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Feature Article

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Technology's Impact on Business Interruption Coverage— *Data Breaches, Protests, and Power Outages*

Business interruption insurance is designed to protect the prospective earnings of a business. It is also designed to do for the insured, in the event of a loss, what the business would have done for itself if an interruption in the operation of the business had not occurred. Thus, business interruption insurance is designed to *indemnify* for losses arising from a business's inability to continue its normal operations and functions. Coverage is generally triggered by the total or partial suspension of business operations due to the loss, loss of use, or damage to all or part of a building, plant, machinery, equipment, or other personal property as the result of a covered cause of loss.

Coverage is generally provided for the "period of restoration," which is usually considered to be the period required to rebuild, repair, or replace the damaged property at the described premises with reasonable speed and similar quality. It usually commences with the date of such damage or destruction and it is not generally limited by the date of the policy's expiration. Moreover, actual profits and business expenses covered by the policy are usually determined in a manner which gives due consideration for the character of the business along with the manner in which it conducts its activities.

Coverage Requirements

There are three separate components that must be connected in order to satisfy the requirements of the typical business interruption insuring agreement: (1) a covered cause of loss must cause *direct physical loss* of or damage to the property *at the described premises*; (2) the covered loss must cause a *necessary suspension or interruption of operations*; and (3) the *business income loss* must be caused by the suspension or interruption. For example, in *Gregory v. Continental Insurance Co.*, 575 So. 2d 534 (Miss. 1990), the court held that the business interruption loss coverage under a country club's multi-peril policy did not cover for loss arising from the shutdown of the entire golf course after trees had been blown onto the course during a hurricane. Rather, the coverage was limited to the business income loss that resulted *only* from the damage to buildings specifically described in the policy.

Claim Valuation

There is no prescribed or accepted formula for the determination of the actual loss of net profits and business expenses covered by business interruption insurance. The method employed, however, should test the past experience and the probabilities of the future, and the loss should be determined in a practical way, having regard for the nature of the business and the methods employed in its operation. Further, it should give practical effect to the intentions of the parties and the purpose of the insurance, as evidenced by the terms, conditions, and provisions of the policy. Thus, the insured's

books and accounting system are not controlling in determining the recoverable loss under a business interruption policy of insurance. On the other hand, they are not irrelevant and should be given such weight as practical judgment dictates.

The business interruption policy may be either "valued," in which case the value of the loss is agreed upon in advance and fixed by the policy, or "open," in which case the amount of the loss sustained is to be determined by competent proof. A policy also may be partially valued and partially open. Open policies have commonly provided for the recovery, during the time of the business suspension, of the insured's actual loss consisting of (1) the net profits thereby prevented from being earned (or gross earnings, less the cost of production or less the cost of the merchandise sold); (2) fixed charges and expenses necessarily continuing during the suspension period to the extent that they would have been earned; and (3) expenses incurred to reduce the loss.

Where the policy is open and the agreement of the insurer is to indemnify the insured within the policy limits for "actual loss," the burden is on the insured to prove the amount of loss, if any, that it has sustained. "Actual loss sustained" means lost net sales, less the cost of goods sold, preparation costs, and selling and administrative expenses.

Coverage Limitations

Business interruption policies typically provide that the insurer will be liable, within policy limits, for the insured's fixed charges and expenses necessarily continuing during the period following a total or partial suspension of business. Generally, however, coverage is provided only to the extent that income would have been earned if the contingency causing the suspension had not occurred.

In that regard, the ISO Business Income Coverage Form, CP 00 30 04 02 provides:

BUSINESS INCOME (AND EXTRA EXPENSE) COVERAGE FORM

A. Coverage

1. Business income
   Business income means the:

   a. Net Income (Net Profit or Loss before income taxes) that would have been earned or incurred; and

   b. Continuing normal operating expenses incurred, including payroll. For manufacturing risks, Net Income includes the net sales value of production.

2. Extra Expense

   a. Extra Expense coverage is provided at the premises described in the Declarations only if the Declarations show that Business Income coverage applies at that premises.

b. Extra Expense means necessary expenses you incur during the "period of restoration" that you would not have incurred if there had been no direct physical loss or damage to property caused by or resulting from a Covered Cause of Loss.

We will pay Extra Expense (other than the expense to repair or replace property to):

1. Avoid or minimize the "suspension" of business and to continue operations at the described premises or at replacement premises or temporary locations, including relocation expenses and costs to equip and operate the replacement location or temporary location.

2. Minimize the "suspension" of business if you cannot continue "operations."

We will also play Extra Expense to repair or replace property, but only to the Extent it reduces the amount of loss that otherwise would have been payable under this Coverage Form. ©ISO Properties, Inc., 2001

Definition of "Expense" Construed

Under a business interruption policy, issues frequently arise regarding the construction of the term "expense." For example, in the case of *Western American, Inc. v. Aetna Casualty & Surety Co.*, 915 F.2d 1181 (8th Cir. 1990), a fire destroyed most of Western's adhesives manufacturing plant. Aetna insured Western and paid the loss for the plant and its contents. A dispute arose, however, over the interpretation of the policy's gross earnings and extra expenses clauses. Aetna paid for the loss of gross earnings for 5¼ months of the suspension of business, but refused to pay for any extra expenses incurred to reduce losses during the rebuilding period. Western sued Aetna for lost rents, extra expenses and business interruption damages during the entire 10-month rebuilding period.

The jury awarded Western $759,616, the full extent of its coverage under the gross earnings clause, but denied recovery for lost rents and extra expenses. Aetna argued that Western failed to prove profit and expense figures that were necessary to calculate the business interruption damages under the gross earnings clause.

In its analysis, the district court considered a dispute involving a similar Aetna policy in *Associated Photographers, Inc. v. Aetna Casualty & Surety. Co.*, 677 F.2d 1251 (8th Cir. 1982), and approved essentially the same jury instruction. Aetna claimed the instruction was misleading because it did not specifically instruct the jury to consider the theoretical time it would have taken Western to rebuild, and because it directed the jury to add time to the business interruption period for delays caused by Aetna.

The appellate court agreed with the district court that there was sufficient evidence for the jury to determine the extra expenses that served to reduce the loss to Western's business due to the fire, and concluded that Aetna established no error in the district court's denial of its motion for a new trial. Also, the appellate court held that the jury's verdict denying Western's extra expense claim was amply supported by the evidence. Therefore, the judgment was affirmed.

Definition of "Depreciation" Construed

Under a business interruption policy, there are also usually questions concerning the extent to which an insured may include depreciation as an "expense" when the claimed business property has been totally destroyed. The court in *Cohen Furniture Co. v. St. Paul Insurance Co. of Illinois*, 214 Ill. App. 3d 408 (3d Dist. 1991), examined this issue and held that an insured may not include depreciation as an "expense" under a business interruption policy where the business property has been totally destroyed since depreciation only involves the useful life of an asset.

It is important to note, however, that in *Grevas v. United States Fidelity & Guaranty Co.*, 152 Ill. App. 2d 407 (1992), the Illinois Supreme Court distinguished the appellate court's decision in *Cohen*. In *Grevas*, the plaintiff owned an apartment building that suffered a loss by fire. The policyholder filed a claim with his insurer USF&G for loss of business income. The insurer calculated the damages by deducting the non-continuing expenses, such as utilities and lawn maintenance from the building's gross income, and deducted an additional amount for depreciation of the premises, claiming that depreciation was an expense that was non-continuing.

The trial court entered judgment for Grevas, finding that the policy was ambiguous as to whether depreciation was a non-continuing expense. The appellate court reversed and the plaintiff was granted leave to appeal. The Supreme Court distinguished *Cohen* based upon a finding that, unlike the policy in *Cohen*, Grevas' policy contained coverage for both loss of gross earnings (a general clause), as well as, coverage for loss of rents (a specific clause). The Supreme Court further held that, in such cases, where both a general and a specific provision in a contract address the same subject, the more specific clause controls. Accordingly, the Supreme Court concluded that under the loss of rents provision, depreciation is solely a tax device and is not considered a non-continuing charge or expense.

Policy Exclusions and Limitations

Most business interruption policies limit the insurer's liability to the extent that the business's charges and expenses would have been earned if the loss causing the interruption had not occurred. However, partial business interruption limits the insurer's liability to a *proportion* of the liability that would have been incurred by a total suspension of business. For example, in *Metalmasters of Minneapolis, Inc. v. Liberty Mutual Insurance Co.*, 461 N.W.2d 496 (Minn. Ct. App. 1990), the appellate court upheld the trial court's determination that Metalmasters incurred no "actual loss" in sales since Metalmasters presented no evidence of lost sales and proved no reduction in gross earnings. The appellate court further agreed with the trial court that, *without a proven actual loss*, the business interruption coverage did not extend to the value of services provided by Metalmasters' president, in the amount of $60,000, which were used on cleanup during the interruption of business rather than to the advantage of the corporation.

In a more recent case, *Lyon Metal Products, LLC v. Protection Mutual Insurance*, 321 Ill. App. 3d 330 (2d Dist. 2001), the court cited to *Metalmasters* when it analyzed an endorsement that stated that if the insured is able to continue its business operations through the use of any of its property, including the damaged inventory, then the insured is required to do so. The endorsement also provided that the insurer was liable for the actual loss sustained in net profit that was prevented from being earned due to the interruption, as well as, the fixed charges that would have been earned had no interruption occurred. Moreover, if there was enough inventory to meet the projected sales for the period of interruption, there was no loss of earnings.

On that note, the next section of this article will examine a number of recent decisions where courts have granted or denied business interruption coverage for losses arising out Data Breaches, Power Outages, Protests and Civil Disobedience.

Data Breaches, Ransomware and Other Types of Cyber Attacks

Coverage Granted

In *NMS Services Inc. v. Hartford,* 62 Fed. Appx. 511 (4th Cir. 2003), a former employee of the insured's software development company installed two hacking programs on the insured's network systems. The hack caused the erasure of vital computer files and databases necessary for the operation of the company's manufacturing, sales, and administrative systems.

The insurer denied coverage and litigation ensued. The court upheld coverage for business interruption under policy language stating that the insurer would pay for the "actual loss of Business Income" during the period of restoration. In that regard, the court noted that the suspension must be caused by "*direct physical loss of or damage* to property at the described premises." *NMS* Services, 62 Fed. Appx. At 514. The court further found that the insured suffered damage to its property, specifically, damage to the computers it owned, which satisfied the requirement of direct physical loss of or damage to property.

In *Lambrecht & Associates, Inc. v. State Farm Lloyds, 119 S.W.3d 16 (Tex. App. 2003),* the insured sought coverage for a loss of computer data and the related loss of business income after a virus caused the insured's computers to malfunction and eventually become completely useless. The insured's computer system had to be taken offline and its employees were unable to use their computers until the server was restored. The insurance policy at issue committed the insurer to pay for accidental direct physical loss to business personal property, and the actual loss of business income the insured sustained due to the necessary suspension of its operations during the period of restoration.

The court disagreed with the insurer's argument that loss of information on the computer systems was not a physical loss because the data did not exist in physical or tangible form. The court held that the plain language of the policy dictated that the personal property losses alleged by the insured were physical as a matter of law. The court also found the business income lost was covered under the policy.

In *Landmark American Insurance Co. v. Gulf Coast Analytical Laboratories, Inc., No. 10-809, 2012 WL 1094761 (M.D. La. March 26, 2012),* the insured provided chemical data analysis to the petrochemical industry and certain governmental agencies. Part of the insured's business involved analyzing chemical samples and storing the information as electronic data on a hard disk storage system. This system failed to read two hard disk drives and resulted in the corruption of data, resulting in severe recovery costs to third party vendors and losses in business income.

The insured sought coverage under its property policy. The policy covered risks of direct physical loss or damage, including computer viruses, except those causes of loss and damage listed in the Exclusions. The insurer filed suit seeking a declaratory judgment from the court that electronic data is not susceptible to direct physical loss or damage. The insurer argued that electronic data is intangible in nature and thus not susceptible to "direct, physical loss or damage" as a covered loss.

The court disagreed with the insurer and found that the insured's electronic data was "corporeal movable or physical in nature." The court further explained that the insured's electronic data "has physical existence, takes up space on the tape, disc, or hard drive, makes physical things happen, and can be perceived by the senses." *South Central Bell Telephone Co. v. Barthelemy*, 643 So. 2d 1240, 1246 (La. 1994). *See also Vonage Holdings Corp. v. Hartford Fire Insurance. Co.*, No. 11-6187, 2012 WL 1067694, at *3 (D.N.J. Mar. 28, 2012) (allegations that hackers took over and controlled servers sufficed to defeat insurer's motion to dismiss coverage complaint on the ground that the insured had suffered no loss of use under a first-party policy); *WMS Industries, Inc. v. Federal Insurance Co*., 384 F. Appx. 372, 375 (5th Cir. 2010) (the Fifth Circuit found business interruption and contingent business interruption coverage for post-Katrina interruptions of network of slot machines and electronic gambling machines); *Southeast Mental Health Center, Inc. v. Pacific Insurance Co., Ltd., Co*., 439 F. Supp. 2d 831, 837 (W.D. Tenn. 2006) ("The Court finds that the corruption of the pharmacy computer constitutes 'direct physical loss of or damage to property' under the business interruption policy)."

Coverage Denied

In *Ward General Insurance Services, Inc. v. Employers Fire Insurance Co.*, 114 Cal. App. 4th 548 (2003), the insured suffered a computer crash during a system update that resulted in significant losses of electronically stored data. Restoration of the data came at great expense to the company in terms of lost productivity, commissions, and profits. When presented with the insured's claim, the insurer denied coverage under the policy on the grounds that the loss did not result in "direct physical loss of or damage to" property. In the resulting coverage lawsuit, the court agreed with the insurer. In particular, the court noted that the data is stored on a tangible medium and that the information itself remains intangible. The court concluded that electronic data loss could not provide a basis for coverage under a first-party insurance policy because electronic data does not have a "material existence."

In *Taylor & Lieberman v. Federal Insurance Co.*, 681 Fed. Appx. 627 (9th Cir. 2017), the court found an accounting firm was not covered under a crime policy for the loss of a client's funds through a fraudster's email scheme. The court held that the loss didn't fall under any of the relevant policy provisions.

In *Aqua Star (USA) Corp. v. Travelers Casualty and Surety Co. of America*, No. C14-1368RSL 2016 U.S. Dist. LEXIS 88985 (W.D. Wash. July 8, 2016), a phishing scam caused the insured's vice president to be tricked into sending funds to an overseas fraudster. The court held coverage was barred by an exclusion for losses "resulting directly or indirectly from the input of electronic data by a person with authority" (The VP had such authority).

P.F. Chang's China Bistro Inc. v. Federal Insurance Co., No. CV-15-01322-PHX-SMM, 2016 U.S. Dist. LEXIS 70749 (D. Ariz. May 31, 2016), involved a data breach that compromised credit cards of over 60,000 of insured's customers. The court found that the cyber policy was intended to provide coverage for claimants who themselves had suffered a privacy injury, and not for the insured's economic loss arising out of the theft of customers records.

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Power Outages

Coverage Granted

In *Southeast Mental Healthcare Center, Inc. v. Pacific Insurance Co., Ltd.*, 439 F. Supp. 2d 831 (W.D. Tenn. 2006), a heavy rain and windstorm resulted in the loss of power at the insured's property. The insured alleged that the power outage also damaged its pharmacy's computer, which resulted in the loss of data. Furthermore, the insured claimed its "operations were suspended and it lost significant business income." *Southeast Mental Healthcare*, 439 F. Supp. 2d at 834. The insurer argued that the business losses due to the damaged pharmacy computer were not covered because there was no direct physical damage to the computer. The court rejected this argument and found the damage to the pharmacy computer constituted direct physical loss of or damage to property under the interruption policy.

In *Wakefern Food Corp. v. Liberty Mutual Fire Insurance Co., 406 N.J. Super. 524 (2009),* problems with the North American power grid resulted in prolonged electrical power outages through much of the northeastern United States and eastern Canada. The insured supermarkets suffered severe losses due to food spoilage and subsequent loss of business. The insureds had purchased, in addition to a basic property policy, a "Services Away From Covered Location Coverage Extension." The coverage extension "extended coverage for consequential loss or damage resulting from an interruption of electrical power to [the insureds'] supermarkets where that interruption is caused by 'physical damage' to specified electrical equipment and property located away from the supermarkets." *Wakefern*, 406 N.J. Super. at 530.

Following the outage, the insureds sought coverage for spoiled food and business interruption and the insurer denied coverage. The insurer deemed the food-spoilage damages to be consequential and not direct losses. The trial court granted summary judgment for the insurer holding that the grid was not physically damaged because it could be returned to service after the interruption.

On appeal, the court determined the term "physical damage" was ambiguous. The court found that the electrical grid was physically damaged because, due to a physical incident or series of incidents, the grid and its component generators and transmission lines were physically incapable of performing their essential function of providing electricity. Moreover, the court found that from the perspective of the millions of customers deprived of electric power for several days, the system certainly suffered physical damage, because it was incapable of providing electricity. The Appellate Division subsequently reversed the trial court opinion and remanded the case.

In *Cincinnati Insurance Co. v. Washer & Refrigeration Supply Co., Inc.*, No. 07-0330-CG-B, 2008 U.S. Dist. LEXIS 112464 (S.D. Ala. Aug. 8, 2008), the court found the policy provisions at issue were unambiguous in regard to power outages and inaccessibility problems caused by Hurricane Katrina. The business income and extra expense coverage form clearly stated that to be covered, a "suspension" must be caused by direct physical loss of or damage to property. There was no dispute that the insured's location incurred direct physical loss of or damage to property from the hurricane. Thus, the court concluded, that property damage entitled the insured to business interruption and extra expense coverage.

In *Allianz Cornhill Int'l v. Great Lakes Chemical Corp.*, No. H-04-1668, 2006 U.S. Dist. LEXIS 17828 (S.D. Tex. Mar. 24, 2006), two different ice storms caused extensive power outages. The power outages caused subsequent mechanical failures. After the storms, the insured filed a claim for business interruption. The court ultimately held there was coverage under the policy after determining that the ice storm—a covered peril—was the proximate cause of the business interruption losses.

In *American Guaranty & Liability Insurance v. Ingram Micro, Inc.*, No. 99-185, 2000 WL 726789 (D. Az. April 18, 2000), Ingram's computer systems were rendered inoperable due to a power outage. Specifically, Ingram experienced a 90-minute loss of programming information and custom configurations necessary for function. Although the Data Center was up and running after 90 minutes (and after Ingram employees manually reloaded the data), the connections from the Center to the rest of the system were interrupted for 8 hours until employees manually bypassed a malfunctioning matrix switch. Days later, to ultimately fix the problem, the matrix switch had to be reprogrammed.

American Guarantee denied coverage under a property damage policy that insured against certain business interruption and service interruption losses, claiming there was no "physical damage" because the computer system and matrix switch still maintained their capability to perform their intended functions. The court found coverage since, until the restorative work was performed by Ingram's employees, the mainframe and connectivity to the rest of the system were inoperable and therefore "physically damaged."

In support of its conclusion, the court did not cite any case law. Rather, after noting that we live in a time "when computer technology dominates our professional as well as personal lives," it relied on the definitions of "damage" found in various federal and state computer crime statutes, such as 18 U.S.C. § 1030 (West 1999). *Ingram*, 2000 WL 726789, at *3. That statute defines "damage" as "any impairment to the integrity or availability of data, a program, a system, or information." 18 U.S.C. § 1030(e)(8). Similarly, Missouri defines damage to a computer as any alteration, deletion, or destruction of any part of a computer system or network.

The court was cognizant of the fact that the foregoing definitions originate in penal statutes and not in insurance case law. However, since various legislatures have termed interruption of a computer's services "damage," it opined that it would be "archaic" to limit the policy definition to the language advanced by the insurer. *Ingram*, 2000 WL 726789, at *3.

Coverage Denied

In *Pentair, Inc. v. American Guarantee & Liability Insurance Co.*, 400 F.3d 613 (8th Cir. 2005), an earthquake caused a loss of power to two Taiwanese factories. The factories could not supply products to a subsidiary of Pentair for two weeks. Pentair argued that the property of the Taiwanese factories suffered "direct physical loss or damage" when the power outages prevented the factories from performing their function of manufacturing products. Although the court noted that once physical loss or damage is established, loss of use or function is certainly relevant in determining the amount of loss, particularly a business interruption loss. The court, nonetheless, refused to adopt the position that "direct physical loss or damage is established *whenever* property cannot be used for its intended purpose." *Pentair*, 400 F.3d at 616. Therefore, summary judgment for the insurer was affirmed.

In *Red Bird Egg Farms, Inc. v. Pennsylvania Manufacturers Indemnity Co.*, 15 Fed. Appx. 149 (4th Cir. 2001), a lightning strike caused a power outage that resulted in the burning of 100 ventilation vans and the deaths of 500,000 chickens. The insured-plaintiff filed a claim, which the defendant-insurer paid in satisfaction, with the exception of the business interruption claim. The district court ruled that there was no ambiguity in the relevant portions of the insurance policy that did not cover power outages, and thus plaintiff was not due coverage for business interruption. The appellate court affirmed the denial.

In *Newman Myers Kreines Gross, P.C. v. Great Northern Insurance Co.*, 17 F. Supp. 3d 323 (S.D.N.Y. 2014), widespread power outages during and after Hurricane Sandy led to plaintiff law firm being without power for several

days. The firm brought suit under its property insurance policy arguing for loss of business income and extra expenses occasioned by its inability to access its office during the power outage. The defendant-insurer denied the claim on the ground that the firm did not suffer a covered loss and litigation followed.

The court analyzed the policy and determined that under the "Loss of Utilities" provision, and the general "Premises Coverage" provision of the "Business Income With Extra Expense For Law Firms" section, loss of business income and extra expense coverage was limited to "the period of restoration," not to exceed the applicable Limit of Insurance. The term "period of restoration," was defined in the policy of "the period of time that . . . begins immediately after the time of direct physical loss or damage by a covered peril to property," and "will continue until your operations are restored, . . . including the time required to repair or replace property." *Newman Myers*, 17 F. Supp. 3d at 332.

The court reasoned that the words "repair" and "replace" contemplated physical damage to the insured premises as opposed to loss of use of it. *Id.* (*citing United Airlines Inc. v. Insurance Co. of the State of Pennsylvania*, 385 F. Supp. 2d 343, 349 (S.D.N.Y. 2005) (policy language limiting coverage "for only such length of time [needed] to rebuild, repair or replace such part of the Insured Location(s) as has been damaged or destroyed" supports the notion that "physical damage is required before business interruption coverage is paid" in regard to September 11, 2001 events.)); *see also Philadelphia Parking Auth. v. Federal Insurance Co.*, 385 F. Supp. 2d 280, 287 (S.D.N.Y. 2005) ("'Rebuild,' 'repair' and 'replace' all strongly suggest that the damage contemplated by the Policy is physical in nature."); *Roundabout Theater Co. v. Continential Casualty Co.*, 302 A.D.2d 1, 8 (N.Y. 2002) (stating that, absent a physical damage requirement, a provision limiting coverage to the time necessary to "rebuild, repair, or replace" would "be meaningless)."

"By contrast", the court explained, "construing 'direct physical' loss or damage to require actual physical damage to the insured premises gives effect to all provisions of the Policy." *Newman Myers*, 17 F. Supp. 3d at 332. The court, therefore, held that the insured did not meet its burden of showing the policy covered the losses and entered summary judgment in favor of the insurer.

In *Schultz Furriers, Inc. v. Travelers Casualty Insurance Co. of America*, No. A-0170-15T1, 2017 N.J. Super. Unpub. LEXIS 1072 (N.J. Super. Ct. May 3, 2017), the plaintiff leased premises and operated a business selling luxury outerwear and fur garments, in addition to garment cleaning, storage, and repair services. The plaintiff obtained a commercial insurance policy from defendant covering certain losses pertaining to that business. Hurricane Sandy knocked down certain electrical transformers, which disrupted the power supply and caused plaintiff to close its business. The plaintiff filed an insurance claim with defendant seeking coverage associated with its business interruption. The defendant disclaimed coverage, and plaintiff filed suit.

The defendant, relying on a "Power Pac Endorsement" in the insurance policy, tendered $2,500 to the plaintiff for the business loss. Although the plaintiff sought coverage for more than that, the defendant concluded that this payment constituted the maximum amount of insurance coverage for the business interruption. In issuing the orders under review, the trial judge agreed with the defendant's interpretation of the insurance policy.

On appeal, the plaintiff argued the language of the insurance policy was ambiguous; the insurance policy was an "all risk" policy and thus the burden of proving an exclusion rested with defendant; and plaintiff was entitled to insurance coverage under the civil authority section of the policy. The appellate court rejected the plaintiff's arguments and affirmed the trial court holding that the plaintiff was not covered because the policy unambiguously excluded coverage for loss or damage caused by windstorms.

In *Howard Berger Co., LLC v. Liberty Mututal Fire Insurance*, No. 1:14-cv-06592, 2017 U.S. Dist. LEXIS 78336 (D.N.J 2017), the plaintiff insured sought business interruption coverage due to power outages caused by Hurricane

Sandy. The policy at issued covered "any electrical generating plant…or any other plant or facility responsible for providing the services…" However, the cause of the plaintiff insured's power outage was due to damage to a wooden pole and an overhead distribution line that directly supplied power to the premises. The policy, however, did not cover "overhead transmission and distribution lines." Thus, the court determined plaintiff insured was precluded coverage for loss of business income due to the electrical interruption.

Other cases of interest include *Houstoun v. Escalante's Comida Fina, Inc.*, No. 01-11-00745-CV, 2014 Tex. App. LEXIS 5935 (1st Dist. June 3, 2014), in which the appellate court held that the trial court erred in awarding judgment to an insured in its action against an insurance agent for breach of contract because of the jury's finding that insured's business interruption loss from a hurricane, not covered by its policy with the insurer, would have been covered by a prior policy with another insurance company, was not supported by the evidence, and *Lyle Enterprizes v. AXA Re Property and Casualty Insurance Co.*, No. 04-75099, 2005 U.S. Dist. LEXIS 28622 (E.D. Mich. Nov. 18, 2005), in which the court held that because the failure of power occurred away from the insured's store and did not result in a covered cause of loss, the exception to the policy's power failure exclusion was not applicable. Consequently, the exclusion precluded coverage for all of the insured's losses. Therefore, summary judgment was granted in favor of the insurer.

Protests and Civil Disobedience

Coverage Granted

In *Southlanes Bowl, Inc. v. Lumbermen's Mutual Insurance Co.*, 46 Mich. App. 758 (Mich. Ct. App. 1973), the plaintiffs were engaged in the business of operating places of amusement consisting of bowling alleys, restaurants, taverns, snack bars, cocktail lounges, and motels. These establishments were covered by policies of business-interruption insurance drawn and issued by the defendant.

In the summer of 1967 and again after the assassination of Dr. Martin Luther King, Jr., in April of 1968, widespread riots and civil commotion accompanied by burning and looting erupted in and around the City of Detroit. However, none of the plaintiffs' businesses were physically damaged. On each occasion, the Governor declared a state of emergency, imposed a curfew, and closed all places of amusement within the cities of Detroit, Highland Park, Hamtramck, Ecorse, and River Rouge. In accordance with the Governor's order, plaintiffs closed their establishments and as a result suffered a $49,687.69 net loss.

At trial, the plaintiffs asserted that the risk insured against under the business-interruption policies here in question was the prohibition of access to their businesses by order of a civil authority arising from any of the enumerated perils, *e.g.*, riot, without any requirement of physical damage to the insured property. On the other hand, the defendants contended that under the terms of the business-interruption policies there is no coverage unless there has been direct and actual physical damage to the insured property; and inasmuch as none was inflicted here, it was not liable to pay benefits for plaintiffs' net loss. The trial court concurred and found for these defendants.

On appeal, the appellate court considered whether under the language of the business-interruption policy here in question, physical damage to the insured premises is a condition precedent to the insurer's liability to pay benefits. In that regard, the court reversed the trial court and held that where the insured businesses were closed by order of a civil authority, physical damage to the insured premises was not a prerequisite to the insurer's obligation to reimburse the

insured for the net losses resulting therefrom. Southlanes, 46 Mich. App. at 760, citing *Sloan v Phoenix of Hartford Insurance Co.*, 46 Mich. App. 46 (1973). (Note: Very few courts have found that access was prohibited where the order of a civil authority required the insured's premises to close, thereby invoking coverage for business losses.)

Coverage Denied

Courts have denied coverage under a "civil authority" provision in the following cases where the civil authority order had only the indirect effect of restricting or hampering access to the business premises. *See 54th Street Limited Partners, L.P. v. Fidelity and Guaranty Insurance Co.*, 306 A.D.2d 67 (N.Y. 2003) (no coverage where "vehicular and pedestrian traffic in the area was diverted, [but] access to the restaurant was not denied; the restaurant was accessible to the public, plaintiff's employees and its vendors"); *St. Paul Mercury Insurance Co. v. Magnolia Lady, Inc.*, No. 2:97CV-153-B-B,1999 U.S. Dist. , at *8 (N.D. Miss. Nov. 4, 1999) (no coverage when state authorities hampered access to claimant's casino-hotel by closing damaged bridge, because "casino-hotel was accessible during the period of time the bridge was under repair"); *Syufy Enterprises v. The Home Insurance Co. of Indiana*, No. 94-0756FMS, 1995 U.S. Dist. LEXIS 3771, , at **5-6 (N.D. Cal. Mar. 21, 1995) (rejecting plaintiff's claim for business interruption coverage for losses sustained during curfews imposed after the Rodney King verdict where policy required that access to plaintiff's premises be specifically prohibited by order of civil authority, and a direct result of damage to or destruction of property adjacent to the premises, because curfews were imposed to prevent potential looting and rioting and not as a result of adjacent property damage).

Conclusion

It is very interesting to witness the evolution of business interruption coverage and how courts are changing their interpretation of these policies as technology advances. That said, as more and more businesses come to realize that cyber-attacks and data breaches pose a serious threat to their operations and contingency planning, the insurance industry will increasingly be called upon to develop new products, which are untested in the courtroom, in an effort to address these loss exposures. Still, for now and seemingly in the immediate future, business interruption policies and language vary widely amongst insurers. For the time being, courts will continue to grapple and likely offer inconsistent opinions on how these policies should be construed.

About the Author

Rick Hammond is a Partner with *HeplerBroom LLC*. He serves as national counsel on matters relating to property insurance coverage, fire and explosion cases, bad faith, and as counsel to corporate executives, municipalities and elected officials on high-profile business litigation cases. Mr. Hammond is Past-President of the Illinois Association of Defense Trial Counsel, formerly served on the faculty and Board of Directors of the Insurance School of Chicago, and he is a columnist for the International Association of Special Investigation Units' (IASIU) magazine, *SIU Today*. Mr. Hammond is a member of the Federation of Defense and Corporate Counsel and former Chair of their Property Insurance Law

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