

ANALYTICAL APPROACH TO BUSINESS  
INTERRUPTION, EXTRA EXPENSE, AND  
CIVIL AUTHORITY COVERAGE ISSUES

*Peter E. Kanaris*

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In the last seven years, there have been more reported decisions interpreting business interruption, extra expense, and civil authority coverages than in the previous forty. Courts have confronted a variety of factual scenarios and provisions peculiar to these first-party policies. However, key coverage elements have been reconfirmed. Specifically, the necessity of physical damage from a covered peril either preventing the business operations or directly resulting in an order of civil authority remains a vital prerequisite to coverage. This article examines an analytical approach that has emerged in the case law to address business interruption, extra expense, and civil authority coverage. In addition, this article provides a framework for analysis of the issues that could potentially result in an impediment to coverage or affect the determination of the loss amount.

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*Peter E. Kanaris is co-managing director of Fisher Kanaris, P.C., in Chicago, where his practice focuses on first-party insurance and reinsurance coverage; and antitrust, commercial, construction, environmental and toxic tort, and employee dispute law.*

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## I. BUSINESS INTERRUPTION COVERAGE

After the initial step of a careful reading of the insurance contract, virtually all business interruption claims, as a general rule, can be analyzed within the following framework: (1) Did a covered peril (2) cause direct physical damage or physical loss (3) to insured property or property at the described location (4) during the policy period (5) resulting in an actual loss of business income (6) due to the necessary suspension of the insured's operations?

The insured bears the burden of proving each of the foregoing elements to a business interruption claim; in particular, the necessary suspension of operations and actual loss of income must have been directly sustained as a result of the physical damage. When the physical damage has been repaired to allow the business to operate, the period of indemnity ends.

The general purpose of business interruption insurance is to indemnify the insured against losses arising from an inability to continue normal business operations due to an insured loss.<sup>1</sup> The goal is to preserve the continuity of the insured's earnings during the period of repairing the covered physical loss to the insured property.<sup>2</sup> In other words, the policy coverage "is designed to do for the insured in the event of business interruption caused by [a covered peril], just what the business itself would have done if no interruption had occurred—no more."<sup>3</sup> That does not mean that the recovery must leave the insured in the same financial position had there been no interruption of business.<sup>4</sup> Thus, new expenses incurred as a result of business interruption are not covered, and expenses saved due to the interruption of business are not recoverable.<sup>5</sup>

### A. *Direct Physical Damage*

In order to sustain any business interruption claim, the insured must prove the existence of covered physical damage. As a practical matter, there must be a material or substantive physical change to the insured property.<sup>6</sup> The subjective belief of damage due to the unmerchantability

1. *Pac. Coast Eng'g Co. v. St. Paul Fire & Marine Ins. Co.*, 88 Cal. Rptr. 122 (Ct. App. 1970); *see also* 15 GEORGE J. COUCH, *COUCH CYCLOPEDIA OF INSURANCE LAW* § 57:28-32 (2d ed. 1983).

2. *Gordon Chem. Co. v. Aetna Cas. & Sur. Co.*, 266 N.E. 2d 653 (Mass. 1971).

3. *Nat'l Union Fire Ins. Co. of Pittsburgh v. Anderson-Prichard Oil Corp.*, 141 F.2d 443, 446 (10th Cir. 1944); *Hartford Fire Ins. Co. v. Wilson & Toomer Fertilizer Co.*, 4 F.2d 835 (5th Cir. 1925).

4. *E. Associated Coal Corp. v. Aetna Cas. & Sur. Co.*, 632 F.2d 1068, 1079 (3d Cir. 1980) (insured not permitted to recover new expenses that would not have been incurred absent the interruption of business).

5. *Associated Photographers, Inc. v. Aetna Cas. & Sur. Co.*, 677 F.2d 1251, 1254 (8th Cir. 1982).

6. *Cope Constr. Co. v. Am. Home Assurance Co.*, 622 P.2d 395 (Wash. Ct. App. 1980).

of insured property is insufficient to prove physical loss or damage.<sup>7</sup> Instead, the insured must demonstrate a material occurrence or injury to the insured property.<sup>8</sup>

Two cases arising from the civil disturbances in the 1960s illustrate the physical damage requirement. In *Brothers Inc. v. Liberty Mutual Fire Insurance Co.*<sup>9</sup> and *Two Caesars Corp. v. Jefferson Insurance Co.*,<sup>10</sup> the insureds made claims for business interruption that allegedly resulted from a curfew imposed by a city ordinance. Each insured argued that its business losses due to the curfew were covered under the business interruption provisions of the policies in question. In each case, because the insureds failed to allege and prove damage or destruction to the insured property, the court held that there was no business interruption coverage.

Similarly, in *National Children's Expositions Corp. v. Anchor Insurance Co.*,<sup>11</sup> the court rejected the business interruption claim for want of direct physical damage to the insured property. There, an unprecedented snowstorm reduced attendance at an exhibition. Neither the exhibition hall nor any other insured property sustained physical damage from the snowstorm. Accordingly, the court found no business interruption coverage.

Somewhat problematical to the physical damage requirement is the decision of the Eighth Circuit in *Hampton Foods, Inc. v. Aetna Casualty & Surety Co.*,<sup>12</sup> where the insured recovered lost business profits when its grocery store was in imminent danger of collapse.<sup>13</sup> Several days after a severe windstorm, the city building commissioner ordered the insured to vacate the premises because of the potential for collapse. The insured made a business interruption claim that was denied on several grounds, including the lack of any direct physical loss.

The Eighth Circuit found coverage and is the only known court that has held the terms *risk of direct physical loss or damage* to be ambiguous. The court found that the all-risk insuring agreement could reasonably be interpreted to mean danger of physical loss. Inasmuch as the insured property was in "immediate, concrete, and direct" danger of collapse, the court opined that coverage had been established.

No case decided after *Hampton Foods* has followed its reasoning. Although the decision rests on a finding that the term *risk of direct physical loss or damage* is ambiguous, a material change to the grocery store building

7. *Glens Falls Ins. Co. v. Covert*, 526 S.W.2d 222 (Tex. App. 1975).

8. *J.N. Futia Co. v. Nat'l Sur. Co.*, 30 A.D.2d 989, 294 N.Y.S.2d 74 (App. Div. 1968).

9. 268 A.2d 611 (D.C. 1970).

10. 280 A.2d 305 (D.C. 1971).

11. 279 F.2d 428 (2d Cir. 1960).

12. 787 F.2d 349 (8th Cir. 1986).

13. *But see Cleland Simpson Co. v. Firemen's Ins. Co.*, 140 A.2d 41 (Pa. 1958) (threat of fire absent actual physical damage insufficient to trigger business interruption).

had occurred. The windstorm damage made collapse of the building imminent because of a material injury to its structural integrity. The imminent collapse due to the physical injury to the structure necessarily interrupted the business. The court could, therefore, have fashioned a rational basis for coverage without resorting to a finding of ambiguity that runs counter to more than eighty-five years of precedent on the meaning of *at risk of direct physical loss or damage*.<sup>14</sup>

Indeed, since the *Hampton Foods* decision, almost all courts continue to require physical loss or damage to the insured property as a condition precedent to business interruption coverage. For instance, in *Witcher Construction Co. v. St. Paul Fire & Marine Insurance Co.*,<sup>15</sup> an explosion happened four blocks away from the insured's construction project. No visible damage to the construction was apparent; however, the insured chose to stop construction until experts inspected the project to determine whether there had been any structural damage. Expert examination confirmed no damage to the construction, but the insured still made a claim for the losses stemming from the construction downtime. The Minnesota court rejected the insured's contention that the coverage grant relating to risks of direct physical loss was ambiguous. The court held that to sustain a claim for business interruption, the insured must first demonstrate physical damage to the insured property and not merely a suspension of operations. Under the circumstances, there was no business interruption coverage.<sup>16</sup>

Recently, the Second Circuit affirmed the Southern District of New York's confirmation of the physical damage requirement in *United Air Lines, Inc. v. Insurance Co. of the State of Pennsylvania*.<sup>17</sup> In that case, the insured sought business interruption coverage for its systemwide revenue loss resulting from the terrorist attacks that destroyed its ticket counter in the World Trade Center. The insured further asserted that its "gate property at Washington Reagan National Airport was physically impacted by the terrorist attack at the Pentagon, resulting in the accumulation of ash at the United gates."<sup>18</sup> Additionally, the insured argued that the policy did not require physical damage to trigger business interruption coverage as the insurer did not insert the word *physical* before the word *damage* in the policy. In rejecting the insured's contention, the court held that physical damage is a prerequisite to coverage for business interruption under the policy. Indeed, a contrary ruling would transform the business interruption

14. *British & Foreign Marine Ins. Co. v. Gaunt*, [1921] 2 A.C. 41, 90 L.J.K.B. 801.

15. 550 N.W. 2d 1 (Minn. Ct. App. 1996).

16. *Id.*

17. 385 F. Supp. 2d 343 (S.D.N.Y. 2005), *aff'd*, 439 F.3d 128 (2d Cir. 2006).

18. *Id.* at 346.

provision into a financial guarantee provision, thereby circumventing the plain language of the policy as a whole.<sup>19</sup>

The court also rejected the insured's argument that the destruction of the insured's ticket counter in the World Trade Center and the accumulation of ash at the Reagan Airport gates triggered coverage for systemwide business interruption losses because the insured's claim bore no relation to the actual physical damage.<sup>20</sup> Consequently, the Southern District of New York found that in the absence of physical loss or damage, no business interruption claim arises as a matter of law.<sup>21</sup>

Another New York court reached a comparable conclusion concerning the requirement of physical damage in *Roundabout Theatre Co. v. Continental Casualty*.<sup>22</sup> There, the insured canceled performances after its theater became inaccessible to the public and submitted a claim for business interruption loss resulting from off-site property damage. The policyholder maintained that the policy's reference to "loss of, damage to, or destruction of properties or facilities" should be read to include "loss of use" of the premises. Nonetheless, the appellate court reversed the trial court and held that coverage is limited to instances in which the insured's property suffered direct physical damage.<sup>23</sup>

The requirement of physical damage necessarily interrupting the business was critical to the court's decision in *Harry's Cadillac-Pontiac-GMC Truck Co. v. Motors Insurance Corp.*, finding no business interruption coverage. The policyholder sought coverage for a business interruption loss due to a partial roof collapse, caused by a snowstorm, over a portion of its car dealership showroom.<sup>24</sup> Because the roof damage did not prevent the car dealer from showing and selling its cars, the court upheld the insurer's denial of coverage. Although the insured could establish a reduction in revenues, there was no causal connection to the roof damage as the cars were on the lot and could be shown to all prospective purchasers. Instead, the court posited that the snow conditions kept customers away with a resulting decline in sales.<sup>25</sup>

Covered physical damage is thus the first step to analyzing whether business interruption exists. As discussed below, the connection between the physical damage and the interruption of business operations mentioned in cases such as *Witcher Construction*, *United Air Lines*, *Roundabout Theatre*, and *Harry's Cadillac* becomes paramount to the determination of whether there

19. *Id.* at 348.

20. *Id.* at 350.

21. *Id.* at 351.

22. 751 N.Y.S.3d 4 (App. Div. 2002).

23. *Id.* at 13.

24. 486 S.E.2d 249 (N.C. Ct. App. 1997).

25. *Id.* at 251.

has been a necessary suspension of operations. Simply stated, the physical damage to insured property must cause the suspension or interruption of the insured's business operations.

#### B. Necessary Suspension of Operations

The International Standards Organization (ISO) form for business interruption uses the phrase *necessary suspension* of the insured's operations. *Webster's Third New International Dictionary* defines *suspension* as "the act of suspending or the state or period of being suspended, interrupted or abrogated." *Suspended* is further defined as "temporarily debarred, inactive, inoperative." The common understanding of the term *suspension* connotes a temporary, but complete, cessation of business activity, as opposed to a mere decrease in customers, attendance, or sales.<sup>26</sup> The business operations must therefore actually stop, albeit the stoppage of one production line in a multiline factory or one floor of a building from which a service is provided may be sufficient.<sup>27</sup> The vast majority of courts hold that the absence of an interruption of business operations is insufficient to implicate business interruption coverage.

Most recently, two courts, *54th Street Ltd. Partners, L.P. v. Fidelity & Guaranty Insurance Co.*,<sup>28</sup> and *Buxbaum v. Aetna Life & Casualty Co.*,<sup>29</sup> have reaffirmed the proposition that the insured must show an unavoidable prevention of business operations. A loss of income associated with some event is

26. See, e.g., *Home Indem. Co. v. Hyplains Beef*, 893 F. Supp. 987, 991 (D. Kan. 1995) ("if one were to apply the plain, ordinary meaning to the use of the phrase 'necessary suspension' within the policy, in order for a claim to fall within coverage provision it would require that any direct physical loss of or damage to property result in the cessation of [the insured's] operations."); *Ramada Inn Ramogren, Inc. v. Travelers Indem.*, 835 F.2d 812 (11th Cir. 1988) (no coverage for hotel due to decrease in occupancy where hotel operation was able to accommodate the same number of patrons); *Howard Stores Corp. v. Foremost Ins. Co.*, 441 N.Y.S.2d 674 (App. Div. 1981) (no coverage for business interruption where there was no actual suspension of the insured's business operations but merely an adverse effect on continuing sales); *Nat'l Children's Expositions Corp. v. Anchor Ins. Co.*, 279 F.2d 428 (2d Cir. 1960) (no coverage for interruption of "use or occupancy" where loss did not occur from the insured's inability to hold an event but rather from a reduction in attendance resulting from a snowstorm).

27. See *Hyplains Beef*, 893 F. Supp. at 991. In *Hyplains Beef*, the insured's business consisted of the purchase, slaughter, and processing of cattle for the wholesale market. In renovating its facility, the insured computerized its plant to collect electronic data and create records for its fabrication and inventory operations. It took several months for the computer system to work; and although the hardware was not damaged, the insured could not retrieve, sort, or use the electronic data collected. The insured contended that it suffered a "direct physical loss" of the collected, but unusable, data, which caused its business to function less profitably. The court did not address the issue of whether there was a "direct physical loss" because there was never a cessation of the insured's business operations.

28. 763 N.Y.S.2d 243 (N.Y. App. Div. 2003).

29. 126 Cal. Rptr. 2d 682, 693-94 (Cal. Ct. App. 2002).

insufficient to trigger business interruption coverage; instead, there must be a causal nexus between the physical damage and the interruption of business.<sup>30</sup>

Rather than focus solely on the distinction between a partial versus complete cessation of business operations, several commentators<sup>31</sup> and courts have focused on the nexus between the physical damage and the interruption of business. For instance, in *Ramada Inn Ramogreen, Inc. v. Travelers Indemnity Co.*,<sup>32</sup> the court upheld the denial of business interruption coverage for a claim made by a hotel owner. The fire damaged a restaurant adjoining the hotel, but there was no damage to any part of the hotel or its rooms. Although the hotel owner could demonstrate a decrease in occupancy and resultant lost profits, there was no covered physical damage or loss to any of the hotel rooms that prevented their use. Accordingly, the court found that there was no necessary interruption of the insured operations resulting from a covered physical loss to insured property.

Likewise, in *Keetch v. Mutual of Enumclaw Insurance Co.*,<sup>33</sup> the court held that there was no necessary suspension of business operations due to the direct physical damage. The insured made a claim, arguing that the number of guests staying at its hotel decreased due to the Mount Saint Helens volcanic eruptions. Despite the fact that volcanic ash had fallen onto the premises, the insured's motel remained open during and after the volcanic eruptions. The court noted that although the volcanic ash made the motel "less attractive," it did not result in the inability to use any of the motel rooms. The motel had the same number of rooms available both before and after the volcanic eruptions. None of the motel rooms had been damaged by the volcanic ash. The court therefore concluded that inasmuch as there was no physical damage preventing the use of any of the rooms, the predicate for business interruption coverage had not been met.<sup>34</sup>

30. *Id.*

31. See ROBERT M. MORRISON ET AL., BUSINESS INTERRUPTION INSURANCE: ITS THEORY AND PRACTICE, in which the authors note thus:

Does "type of [business activities]" mean "retail sales"? If so... the shutting down of one department in a department store because its stock was damaged would not constitute a suspension of the type of business operations as a whole. But it could not mean that, otherwise how could there be a 'partial loss'? There would be no recovery if half of the machinery in a factory was damaged by fire, but the other half continued to operate. A more reasonable interpretation would be to include in the meaning of "suspension" the inability of any part of the insured property to carry on the function to which it had been dedicated by the insured. Such an interpretation would consider the shutting down of a single department in a department store as a suspension under the terms of the contract.

32. 835 F. 2d 812 (11th Cir. 1988).

33. 831 P. 2d 784 (Wash. Ct. App. 1992).

34. *Id.* See also *Harry's Cadillac-Pontiac-GMC Truck Co. v. Motor Ins. Corp.*, 486 S.E.2d 249, 251 (N.C. Ct. App. 1997) (denial of coverage upheld when plaintiff failed to prove a connection between physical damage and claimed suspension of operation).

Finally, the case of *Royal Indemnity Insurance Co. v. Mikob Properties Inc.*<sup>35</sup> is yet another good example of focus by the courts on whether covered physical damage has suspended any portion of the business operations. The insured owned a three-building apartment complex. Fire damaged one of the three buildings but did not damage the other two. No evidence was adduced to show damage to the other two buildings that prevented the use of any apartment units. The only allegation of damage was that soot containing asbestos from the fire prevented the tenants in the undamaged buildings from using amenities near the fire-damaged building, making the complex less attractive to potential and current renters.<sup>36</sup> The court rejected the business interruption claims submitted for the two buildings not damaged by the fire. The court found that the fire did not cause any of the units in the other two buildings to have sustained damage that prevented their use. The court held that no evidence was presented to show that the apartment units could not be occupied. There was no trigger of coverage despite the fact that the inability to use amenities near the fire-damaged building may have made the other two buildings less attractive to potential and current renters.<sup>37</sup>

### C. Actual Loss

Although the purpose of business interruption coverage is to protect the prospective earnings of the insured's business only to the extent that they would have been earned if no interruption had occurred, courts do not allow awards for damages based on speculation.<sup>38</sup> Especially when it comes to lost profits, courts have viewed the recovery of such damages cautiously. In order to obtain a damage award for lost profits, the insured must produce evidence that provides an adequate basis for estimating lost profits with reasonable certainty.<sup>39</sup>

One of the leading business interruption cases, *National Union Fire Insurance Co. v. Anderson-Prichard Oil Corp.*,<sup>40</sup> provides a good explanation of the actual loss sustained requirement. Here, the insured operated a refinery that sustained fire damage to a newly installed cracking unit. The fire damage to the cracking unit suspended the insured's operations for two days until certain modifications were made to begin partial operation.

35. 940 F. Supp. 155 (S.D. Tex. 1996).

36. *Id.*

37. *Id.*

38. See *Polytech, Inc. v. Affiliated FM Ins. Co.*, 21 F.3d 271, 276 (8th Cir. 1994); *Stone Container Corp. v. Arkwright Mut. Ins. Co.*, No. 93-c-6626, 1997 U.S. Dist. LEXIS 3978 (N.D. Ill. Mar. 25, 1997); *Associated Photographers, Inc. v. Aetna Cas. & Sur. Co.*, 677 F.2d 1251 (8th Cir. 1982).

39. See, e.g., *Polytech*, 21 F.3d at 276.

40. 141 F.2d 443 (10th Cir. 1944).

For a period of fifteen days afterward, the refinery operated in a “crippled condition” with curtailed production of gasoline. Eventually, the damaged parts were repaired, and the refinery went into full operation; however, the parties could not agree upon the actual loss sustained for the period of the partial suspension of business.<sup>41</sup>

In assessing the determination of actual loss sustained, the court posited that “there is no prescribed formula . . . except the test of past experience and probabilities of the future.”<sup>42</sup> The court added that “this test is of course to be applied in a practical way, having regard for the nature of the business and its methods employed in its operations.”<sup>43</sup> The court then proceeded to uphold the insured’s proof of actual sustained loss, which had been based on a comparison of earnings between a normal fifteen-day period of operations and the fifteen-day period of partial suspension of business.

The court’s decision in *Howard Stores Corp. v. Foremost Insurance Co.*<sup>44</sup> provides insight as to the circumstances where actual loss is unproven. In that case, water leakage damaged plaintiff’s merchandise at a retail store. Plaintiff was an additional insured under the policy but did not own the retail store in question. The loss due to water damage was settled, but the owner of the merchandise made a separate claim for business interruption. The insurer rejected the initial claim for business interruption, noting that the retail earnings had actually increased after the water damage incident.<sup>45</sup>

The merchandise owner nonetheless filed suit and contended that the increased sales did not defeat its business interruption claim. Plaintiff offered evidence that the increased sales were at a lower-than-projected rate, based on sales analyses from four comparable stores. In upholding the denial of the business interruption claim, the court stated that “there is simply no evidence that any failure to meet the projected sales increases was directly attributable to the water damage.”<sup>46</sup> In the court’s words, “why the sales . . . were lower than projected and why the sales at the other two stores were lower than projected is pure speculation.”<sup>47</sup> The court held that there was no proof of an actual loss sustained, thereby precluding business interruption coverage.

Similarly, in *Eastern Associated Coal Corp. v. Aetna Casualty & Surety Co.*,<sup>48</sup> the Third Circuit held that to the extent a business interruption claim

41. *Id.* at 445.

42. *Id.* at 446.

43. *Id.*

44. 441 N.Y.S.2d 674 (App. Div. 1981).

45. *Id.*

46. *Id.* at 676.

47. *Id.*

48. 632 F.2d 1068 (3d Cir. 1980).

required the jury to speculate, no actual loss sustained had been proven. One of the many issues in the case following a fire during an underground mine derailment concerned the alleged lost production of metallurgical versus steam coal. The distinguishing factor between the two classifications of coal is that metallurgical coal has a lower sulphur content. At trial, the insurers argued that the methodology to prove lost profits from production of metallurgical coal was flawed. The insured could not provide sufficient proof of the sulphur content of the coal at the time of delivery, a factor that obviously affected the price. The Third Circuit agreed and held that the jury could only speculate concerning the sulphur content at the time of delivery. The speculative sulphur content resulted in a speculative lost profit calculation and, therefore, was insufficient to meet the policy requirements of an actual loss sustained.

Most business interruption coverage provides that the past experiences of the business before the loss shall be considered in determining the probable experience had there been no loss. The problem arises when the insured has little, if any, prior experience with a new business activity for which a claim has been made. Some courts go so far as to conclude that in order to prove business interruption, "there must be an on-going business with an established sales record and proven ability to realize profits at the established rate."<sup>49</sup> In that regard, a reasonable time period prior to the interruption is required to establish competent proof of income and expenses of the new business.<sup>50</sup>

Thus, in *Dictiomatic, Inc. v. U.S. Fidelity & Guaranty Co.*,<sup>51</sup> the court found that the business interruption claim following Hurricane Andrew was too speculative. The claim included alleged lost profits for a talking translator and a new model that did not exist at the time of the hurricane. The evidence showed that the talking translator failed to sell for months before the hurricane, and projected profits for the new model had too many variables to serve as proof. Accordingly, the insured failed to prove that a profit would have been realized during the period of restoration.<sup>52</sup>

The rules developed in these actual loss cases require that the insured provide a reasonable basis upon which to calculate its alleged lost business profits. To the extent that the insured's methodology requires speculation to calculate lost profits, the claim for business interruption must fail for want of an actual sustained loss. This is especially true where the insured's actual business after the covered event does the same or better than before the covered physical loss or damage. It is also indispensable that proof of

49. *Dictiomatic, Inc. v. U.S. Fid. & Guar. Co.*, 958 F. Supp. 594, 606 (S.D. Fla. 1997).

50. *Id.* at 605.

51. *Id.*

52. *Id.*

loss of profits should include some assessment of income and expenses of a business at prior times.<sup>53</sup>

#### D. Suspension Period

In general, where the damaged premises are actually restored, the computation period for business interruption losses ends with the restoration unless that period exceeds the theoretical period of repair.<sup>54</sup> The theoretical suspension period is that length of time within which the insured, through the exercise of reasonable dispatch and due diligence, should have completed the repair of the physical damage so as to allow the business operations to resume.<sup>55</sup> Obviously, where the premises are not restored, the theoretical suspension period controls the duration of the business interruption claim.

Business interruption coverage limiting recovery to the duration of the actual suspension period<sup>56</sup> and a theoretical suspension period limitation have been uniformly accepted by the courts as unambiguous.<sup>57</sup> When presented with evidence of the insured's delay in restoring the damaged portions of the insured property and expert opinion testimony as to the reasonable time to complete the repairs so as to permit the resumption of the business operations, courts have routinely enforced limits on the length of the business interruption period.<sup>58</sup>

In *Fireman's Fund Insurance Co. v. Mitchell-Peterson, Inc.*,<sup>59</sup> the insured was the owner/operator of Perkins Cake and Steak in Middletown, Ohio. When fire damaged its restaurant, the insured brought a business interruption claim, including a seven-month suspension period. The trial court found that the reopening of the restaurant seven months after the fire was unreasonable. On appeal, the trial court decision was affirmed with the appellate court expressly holding that the evidence amply supported the "non-diligent efforts to restore operations."<sup>60</sup> The reduction of sixty days from the length of the actual suspension period, representing the time that it should have taken to repair and reopen the business, was upheld.

53. See *Polytech, Inc. v. Affiliated FM Ins. Co.*, 21 F.3d 271, 276 (8th Cir. 1994).

54. *Steel Prods. Co. v. Millers Nat'l Ins. Co.*, 209 N.W.2d 32 (Iowa 1973).

55. *Beautytuft, Inc. v. Factory Ins. Ass'n*, 431 F.2d 1122, 1124 (6th Cir. 1970).

56. *W. Am., Inc. v. Aetna Cas. & Sur. Co.*, 915 F.2d 1181, 1183-84 (8th Cir. 1990); *Nw. St. Portland Cement Co. v. Hartford Fire Ins. Co.*, 360 F.2d 531, 534 (8th Cir. 1966); *Metal-masters of Minneapolis, Inc. v. Liberty Mut. Ins.*, 461 N.W.2d 496, 499-500 (Minn. Ct. App. 1990); see also 15A *COUCH*, *supra* note 1, § 57:31.

57. *Pennbarr Corp v. Ins. Co. of N. Am.*, 976 F.2d 145 (3d Cir. 1992); *Rogers v. Am. Ins. Co.*, 338 F.2d 240, 242 (8th Cir. 1964); 83 A.L.R.2d 885, 896.

58. See, e.g., *Fireman's Fund Ins. Co. v. Mitchell-Peterson, Inc.*, 578 N.E.2d 851 (Ohio Ct. App. 1989).

59. *Id.*

60. *Id.* at 860.

Several courts have emphasized that the determination of the suspension period should be theoretical and “not subject to vagaries like owner indecision, strikes or failure of lease negotiation which might affect the actual rebuilding time.”<sup>61</sup> The Sixth Circuit held that it was wrong for the trial court to allow the jury to consider the insured’s financial condition and the failure of the insurer to make prompt payments when computing the suspension period in *Bard’s Apparel Manufacturing, Inc. v. Bituminous Fire & Marine Insurance Co.*<sup>62</sup> The court of appeals ordered a new trial, stating that the determination of the theoretical suspension period must be “amenable to computation in advance” without regard to the insured’s unique circumstances, i.e., financial condition.<sup>63</sup> In addition, the jury could not be instructed to consider the insurer’s “misfeasance of any duty under the policy” in determining the theoretical suspension period.<sup>64</sup>

It must be emphasized that the theoretical period of restoration becomes relevant only when the business could have resumed sooner than it actually did or when the policyholder decides not to repair or replace the damage. Once the business has reopened, it is axiomatic that there has no longer been a necessary interruption, and the period of indemnity has ended. Not surprisingly, the court in *Royal Indemnity v. Retail Brand Alliance*<sup>65</sup> recently rejected the policyholder’s argument that the period of recovery continued even though its business reopened. The insured contended that the period of indemnity should be measured until the reconstruction of the World Trade Center was or should have been completed.<sup>66</sup> Relying on a few cases, including *Streamline Capital, L.L.C. v. Hartford Casualty Insurance Co.*,<sup>67</sup> the court held that “once the store resumed operations on September 12, 2002, a year after the terrorist attack on the World Trade Center, the business income coverage terminated, regardless of whether the insured’s income was back to pre-loss levels.”<sup>68</sup>

61. *Beautytuft, Inc. v. Factory Ins. Ass’n*, 431 F.2d 1124, 1125 (6th Cir. 1970).

62. 849 F.2d 245 (6th Cir. 1988).

63. *Id.* at 252.

64. *Id.*

65. 822 N.Y.S.2d 268 (App. Div. 2006).

66. *Id.*

67. No. 02 CIV 8123, 2003 U.S. Dist. LEXIS 14677, at \*23–27 (S.D.N.Y. Aug. 22, 2003).

68. *Royal Indemnity*, 822 N.Y.S.2d at 270. The *Royal Indemnity* court also relied on *54th St. Ltd. Partners and Madison Maidens v. American Manufacturers Mutual Insurance Co.*, No. 05 CIV. 4585, 2006 U.S. Dist. LEXIS 39633, at \*7–9 (S.D.N.Y. June 14, 2006). Further support of this position can be found by the decision in *Dictiomatic*, in which an insured suffered damage as a result of Hurricane Andrew. The insured submitted a business interruption claim for loss of business for months after it reopened its facility. The insurer rejected the claim and filed a declaratory action. In issuing summary judgment in favor of the insurer, the court held that the insured “is only entitled to recover its actual loss of business income during the period of time necessary to restore the business operation.” *Dictiomatic, Inc. v. U.S. Fid. & Guar. Co.*, 958 F. Supp. 594, 602 (S.D. Fla. 1997). Therefore, *Dictiomatic* was only entitled

In *Streamline Capital*, the insured's headquarters at the World Trade Center in the September 11 terrorist attacks were completely destroyed. Shortly afterward, the insured temporarily relocated its business to 135 East Fifty-seventh Street in Manhattan but found its new location to be unacceptable.<sup>69</sup> The insured moved for summary judgment on the issue of the length of the period of restoration, contending that the term *property at the described premises* in the policy meant the real and personal property at the World Trade Center, whether owned by the insured or not, and that, as a result, the period of restoration should last until the World Trade Center was rebuilt.<sup>70</sup> Alternatively, the insurer argued that the term meant property belonging to the insured in the insured's offices, and, thus, the period of restoration concluded by the time the insured should have been able to reestablish its operations, either at the World Trade Center or in some other location.<sup>71</sup>

Denying the insured's motion for summary judgment, the *Streamline Capital* court held that the phrase *property at the described premises* used in the period of restoration section "means the plaintiff's [insured's] own personal property in its office suite."<sup>72</sup> The court reasoned thus:

Construing the words "described premises" to mean plaintiff's suite of offices in One World Trade Center is a far more reasonable construction than taking those words to mean either One World Trade Center or the World Trade Center site as a whole.... Given that "premises" in the phrase "property at the described premises" means plaintiff's office suite, the only reasonable construction of the word "property" is the plaintiff's own personal property—computers, desks, chairs, etc.<sup>73</sup>

Following the rationale in *Streamline Capital*, the court in *Lava Trading Inc. v. Hartford Fire Insurance Co.* rejected the insured's claim that the period of restoration ended when the "described premises" themselves should have been repaired rather than when the "property at the described premises" should have been fixed.<sup>74</sup> There, the insured operated a computer software business that specialized in the electronic trading of equities

to its loss of business income for the period of time beginning on the date of the occurrence of the physical damage to its property and ending on the date when the business was back in operation. *Id.*; see also *Manduca Datsun Inc. v. Universal Underwriters Ins. Co.*, 676 P.2d 1274 (Idaho Ct. App. 1984); *Berkely Inn, Inc. v. Centennial Ins. Co.*, 422 A.2d 1078 (Pa. Super. Ct. 1980); *Hampton Foods, Inc. v. Aetna Cas. & Sur.*, 787 F.2d 349 (8th Cir. 1986); *Goetz v. Hartford Fire Ins. Co.*, 215 N.W. 440 (Wis. 1927); *Steel Prod. Co. v. Millers Nat'l Ins. Co.*, 209 N.W.2d 32 (Iowa 1973).

69. *Streamline Capital*, 2003 U.S. Dist. LEXIS 14677, at \*23-27.

70. *Id.* at \*24.

71. *Id.*

72. *Id.* at \*27-28.

73. *Id.* at \*25-26.

74. 365 F. Supp. 2d 434, 442 (S.D.N.Y. 2005).

in various equity markets. At the time of the loss, the insured was also in the process of completing a backup center at 75 Broad Street.<sup>75</sup> After the terrorist attack, the insured moved its operations to temporary offices at 75 Broad Street. By April 30, 2002, it relocated to new offices at 95 Morton Street.<sup>76</sup>

The insurer argued that the period of restoration ended, at the latest, on April 30, 2002, when the insured's Morton Street offices were completed.<sup>77</sup> The insured contended that the period of restoration was calculated from the rebuilding or replacement of the World Trade Center and that even by April 30, 2002, its operations were not restored because its backup facility was not completed until October 22, 2002.<sup>78</sup> Because the World Trade Center would not be rebuilt within thirteen months and the backup facility was not completed until October 2002, the insured claimed it was entitled to the full thirteen-month period of restoration limit in the policy.<sup>79</sup>

Rejecting the insured's arguments, the court held that the period of restoration ended on April 30, 2002, at the latest.<sup>80</sup> As was the case in *Streamline Capital*, the court explained that the term *property at the described premises* referred to the property in the insured's offices on the eighty-third floor of the World Trade Center. Further, the "period of restoration ends when the property at [the insured's] 83rd floor offices should have been repaired, rebuilt or replaced with reasonable speed and similar quality."<sup>81</sup>

Notably, the court relied on the following reasoning set forth by the court in *Streamline Capital*:

It is wholly unreasonable to think that the period of restoration should be tied to the rebuilding of real property over which neither the insured nor the insurer had any control, instead of tying it to a process that the plaintiff controlled: the acquisition of replacement office space and the installation of the plaintiff's personal property in that space.<sup>82</sup>

Additionally, the *Lava Trading* court stressed that no additional time should be given for the delay in completing the backup facility because the period of restoration was measured by when the property that was in the described premises<sup>83</sup> should have been repaired, replaced, or rebuilt.

75. *Id.* at 437.

76. *Id.*

77. *Id.* at 440-41.

78. *Id.*

79. *Id.*

80. *Id.* at 442.

81. *Id.* at 441-42.

82. *Id.* at 442.

83. The described premises in this case were the insured's offices on the eighty-third floor of the World Trade Center (WTC).

The backup facility was not part of the described premises because it was a couple of blocks away from the World Trade Center.<sup>84</sup>

*Duane Reade, Inc. v. St. Paul Fire & Marine Insurance Co.* is another recent case where the court was concerned not with whether the building the tenant occupied was rebuilt but instead with whether the tenant rebuilt substantially similar office space at another location.<sup>85</sup> The insured, a large New York metropolitan pharmacy chain, had a location in the World Trade Center.<sup>86</sup> The insured argued that its period of restoration for its business interruption claim was tied to the reconstruction of the World Trade Center site and the reopening of one of its stores at the site.<sup>87</sup> The insurer argued that it would be unreasonable to expect the period of restoration to be tied to the reconstruction of a building that was not insured by the policy and to which the insured had no ownership interest.<sup>88</sup>

Applying the court's rationale in *Streamline Capital*, the *Duane Reade* court held that it would be totally unreasonable to interpret the Restoration Period to include the time it would take Duane Reade to resume operations in a store located at its former site where that site was neither the subject of the insurance policy nor expressly provided for in the calculus set forth in the Restoration Period.<sup>89</sup>

Explaining that restoration period clauses are meant to cover a "hypothetical or constructive . . . time frame for rebuilding," the *Duane Reade* court concluded that the subject restoration period clause stated that business interruption coverage lasted only for the reasonable amount of time it would take the insured "exercising due diligence and dispatch to rebuild, repair, or replace such property that has been destroyed or damaged."<sup>90</sup>

In contrast to the reasoning of *Streamline Capital*, *Lava Trading*, and *Duane Reade*, two courts have held that the phrase *property at the described premises* is geographically limited to the specific property described in the policy.<sup>91</sup> In one such case, the court in *Zurich American Insurance Co. v. ABM Industries, Inc.*,<sup>92</sup> attempted to distinguish *Duane Reade* and *Streamline Capital*. The

84. *Lava Trading*, 365 F. Supp. 2d at 441-42.

85. 411 F.3d 384 (2d Cir. 2005).

86. *Id.* at 387.

87. *Id.*

88. *Id.* at 388.

89. *Id.* at 396-98.

90. *Id.* at 398.

91. See *Int'l Office Ctr. Corp. v. Providence Wash. Ins. Co.*, No. 04-cv-990, 2005 WL 2258531 (D. Conn. Sept. 16, 2005) (holding that the property at the described premises is geographically limited to that specific property that is described in the declarations because the WTC tenants' business was dependent on operating at that location, unlike the tenants in *Lava Trading*, *Streamline Capital*, or *Duane Reade*); see also *Zurich Am. Ins. Co. v. ABM Indus., Inc.*, 2006 U.S. Dist. LEXIS 28249, at \*2 (S.D.N.Y. 2006).

92. *ABM Indus.*, 2006 U.S. Dist. LEXIS 28249, at \*2.

court glossed over the terms of the policy to find a considerably longer period of recovery for an engineering and janitorial services contractor, which did not even own space in the World Trade Center.<sup>93</sup> Instead, the insured provided janitorial, lighting, and engineering services in the common areas and also provided janitorial services for almost all of the tenants.<sup>94</sup>

The insurer argued that the period of recovery “should end when ABM’s [insured’s] customers, i.e., the WTC [World Trade Center] tenants, have relocated their businesses.”<sup>95</sup> Distinguishing *Duane Reade* and *Streamline Capital*, the court held that the appropriate period of recovery is the hypothetical length of time required to rebuild the World Trade Center.<sup>96</sup> It explained thus:

The nature of ABM’s business is fundamentally different from that of either of the plaintiffs in those cases [*Duane Reade* and *Streamline Capital*]. Unlike *Duane Reade* and *Streamline Capital*, ABM cannot simply relocate to another building and carry on its business. To the contrary, ABM’s business was, as the Court of Appeals recognized, fundamentally connected to its use of the common spaces at the World Trade Center. Thus, in contrast to the position of *Duane Reade* and *Streamline Capital*, restoration of the World Trade Center itself is “necessary [for] ABM to resume” its operations.<sup>97</sup>

Moreover, the court noted that, unlike *Duane Reade* and *Streamline Capital*, “the nature of ABM’s business is such that it is impossible to tie the recovery period to a process over which the parties themselves have control.”<sup>98</sup> In further rejecting the insurer’s argument, the court added, “[I]f all of the WTC tenants immediately relocated to other buildings that ABM did not service, ABM’s business would remain interrupted, but it would be unable to recover damages under the Business Interruption provision of the policy, a result the parties could have hardly intended.”<sup>99</sup>

## II. EXTRA EXPENSE COVERAGE

The purpose of extra expense coverage is to provide coverage for additional costs incurred to avoid a cessation or slowdown in business operations.<sup>100</sup>

93. *Id.*

94. *Id.* The parties did not dispute that a significant amount of the insured’s profits was derived from work it performed for the WTC tenants.

95. *Id.* at \*5.

96. *Id.* at \*9.

97. *Id.* at \*7.

98. *Id.*

99. *Id.* at \*8.

100. *Archers Daniels Midland Co. v. Aon Risk Servs., Inc. of Minn.*, No. 97-2185, 2002 U.S. Dist. LEXIS 19314, at \*6 (D. Minn. Sept. 27, 2002); see also STEPHEN A. COZEN, *INSURING REAL PROPERTY* § 3.04[1] (1989) (stating that extra expense coverage allows the insured to continue its normal operations: it reimburses the insured for those expenditures in excess of normal operating costs that are required to keep the business going while repairs to physical property damage are made).

This coverage allows the insured to continue its normal operations: it reimburses the insured for those expenditures in excess of normal operating costs that are required to keep the business going while repairs to physical property damage are made. Extra expense coverage usually means expenses incurred during the interruption of business above normal expenses if there had been no covered loss, and usually the expenses must have been incurred to expedite repairs or minimize the loss, not for some other business purpose.<sup>101</sup> Additional payroll, the cost of renting temporary space, cleanup costs following property damage, and increased utility costs, all above normal, are examples of increased costs that, under certain circumstances, can be extra expense.<sup>102</sup> Extra expense coverage may exist under certain circumstances for temporary repairs of covered physical damage of insured property to resume business operations as nearly as possible to preloss conditions.

As with business interruption coverage, the insured must establish the coverage requirements of a covered peril causing direct physical loss to insured property within the policy period. In other words, extra expense can only be sustained in the event that the insured's claim meets the six-part test of an interruption of business. Moreover, as with business interruption coverage, the policy language at issue must be evaluated to determine the type or extent of extra expense covered.

The Eastern District of Pennsylvania recently considered whether an insured's claim was covered by an extra expense provision.<sup>103</sup> In *Doherty v. Nationwide Mutual Insurance Co.*, the insured owned a multiple-unit apartment building that was damaged by a fire.<sup>104</sup> One day after the fire, the insured began cleanup and repair efforts, engaging the services of John Rush Home Improvements to help with this effort.<sup>105</sup> This included pumping out the floodwater, removing smoke-damaged personal items abandoned

101. Extra expenses are distinct from the fixed and continuing costs covered by business interruption coverage. See Robert J. Brennan & Laura C. Conway, *Business Income Insurance Coverage*, 32 BRIEF 65, 66 (Summer 2003).

102. See, e.g., *Am. Med. Imaging Corp. v. St. Paul Fire & Marine Ins. Co.*, 949 F.2d 690, 693 (3d Cir. 1991) (extra expense coverage may be provided for increased payroll for overtime, additional utility expense, and alternative office space); *Charles Dowd Box Co. v. Fireman's Fund Ins. Co.*, 218 N.E. 2d 64, 71 (Mass. 1996) (extra expense coverage provided for overtime and utility and telephone costs); *Traveler's Indem. Co. v. Pollard Friendly Ford Co.*, 512 S.W. 2d 375, 380-81 (Tex. App. 1974) (extra expense coverage provided for overtime, rent for alternative office space, and temporary property and cleanup expenses).

103. *Doherty v. Nationwide Mut. Ins. Co.*, No. 05-6222, 2006 U.S. Dist. LEXIS 59936 (E.D. Pa. Aug. 23, 2006) (The extra expense provision in the policy provided that Nationwide would pay plaintiffs for the "necessary Extra Expense [that plaintiffs] incur during the 'period of restoration' that [they] would not have incurred if there had been no direct physical loss or damage to property at the described premises." The policy further stated that *extra expense* means expenses incurred "to avoid or minimize the suspension of business and to continue operations.").

104. *Id.* at \*2.

105. *Id.* at \*3.

by tenants, repairing holes in the roof, and returning the building to a safe and livable condition.<sup>106</sup>

The insured sought \$136,984.62 in extra expenses that were incurred for work done in the months immediately following the fire to keep the building habitable and safe before permanent repairs could be made.<sup>107</sup> After reviewing invoices for dumpsters, interior and exterior debris removal, interior roof supports, exterior building bracing, temporary replacement locks for the building as well as each apartment, and removal of hazardous materials, the court held that all of this work met the definition of *extra expense* under the policy "in that it was necessary to continue operations as a residential apartment building during the period of restoration."<sup>108</sup> Likewise, the court found that the expenditures for sewer services for the building, outdoor lighting, and landscaping to restore the grounds and shrubbery "avoid[ed] or minimize[d] the suspension of business operations as a residential apartment building during the period of restoration" and thus qualified as extra expenses under the policy.<sup>109</sup>

In *Butwin Sportswear Co. v. St. Paul Fire & Marine Insurance Co.*, the Minnesota Court of Appeals interpreted an extra expense clause and found that the fee paid by an insured to a "public adjuster" who assisted the insured with the preparation of its insurance claim following a fire at its manufacturing plant was not a covered extra expense.<sup>110</sup> The court found that the public adjuster's fee was not a necessary extra expense because the insurer might have paid all of the insured's covered losses without his involvement, and the insured engaged him in anticipation of conflict and to maximize its claim.<sup>111</sup> However, the court noted that to the extent that the insured could establish that some of the public adjuster's services, "such as salvaging damaged goods and helping get the business running again," were incurred as a consequence of the interruption of the insured's business, they could be covered.<sup>112</sup>

Another example of a case where a court interpreted the meaning and scope of extra expense coverage is *Tower Automotive, Inc. v. American Protection Insurance Co.*<sup>113</sup> The insured, a manufacturer of parts for the automotive industry, submitted a claim for its losses from the failure of one of its presses at one

106. *Id.*

107. *Id.* at \*6. The court noted that the ability of the insured to keep the building inhabited while permanent repairs could be completed is a basic necessity in order to "continue operations."

108. *Id.*

109. *Id.* at \*7.

110. 534 N.W. 2d 565, 567 (Minn. Ct. App. 1995).

111. *Id.*

112. *Id.*

113. 266 F. Supp. 2d 664 (W.D. Mich. 2003).

of its facilities.<sup>114</sup> Specifically, the insured's delivery of truck parts to Ford Motor Co. was delayed; and Ford informed the insured that as a result of the delay, it incurred idle labor and lost production costs.<sup>115</sup> The insured authorized Ford to debit its account for these costs.<sup>116</sup> Among its claimed losses, the insured argued that the Ford debit was an extra expense under the policy because it was an "expense over and above the total cost of normal operation had Tower's [the insured's] press not failed."<sup>117</sup> Acknowledging that the insured made the payment to Ford voluntarily, the court held that there was no evidence that the payment was "necessary to Tower's ability to resume its normal operation after the failure of the press."<sup>118</sup>

As demonstrated by the aforementioned cases, extra expenses must be both necessary and incurred by the insured. The court in *Chatham Corp. v. Dann Insurance* recently analyzed both of these requirements.<sup>119</sup> In that case, the insured's sterilization facility was shut down for seven months as a result of an equipment explosion.<sup>120</sup> The insured could not sterilize the products of its main customer, Maxxim Medical, Inc., and the insured's contract with Maxxim required the insured to find alternate sterilization facilities and to pay the cost of shipping Maxxim's unsterilized goods from the insured's site to the alternate facilities. Although the insured performed these contractual obligations and the insurer reimbursed the insured for the resulting extra expenses, the insured made a claim for additional extra expenses for the costs of shipping Maxxim's sterilized products from the alternate facilities to Maxxim's customers.<sup>121</sup>

The insurer contended that because the insured was not contractually required to pay Maxxim's outbound freight costs, those costs were not necessary and incurred and thus were not covered extra expenses.<sup>122</sup> In concluding that the policy language regarding extra expenses was unambiguous and that the costs were neither necessary nor incurred by the insured, the Illinois Appellate Court stated thus:

Although the policy does not specifically define the word "necessary," that word is not ambiguous and has a plain, ordinary, and popular meaning of "being essential," indispensable, or requisite. This commonly understood meaning encompasses expenses that the named and additional insureds to the policy, Chatham and SSV [Sterilization Services of Virginia, Inc.], were required to

114. *Id.* at 666.

115. *Id.*

116. *Id.*

117. *Id.* at 669.

118. *Id.* at 669, 671.

119. 812 N.E. 2d 483 (Ill. App. Ct. 2004).

120. *Id.* at 486.

121. *Id.*

122. *Id.*

incur during the reconstruction of the sterilization facilities. It does not encompass expenses that other, nonparties to the contract were required to incur during the facility reconstruction period. The only party required to pay for the cost of shipping Maxxim's sterilized products away from the alternate sterilization facilities was Maxxim itself not Chatham or SSV. In addition, Chatham has failed to address the unambiguous requirement that Chatham or SSV actually "incur" the expenses Chatham now seeks to recover. "Incur" is another term that was not defined in the contract, but it has a plain, ordinary, and popular meaning of "to become liable or subject to through one's own action; [to] bring or take upon oneself." Chatham never became liable or subject to the expense of Maxxim's outbound freight. Maxxim did.<sup>123</sup>

In *Snelling & Snelling, Inc. v. Federal Insurance Co.*, the federal court in Texas granted summary judgment in favor of the insurer, denying the insured's attempt to recover legal fees as extra expenses.<sup>124</sup> There, the insured operated an office near the World Trade Center and had obtained property insurance, including extra expense coverage.<sup>125</sup> As a result of damage sustained on September 11, the insured decided to sublease part of its space in an effort to reduce its losses after the attacks.<sup>126</sup> Subsequently, the insured needed to evict the subtenants and incurred legal fees as a result. The insured then sought extra expense coverage for the legal fees associated with the eviction.<sup>127</sup> The court rejected the insured's claim, finding it to be beyond the scope of the extra expense provision.<sup>128</sup> The court held that the insured's legal fees "were not incurred in an attempt to continue a business activity occurring prior to the loss" but rather were an attempt to terminate an activity that began subsequent to the loss.<sup>129</sup> Further, the court found the attorney fees "too remote to qualify as an attempted continuation of operations."<sup>130</sup>

### III. CIVIL AUTHORITY COVERAGE

Similar to business interruption and extra expense, civil authority coverage turns on the existence of physical damage caused by a covered peril. The covered physical damage must then result in an order by civil authority prohibiting access to the insured premises. Advisory statements, suggestions, or voluntary decisions to close premises fail to come within the ambit of an

123. *Id.* at 488-89 (citing RANDOM HOUSE WEBSTER'S UNABRIDGED DICTIONARY 969, 1883-84 (1998)).

124. No. 03-cv-2948, 2005 U.S. Dist. LEXIS 24835 (N.D. Tex. Oct. 25, 2005).

125. *Id.* at \*2.

126. *Id.*

127. *Id.* at \*9.

128. *Id.* at \*10.

129. *Id.*

130. *Id.*

order by civil authority. Further, a valid order of a civil authority will not give rise to coverage when issued due to the potential future threat of damage or when based on physical damage from an otherwise excluded peril.

Many local governments and other authorities issue evacuation orders, travel advisories, and other forms of civil advisories and orders before, during, and following natural disasters and emergency conditions. Quite often, insureds rely on these advisories and orders when submitting claims under a policy's civil authority provision. A potential civil authority provision contained in an insurance policy may read as follows:

We will pay for the actual loss of "business income" you sustain and necessary Extra Expense caused by order of civil authority that prohibits access to the "described premises" due to direct physical loss of or damage to property, other than at the "described premises," caused by or resulting from any Covered Cause of Loss.

A review of this provision reveals that four basic requirements ordinarily must be met in order for coverage to be afforded: (1) an order by a civil authority (2) prohibiting access to insured property (3) due to physical damage and (4) caused by a covered peril.

Courts interpreting civil authority provisions have uniformly held that coverage is available only where the order in question actually forbids or prevents access to the insured's premises but does not apply where access is simply made more difficult.<sup>131</sup> In other words, a complete barring of access is generally required, and a mere hindrance or impairment will not suffice. For instance, in *Abner, Herrman & Brock, Inc. v. Great Northern Insurance Co.*, the Southern District of New York recently held that the civil authority provision afforded coverage for losses incurred only on the days when the governmental order prohibited access to the insured premises.<sup>132</sup> The insured brought a claim for a business income loss allegedly suffered from lack of access as prohibited by civil authority.<sup>133</sup> The insured did not suffer physical damage to its property, but civil authority prohibited access to the insured's premises for four days as a result of the September 11 attacks.<sup>134</sup> Furthermore, the insured's office was located in an area where vehicular

131. See *Syufy Enters. v. Home Ins. Co. of Ind.*, No. 94-0756, 1995 WL 129229, at \*1 (N.D. Cal. Mar. 21, 1995) (holding that phrase *specifically prohibit access* in civil authority provision is clear and requires a denial of access); *Abner, Herrman & Brock, Inc. v. Great N. Ins. Co.*, 308 F. Supp. 2d 331 (S.D.N.Y. 2004); *S. Hospitality, Inc. v. Zurich Am. Ins. Co.*, No. CIV-02-923-C, 2003 U.S. Dist. LEXIS 18324, at \*1 (W.D. Okla. Sept. 30, 2003), *aff'd*, 393 F.3d 1137 (10th Cir. 2004); *730 Bienville Partners, Ltd. v. Assurance Co. of Am.*, No. CIV. 01-106, 2002 U.S. Dist. LEXIS 18780 (E.D. La. Sept. 30, 2002), *aff'd*, 67 F. App'x 248 (5th Cir. 2003).

132. 308 F. Supp. 2d 331 (S.D.N.Y. 2004).

133. *Id.* at 333-34.

134. *Id.*

traffic was banned until September 17, but pedestrian access was allowed after September 14.<sup>135</sup>

The insured contended that the civil authority provision provided coverage for five days due to civil prohibition against entering the premises and additional coverage for the following twenty-five days due to the constraints that restricted vehicular traffic placed on its normal operating procedures. Among other things, the head of the firm used a private driver to attend client and prospective client meetings.<sup>136</sup> Alternatively, the insurer argued that the policy afforded coverage for losses only on the days when access to the premises was prohibited, not when traffic restrictions made access more difficult.<sup>137</sup>

The court held that the unambiguous policy language afforded coverage only for the four days on which civil authority prohibited access to the premises.<sup>138</sup> The policy did not provide coverage beyond that period regardless of any confusion that the insured's employees may have had concerning getting to work or any difficulties faced by the insured's chairman or its driver.<sup>139</sup>

The Eastern District of Louisiana also addressed a civil authority claim in *730 Bienville Partners, Ltd. v. Assurance Co. of America*.<sup>140</sup> There, the insured hotels sought civil authority coverage after the Federal Aviation Administration (FAA) closed all U.S. airports following the September 11 attack, alleging that hotel patrons were not able to access its hotels because airline flights were canceled.<sup>141</sup> The policy covered loss of "business income" . . . caused by action of civil authority that prohibits access to your premises. . . .<sup>142</sup> The court, under Louisiana law, applied the ordinary meaning test and denied coverage, holding that

135. *Id.*

136. *Id.* at 335.

137. *Id.*

138. *Id.* at 336.

139. *Id.*; see also *54th St. Ltd. Partners, L.P. v. Fid. & Guar. Ins. Co.*, 763 N.Y.S.2d 243, 244 (App. Div. 2003) (holding that a civil authority provision applied only to the two days when access to the premises was denied and did not apply to the subsequent period when vehicular and pedestrian traffic was diverted but access was not denied to the public, employees, or vendors); *Altru v. Health Sys. v. Am. Prot. Ins. Co.*, 238 F.3d 961 (8th Cir. 2001) (coverage afforded under civil authority provision when health authority closed the hospital for three weeks because floodwaters reached parking lot and city's water system failed); *Narricot Indus. Inc. v. Fireman's Fund Ins. Co.*, No. 01-4679, 2002 U.S. Dist. LEXIS 19074 (E.D. Pa. Sept. 30, 2002) (civil authority provision provided coverage for manufacturer prohibited from accessing and operating its facilities); *Travelers Indem. Co. v. Pollard Friendly Ford Co.*, 512 S.W.2d 375 (Tex. App. 1974) (civil authority provision provides coverage "where insured's buildings do not suffer a direct loss, but the area is blocked off by civil authorities thereby denying access to the insured's business by its customers").

140. No. CIV. 02-106, 2002 U.S. Dist. LEXIS 18780 (E.D. La. Sept. 30, 2002), *aff'd*, 67 F. Appx. 248 (5th Cir. 2003).

141. *Id.* at \*2.

142. *Id.* at \*4.

[t]he terms of the policy are unambiguous. To recover for business losses under the Civil Authority Extension, the loss of business income and necessary expenses must be “caused by action of Civil Authority that prohibits access to your premises...” While the FAA’s closure of the airports and cancellation of flights may have prevented many guests from getting to New Orleans and ultimately to plaintiff’s hotels, the FAA hardly “prohibited” access to the hotels.<sup>143</sup>

Likewise, in *Philadelphia Parking Authority v. Federal Insurance Co.*,<sup>144</sup> the insured brought an action for a loss sustained at the parking garage at the Philadelphia International Airport as a result of the September 11 terrorist attacks. The insured contended that the civil authority provision, business income, and contingent business provisions afforded coverage for its loss. The insured alleged that the FAA prohibition “effectively prevented ingress and egress of passengers into terminal areas of the Philadelphia International Airport and [the insured’s] Airport Parking Facilities.” The insured additionally contended that as a “direct consequence of the closure of the Airport and Airport Parking facilities, there was a severe reduction in [the insured’s] business.”<sup>145</sup>

The insurer moved to dismiss, contending that the insured failed to plead three necessary elements to invoke coverage under the civil authority provision: (1) that the FAA “prohibited access to” the insured’s garages; (2) that the FAA ban on flights was ordered “because of direct physical loss or damage”; and (3) that such loss or damage occurred to property “in the vicinity of” the insured’s garages.<sup>146</sup>

143. *Id.* at \*5–6. A Mississippi court also addressed denial of access in *St. Paul Mercury Insurance Co. v. Magnolia Lady, Inc.*, No. 97-cv-153, 1999 U.S. Dist. LEXIS 17895 (N.D. Miss. Nov. 4, 1999). In *Magnolia Lady*, a Mississippi hotel owner sought civil authority coverage after Arkansas authorities closed a Mississippi River bridge leading to the casino hotel for almost three weeks as the result of a barge accident. *Id.* at \*2. Although the casino hotel remained accessible, albeit via the Mississippi side only, and open for business during the bridge closure, revenue allegedly dropped by 80 percent. The policy provided as follows: “We will pay for your actual [business income and extra expense] loss... when a Civil Authority like a fire department denies access to the described location...” *Id.* at \*3. Coverage hinged on whether the bridge closure “denied[d] access” to the casino hotel. Applying the “everyday” meaning of *denies access*, the court held that even though the nearest bridge over the Mississippi River was about fifty miles away, civil authority coverage was unavailable. *Id.* at \*8. The court noted thus:

[I]t is clear to see that there was no denial of access to the defendant’s casino-hotel. The defendant’s casino-hotel was accessible during the period of time that the bridge was under repair, and the defendant continued operating business and accepting customers. Contrary to the defendant’s assertion that customers from Arkansas were denied access, access was never totally denied because customers from Arkansas could have gained access from the Mississippi side of the bridge. Thus, ... coverage under the “Interruption by Civil Authority” subsection ... fails due to the everyday meaning of the words “denies access.”

*Id.* at \*8–9.

144. 385 F. Supp. 2d 280 (S.D.N.Y. 2005) (applying Pennsylvania law).

145. *Id.* at 289.

146. *Id.*

The court found the insurer's arguments persuasive and granted the insurer's motion to dismiss. The court stated that the plain language of the FAA notice did not prohibit access to the insured's garages as the policy required. Further, the notice was issued to "all aircraft operators" and dealt solely with the grounding of airplanes. The court noted that although the order may have obviated the need for the parking spaces, the order did not prohibit access to the insured's parking garages. Accordingly, the order did not invoke coverage under the policy.<sup>147</sup>

The Northern District of Georgia reached the same result in *Paradies Shops, Inc. v. Hartford Fire Insurance Co.*,<sup>148</sup> holding that the policyholder failed to establish that an order of civil authority specifically prohibited access to the insured's premises as a direct result of a loss to property away from the premises. The insured operated gift shops, newsstands, and retail stores in airports throughout the United States<sup>149</sup> and contended that the September 11 ground stop order issued by the secretary of transportation prohibited access to its shops. The policyholder further argued that the ground stop order was based in part on the fear of additional terrorist attacks and in part on attacks that had already occurred.<sup>150</sup> The insurer argued that the order was based solely on the fear that additional airlines might be hijacked and used as terrorist weapons. The insurer also maintained that the FAA orders did not close operations at the insured's stores or prevent customers from accessing those stores.<sup>151</sup>

In finding for the insurer, the court noted that the plain language of the policy required the insured to establish an order of civil authority specifically prohibiting access to its premises. The court further opined that if an order applied to prohibit access, it must have been issued as the "direct result" of property damage by a covered peril away from the insured's premises.<sup>152</sup>

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147. *Id.* The Western District of Oklahoma similarly held that because the FAA's suspension of flights did not bar or prevent access to the insured's hotels, the civil authority provision did not provide coverage for the insured's loss. *S. Hospitality, Inc. v. Zurich Am. Ins. Co.*, No. CIV-02-923-C, 2003 U.S. Dist. Lexis 18324 (W.D. Okla. Sept. 30, 2003). In *Southern Hospitality*, the insured sought coverage for losses sustained as a result of FAA's action. The insured argued that the civil authority provision afforded coverage for its losses because FAA's closing of the airports was an action by a civil authority that hindered access to its hotels. The insurer argued that the hotels remained open for business and FAA did not bar access to the hotels. *Id.* at \*6.

The court held that *prohibit* as used in the civil authority provision was not ambiguous. This provision covers losses sustained when a civil order bars access to an insured's hotels. The court noted that although FAA order impacted the insured's business, it limited the means of travel rather than prohibiting access to the hotels. Because FAA's order did not bar access to the insured's hotels, the policy did not cover the insured's losses. *Id.* at \*8.

148. No. 03-cv-3154, 2004 U.S. Dist. LEXIS 30124 (N.D. Ga. Dec. 15, 2004).

149. *Id.* at \*6.

150. *Id.*

151. *Id.* at \*7.

152. *Id.* at \*12.

Because no order of civil authority specifically was issued as a direct result of the physical damage sustained by the World Trade Center, the Pentagon, or the field in Pennsylvania,<sup>153</sup> no coverage existed. The court found that the ground stop order did not specifically prohibit access to the policyholder's shops. Moreover, the order had been issued because of the threat of additional terrorist attacks and not because of threats that already had occurred.<sup>154</sup>

The court found no coverage in *United Air Lines*,<sup>155</sup> where a civil order prohibited access but had not been issued as the result of covered physical damage away from the premises. United Airlines sought lost revenues under the civil authority provision of its property policy for its systemwide revenue loss resulting from the terrorist attacks that destroyed its ticket counter in the World Trade Center, and it further asserted that its "gate property at Washington Reagan National Airport was physically impacted by the terrorist attack at the Pentagon, resulting in the accumulation of ash at the United gates."<sup>156</sup> In the cross-motions for summary judgment, United also argued that the Pentagon was "adjacent premises" to Reagan Airport under the civil authority provision.<sup>157</sup> The court held that Reagan Airport was not adjacent to the Pentagon because the Pentagon was 3.4 miles away from Reagan Airport and the two facilities were separated by several intervening structures and properties.<sup>158</sup> The court further noted that even if the Pentagon and Reagan Airport were adjacent facilities, the insured was required to show that damage at the Pentagon was the "proximate, efficient and dominant cause" for the civil authority's order. Because access was prohibited in order to "prevent further attacks and as a matter of national security" and not as a result of damage, the court held that the civil authority provision did not afford coverage for the insured's claim.<sup>159</sup>

One court interpreted the damage requirement of a civil authority provision to include the threat of impending damage. In *Assurance Co. of America v. BBB Service Co.*,<sup>160</sup> the insured sought coverage for losses sustained at its restaurants in Florida and Georgia as a result of Hurricane Floyd. The chair of the Brevard County, Florida, commission issued an order that declared a state of local emergency "because of the serious threat to the lives and property of residents of Brevard County from Hurricane Floyd...because of the uncertainty of the path of devastating winds and

153. *Id.* at \*14-15.

154. *Id.*

155. 385 F. Supp. 2d 343 (S.D.N.Y. 2005), *aff'd*, 439 F.3d 128 (2d Cir. 2006).

156. *Paradies Shops*, 2004 U.S. Dist. LEXIS 30124, at \*6.

157. *Id.* at \*12.

158. *Id.* at \*27.

159. *Id.* at \*30.

160. 593 S.E.2d 7 (Ga. Ct. App. 2003).

storm surges.” Some residents were ordered to evacuate.<sup>161</sup> As a result of the order, the insured closed its restaurants and evacuated the area for approximately two and one-half days.

After the insurer rejected the insured’s claim on the basis that the order was issued due to the threat of damage to property, not actual property damage, the insured brought a breach of contract action against the insurer. At trial, the insured introduced testimony of members of the Brevard County policy group who had assembled to make emergency decisions regarding weather-related problems. One member testified that the group watched the storm progress and issued the order because of the damage that had been caused in its path, the forecast that the storm was headed to Brevard County, and the anticipated impact of the storm if it hit the county.<sup>162</sup> The court ultimately ruled in favor of the insured, holding that the evacuation order was issued as a result of actual damage to property.<sup>163</sup>

#### IV. CONCLUSION

The common thread of all three types of coverage—business interruption, extra expense, and civil authority—turns first on a covered peril causing direct physical damage during the policy period. Each type of coverage must then be analyzed based on its own particular language in light of judicial interpretation. Business interruption requires an analysis of the covered physical loss or damage to insured property or property at a described location (1) necessarily suspending the business operations and (2) resulting in actual loss sustained. The final step is to determine the period of interruption, which should end on the date repairs are complete so that operations can resume, unless the theoretical suspension period is of a shorter duration. Extra expense coverage must meet the same initial four requirements of a business interruption claim, and the expense must be incurred above normal costs during the period of business interruption to expedite repairs or reduce the business interruption loss. Expenses incurred for some other business purpose fail to constitute a covered extra expense. Civil authority requires, depending upon the policy language, an order prohibiting access to the insured premises due to physical damage from a covered peril adjacent to the insured property. Within these guideposts, coverage can be determined for almost all claims of business interruption, extra expense, and civil authority.

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161. *Id.*

162. *Id.* at 8.

163. *Id.*