil authority" provision.

Even without evacuation orders, many employees and customers had great difficulty accessing buildings located in storm-affected areas. “Ingress/egress” coverage may apply to business income loss when access to (“ingress”) or from (“egress”) insured premises is restricted or prevented by physical damage near the insured premises.

Electronic Data Processing

Damage to electronic data, equipment or other hardware may be covered under an “electronic data processing” (EDP) provision. Typically, coverage is provided for events that can cause tangible loss to electronic equipment or data. These events may include fire, water, dust, and even changes to temperature or humidity levels. Some EDP clauses cover both property damage and business interruption due to, for example, the temporary loss of data processing facilities. As with the other coverage extensions, the precise scope of EDP coverage may vary from policy to policy.

Documenting Losses and Recovering Expenses

After experiencing a natural disaster, a business’s priority typically includes ensuring people’s safety, preserving its property and resuming its operations. To facilitate insurance recovery for property damage, business interruption loss and additional expenses, businesses should use reasonable best efforts to document and record their losses. Such records include bills and contracts, but also photographs or videos of damaged property. When assessing causes of damage or calculating losses, insurers will seek documentation, and good records will facilitate recovery.

In the aftermath of Harvey and Irma, some insurers have been rushing to send their claims adjusters (and sometimes their drones) to insured premises to survey the damage and process claims.[3] Insurers and independent adjusters on the ground may urge policyholders to accept the insurers’ assumptions about the cause of loss or their measurement of the loss in return for a prompt payment. Policyholders are often better served by waiting to conduct their own investigations and assessments rather than succumbing to pressure to accept insurers’ assumptions or measurements of loss.

And, where there are exclusions or sublimits based on peril, location or nature of property, it can be helpful to involve coverage counsel to ensure that the adjuster is using the appropriate methodology for the policy. Likewise, where coverage (or the amount of available limits) turns on causal issues, involving counsel early can mean avoiding fights down the road. Ultimately, the significant losses from Harvey and Irma warrant the exercise of the same level of careful diligence that any project of a similar financial magnitude would entail.

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[1] ISO CP 00 30 04 02 (“Business Income (and Extra Expense) Coverage Form”), available at http://www.propertyinsurancecoveragelaw.com/files/file/CP00300402.pdf.

[2] While “extra expense” coverage typically provides coverage in addition to business interruption insurance, we have seen insurers claim that losses are limited to “actual loss sustained” and ask for offsets to business interruption claims for extra expenses. These arguments generally lack support in the actual policy language. Policyholders should take care to guard against such erroneous notions.

[3] Suzanne Barlyn and Catherine Ngai, “Insurers Rush to Find, Deploy Adjusters for Harvey, Irma Claims,” Insurance Journal (Sept. 11, 2017), available at http://www.insurancejournal.com/news/national/2017/09/11/463806.htm(last accessed Sept. 14, 2017).
