

Bio

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Business Interruption: Counting on Coverage is a Risky Business

Introduction

“By its plain meaning, ‘interruption of business’ is a breaking or suspension of production earnings of an operating business...The general purpose of business interruption coverage is ‘to do for the business what the business would have done for itself had no loss occurred.’” Great Northern Oil Co. v. St Paul Fire & Marine Ins., 303 Minn. 267, 227 N.W.2d 789, 793 (1975) (“Great Northern”). Such insurance coverage is . . .intended to protect against losses arising from the inability to use those assets to conduct the business.” Citizens Sav. and Loan Ass’n. of New York v. Proprietors Ins. Co., 78 A.D.2d 377, 380, 435 N.Y.S.2d 303, 305 (2nd Dept. 1981).

The term Business Interruption insurance seems quite straight forward, but the policy does not cover all income lost by reason of business interruption. Rather several prerequisites must be met and there may be different requirements depending upon the jurisdiction, the court or even the judge. For a business interruption policy to apply the policyholder’s business must be interrupted and there must be a loss. One without the other is not sufficient. The case law is in conflict as to whether the loss must be of physical damage or just lost income. This article will use examples from

actual cases to show what types of losses have been held to provide or failed to provide payment for business interruption losses.

The Policy

Business interruption insurance coverage is usually purchased as part of a first party property policy, either as a section of the policy or as an added endorsement or rider.

“Business interruption insurance is . . . generally in the form of a rider or endorsement on a policy insuring against loss or damage to physical assets.” Citizens Sav. and Loan Ass’n. of New York v. Proprietors Ins. Co., 78 A.D.2d 377, 380, 435 N.Y.S.2d 303, 305 (2nd Dept. 1981).

Although the business interruption language is fairly standard in most policies, there are many different determinations of what constitutes a recoverable loss under business interruption insurance. The interpretations do not appear to vary with whether the business interruption language is part of the text of the policy or is an endorsement.

One business interruption insuring agreement states:

“This policy . . . insures against loss directly resulting from the necessary interruption of business caused by loss or damage insured hereunder, to property . . . located on the premises [insured by this policy].”

Another variant states:

“This policy insures against loss resulting directly from necessary interruption of business caused by damage to or destruction of real or personal property by the peril(s) insured against* * * on premises occupied by the Insured* **.” Bros., Inc. v. Liberty Mut. Ins. Co., 268 A.2d 611, 613 (D.C. Ct. of App. 1970).

The case law does not necessary make a distinction between policy language and often the court does not quote to policy language in its decision.

Business interruption cases have arisen in several contexts all of which involve a loss of business income to the policyholder. Insurance questions are unlikely to arise in the temporary closing of a business due to a fire or some other event which causes traditional property damage. This article will discuss business losses and whether business interruption insurance provides protection in the following contexts:

1. Where there has been a loss of business income but there is a question as to whether the loss involved physical damage to property;
2. Whether the loss resulted from an insured peril;
3. Was the business able to continue despite the event even though it had no or fewer customers because of the event?
4. Under the order of civil authority provision of the policy, whether it is sufficient that the loss of business happened because the business was shut down or could not be accessed due to the order, or must there also be physical damage to the business property?

I. Did the Loss Involve Physical Damage to Property

Is Physical Damage to Property Necessary for Recovery of Business Interruption Insurance?

What loss or damage to property is required? Must it be “physical damage” to property and, if so, what constitutes “physical damage” necessary to trigger a business interruption insurance policy? Business interruption insurance policies are purchased to provide funds to make up for income lost during a business interruption. Policyholders and insurance companies may vigorously dispute what constitutes the “physical damage” necessary for an insurance recovery. A particularly thorny issue for business interruption insurance is what constitutes “physical damage” to a computer. Is it damage to the hardware, the very tangible mainframe, tower or laptop? Damage to the software, the various programs which enable the computer to function or damage to the data stored on the computer?

The most recent decision involving the question of what constitutes “physical damage” in a business interruption and computer context is

American Guarantee & Liability Insurance Company v. Ingram Micro, Inc., 2000 WL 72689 (D.Ariz. April 18, 2000)(“Ingram”). In Ingram, the court awarded the policyholder partial summary judgment on the issue that a power outage, which resulted in the loss of programming information stored on three mainframe computers, ““ caused direct physical loss or damage from any cause, howsoever or wheresoever occurring.”” The insurance company had contended that “the computer system and the matrix switch were not ‘physically damaged’” as the computer system could still accept and process data. The policyholder successfully argued that “‘physical damage’ includes loss of use and functionality” Ingram, 2000 WL 726789,*2.

The Ingram court relied on no supporting case law and distinguished the one case it did discuss, Seagate Technology, Inc. v. St. Paul Fire and Marines Insurance Co., 11 F.Supp.2d 1150, 1151 (N.D.Ca. 1998) (“Seagate”). Rather the court relied on various federal and state computer fraud statutes which define damage to a computer. For example, the federal computer fraud statute defines damage as “ any impairment to the integrity or availability of data, a program, a system, or information.”18 U.S.C. Section 1030” Ingram, 2000 WL 72689,*2. A computer crime is committed under the Connecticut statute when one “disrupts or degrades or causes the disruption or degradation of computer services.” Conn. Gen. Stat. Section 53a-251(2000).

The Ingram court, in effect, took judicial notice of the computer revolution and the importance of software as well as hardware in making its decision when it provided the following statement as a rationale for its decision:

“At a time when computer technology dominates our professional as well as personal lives, the Court must side with Ingram’s broader definition of ‘physical damage.’ The Court finds that ‘physical damage’ is not restricted to the physical destruction or harm of computer circuitry but includes loss of access, loss of use, and loss of functionality.”). Ingram’s computer network could not function until the data was reentered eight hours later and other reprogramming was necessary in the ensuing days. The court did not determine how long business was interrupted.

In Seagate Technology, Inc. v. St Paul Fire and Marine Ins. Co., 11 F. Supp.2d 1150(N.D. CA 1998) the policyholder made disk drive storage devices which were incorporated into another company's computers. The disk drives were defective and the computer manufacturer sued. The insurance companies refused to defend. The court denied coverage holding that since the underlying complaint did not allege "that the defective drives did or could harm other components of the host computers" there was no coverage. Rather the underlying complaint

"sought recovery of damages resulting from the failure of Seagate's product to perform as promised or warranted....the risk of replacing or repairing a defective product is considered a commercial risk which is not passed on to a liability insurer. See Maryland Casualty Co. v. Reeder, 221 Cal.App.3d 961, 270 Cal .Rptr. 718 (1990). This rule is designed to prevent liability insurance from serving as a warranty or guarantee of an insured's product." Seagate, 11 F.Supp.2d at 1155.

The Ingram court distinguished Seagate, on the basis that the complaint by the computer manufacturer against Seagate did not allege that the drives harmed other parts of the computer; whereas Ingram alleged "that as a result of the power outage, Ingram's computer system and world-wide computer network physically lost the programming information and custom configurations necessary for them to function. Ingram's mainframes were 'physically damaged' for one and one half hours." Ingram, 2000 LW 726789,*3 (D.Ariz). But the allegations in Seagate were very similar to those in Ingram. For example, the computer manufacturer's complaint in Seagate alleged that "data previously recorded cannot be recovered and data cannot be recorded" as well as "loss of customer's information." Seagate, 11 F.Supp.2d at 1154.

Courts have limited business interruption insurance to requiring damage to the exact property for which such insurance is claimed and have refused to grant the policyholder recovery for losses even though they were caused by a closely related loss.

For example, when a restaurant affiliated with a motel or hotel is shut down because of a fire, resulting in fewer rooms being occupied, the owner

of the hotel or motel was refused recovery for its loss of business. Ramada Inn Ramogreen, Inc. v. Travelers Indem. Co. of America, 835 F.2d (11th Cir. 1988)(“Ramada”); Hotel Properties, Ltd. V. Heritage Ins. Co. of America, 456 So.2d 1249 (Fla. Dist Ct. App. 3d Dist. 1984)(“Hotel Properties”). It makes no difference whether the policyholder owned the restaurant, as in Ramada or whether the restaurant was merely a tenant as in Hotel Properties. The Ramada court held that since the two properties, although insured under the same policy, had separate listings– “Location 1- [Building] 1- 4” for the motel and “Location 1-[Building] 5” for the restaurant evidenced “the intent of the parties to treat it as a separate entity.” Ramada, 835 F.2d 812, 814.

In an analogous case involving an extra expense endorsement, Port Murrury Dairy Co. v. Providence Washington Ins. Co., 52 N.J. Super. 350, 145 A.2d 504(Ch.Div. 1958) the court denied insurance to a dairy which was closed by a strike of a newly formed guild of dairy farmers. The strike barred the entrance and exit of the dairy precluding it from getting processed milk and other dairy products to or from its premises. The dairy’s plant was not damaged or destroyed but it sustained losses from the inability to sell milk and milk products which soured during the eight days of the strike. The policy covered “the necessary extra expense incurred by the insured in order to continue the normal conduct of the insured’s business during the period of restoration” after “damage to or destruction of plaintiff’s buildings or contents by any of the perils insured against (fire, vandalism, riot, and the like).” 145 A.2d at 507. The court found that:

“The policy obviously refers to a situation where the insured’s property, whether buildings or contents has been damaged or destroyed by an insured peril, it is that damage or destruction that causes the extra expense incurred in order to continue normal operations during the period of restoration.” 145 A.2d at 508

Here there was no period of restoration as there was nothing to rebuild or replace. “Plaintiff could have obtained and processed milk at its only plant immediately had the rioters lifted the blockade.” 145 A.2d at 508

The court held that the milk and milk products were fine when the strike commenced so they were not damaged. It rejected the dairy owner’s testimony that he understood that he had business interruption insurance. The dairy also had coverage for strike, vandalism and riot protection but the court found none of these activities caused the loss.

An early example of the interpretation of a business interruption policy is Cleland Simpson Company v. Firemen's Fund Ins. Co., 392 Pa. 67, 140 A.2d 41(1958). Cleland Simpson had no access to its business premises for three days and suffered significant losses because of the business interruption. It asserted a claim under its fire insurance policy which had a business interruption provision. The loss resulted from the havoc created by Hurricane Diane to northeastern Pennsylvania in 1955. Water from the hurricane poured through Scranton, Pennsylvania, broke the water mains resulting in no water for fire hydrants.

“Death and destruction in historic figures followed...The dangers to life and the actual and threatened damages to property were so great that all the agencies of civil government, of military services and the voluntary relief and disaster agencies had to make extended efforts to relieve the necessities of the area....the City was defenseless against fire but due to the watchfulness and determination of its citizens the City was spared that disaster there was no fire...**no one of the properties covered by this policy was exposed to any damage by fire or lightning.** ...[in a] wise and considered action. . . the Mayor of Scranton, after consultation with advisors. . .declared a state of emergency and ordered **all stores to close because of a serious fire danger resulting from the flood which cut off the water supply** in the City of Scranton.” 140 A.2d at 42 (emphasis added).

The basic fire policy had an exclusion for “loss by fire or other perils insured against cause[d] directly or indirectly by. . .Order of any civil authority except acts of destruction at the time and for the purpose of preventing the spread of fire. . .” 140 A.2d at 43. The business interruption language provided:

“subject to all its stipulations, limitations and conditions, this policy covers only against loss directly resulting from necessary interruption of business caused by destruction or damage by the perils insured against occurring during the term of this policy.

* * *

‘Interruption by civil authority: Liability under this policy is extended to include actual loss as covered hereunder sustained during the period of time, not exceeding two weeks, when as a direct result of a peril

insured against access to the premises described is prohibited by order of civil authority.” 140 A.2d at 43

The Court held that there was no coverage as the policyholder’s property did not burn.

“Here the specified peril is fire; the risk insured against is loss of profit through business interruption caused directly by fire and extended for a period of time to continued interruption caused by the action of civil authorities in preventing access to the business premises as a direct result of fire.

“By no process of logic can we read into the policy that the risk includes prohibition of access because of apprehension of either the possibility or probability of a fire which never occurred.” 140 A.2d 44.

There was a vigorous dissent on the grounds that the policy covered a “peril insured against” and that peril is an impending or threatening danger” and that an actual fire was not required. 140 A.2d at 45. See also, Simpson Read Estate Corp. v. Firemen’s Ins. Co., 392 Pa. 74, 140 A.2d 47(1958).

3. Was the Business Able to Continue Despite the Event Even Though It Had No or Fewer Customers Because of the Event?

Just because a business has been shut down, does not mean that it can collect for its losses under a business interruption policy. An adverse effect on sales due to a flood, or a loss in profits after a theft of merchandise or lowered attendance at an exhibition because of a blizzard have not resulted in recoveries for the policyholders. See, Howard Stores Corp. v. Foremost Insurance Co., 82 A.D.2d 398, 441 N.Y.S.2d 674 (1981); Rothenberg v. Liberty Mutual Ins. Co., 115 Ga.App. 26, 253 S.E.2d 447 (1967) and National Children’s Expositions Corp. v. Anchor Insurance Co., 279 F2d. 428 (2d Cir. 1960). The theory of these cases is that there was no actual

suspension of business, just a diminution in business not caused by an interruption. National Children's Expositions Corp. v. Anchor Insurance Co., 279 F2d. 428 (2d Cir. 1960). The theory of these cases is that there was no actual suspension of business, just a diminution in business not caused by an interruption of the business, but rather by an outside event whose impact lessened income and profits.

One case illustrating this principle is Keetch v. Mutual of Eneuclaw Ins. Co., 66 Wash. App. 208, 831 P.2d 784 (Div.3 1992)("Keetch"). The policyholder in Keetch operated a motel near Mount St. Helens. Its business slowed down considerably after the eruption of the volcano. There was volcanic ash on the grounds but the rooms of the motel itself were not injured. The insurance company's denial of the business interruption claims was sustained since the business remained open and could have served its customers had they sought to stay at the motel. (See, Great Northern Oil Co. v. St. Paul Fire & Marine Ins. Co., 303 Minn. 267, 227 N.W.2d 789 (1975), holding that damage to areas of a business under construction were not covered by a business interruption policy as the existing business was not harmed)

4. Did the Loss Result from and Insured Peril

Business interruption insurance may be limited to business interruption caused by property damage resulting from a peril insured under the policy. In these policies physical damage to property may be required.

Even if there is property damage the loss may not entitle the policyholder to business interruption coverage. It is also necessary for the business interruption must result from a covered peril. For example, a devastating fire at an insured retail store resulted in the liquidation of the warehouse full of merchandise sold at the retail establishment. The insurance company paid for debris removal and lost business property at the retail location, the fire loss, but refused to pay for the losses resulting from the warehouse's liquidation. Thrift Mart, Inc. v. State Farm Fire & Casualty Co., 251 Neb. 448, 558 N.W.2d 531 (1997). The policy in question provided coverage for loss of business income "during the 'period of restoration'" at the "described premises" or other temporary location. *Id.* at

456. The Supreme Court of Nebraska upheld the insurance company's refusal to pay, finding that the warehouse liquidation resulted from the termination of the business as because of the fire and not its interruption. Any covered loss must arise from the temporary continuation of the operation.

“Clearly, the liquidation of warehouse inventory which occurred, by Thrift Mart's own admission, when the business ceased its operations completely and which does not fit within the policy definitions of 'business interruption' is not covered under the insurance policy's loss of business income provision. The policy specifically states that this coverage is for expenses arising from disruptions during the continuing operation of the business at a temporary site or during the relocation of the business to a new site if operations cannot continue at the premises where the fire occurred. Thrift Mart liquidated its warehouse after deciding to cease business operations—any loss sustained because of the circumstances of liquidation not related to continuing business operations is not recoverable.” Thrift Mart, Inc. v. State Farm Fire & Casualty Co., 251 Neb. 448, 456, 558 N.W.2d 531,537(1997).

The courts are also very strict about the business interruption damage having been caused by an insured peril. In Peerless Dyeing Co., Inc. v. Industrial Risk Insurers, 392 Pa. Super. 434, 573 A.2d 541 (1990) at issue was a named peril policy with a business interruption endorsement(?). The damage resulted from a city water main break which flooded the policyholder's factory. After a trial the jury awarded \$1.3 million dollars including \$334,180 for property damage and \$827,820 for business interruption. On appeal, the appellate court reversed, finding that the loss did not result from damage caused to a named peril, as while water from fire protective equipment was insured, underground water mains were excluded from the definition of fire protective equipment. The court reversed the jury's award for business interruption losses following the insurance company's argument that business interruption insurance is “available only if there is recovery for property damage.” 573 A.2d at 548. The business interruption endorsement required “damage to or destruction of real or personal property. . . by perils insured against” or “loss caused solely by an

accident occurring while this endorsement is in effect to an Object designated and described in the schedules and endorsements.” 573 A.2d at 548. Since there was not damage to a named peril, the court found there was no evidence that there was an accident to an insured Object. 573 A.2d at 548.

In Gregory v. Continental Ins. Co., 575 So.2d 534 (Miss. 1990) a golf course had business interruption insurance. During a hurricane the pro shop and restaurant were injured and many trees were blown down and there was debris on the greens, preventing use of the golf course. The insurance company paid for the damage to the pro shop and restaurant which were specifically itemized on the declaration page, but refused to pay for the 14 day loss of income from the golf course on the grounds that it did not insure trees. The court sustained the denial of insurance.

Whether Physical Damage is Required When the Business Interruption is Caused by the Order of a Government Authority

Business may be interrupted because of governmental decrees establishing a curfew or restricting access to the place of business. This type of stoppage is usually referred to as being closed by “order of civil authority.” The restriction may follow a natural disaster such as a hurricane or tornado or may result from a disturbance such as a riot, strike or civil commotion. Many of these cases arose as a result of the losses occurring during the riots following the assassination of Dr. Martin Luther King and the Rodney King verdict.

Many business interruption policies contain a provision providing coverage when access is restricted by order of a civil authority. A common example of this policy language is:

“This policy is extended to include the actual loss As covered hereunder, during the period of time, not to exceeding 2 consecutive weeks, When as a direct result of the peril(s) insured against, access to the premises described is prohibited by order of civil authority.” Allen Park Theatre Co., Inc. v. Michigan Millers Mut. Ins. Co., 48 Mich. App. 199, 210 N.W.2d 402, 404(1973)(“Allen Park”). See also, Sloan v. Phoenix of Hartford Ins. Co., 46 Mich. App. 46, 207 N.W.2d 434(1973).

One variation of this language is:

“Interruption by Civil Authority

This Endorsement is extended to include the Actual Loss Sustained by the Insured, as cover hereunder, during the length of time, not exceeding two (2) consecutive weeks, when access to such described premises is specifically prohibited by order of civil authority as a direct result of damage as insured against hereunder, to covered property on the described premises or property adjacent to the premises herein described.”

Another variation is:

“the coverage of this policy is extended to include direct loss by * * * Riot* * * (and) Civil Commotion* * *.

When this Endorsement is attached to a policy covering Business Interruption,* * * the term ‘direct,’ as applied to loss, means loss as limited and conditioned in such policy, resulting from direct loss to described property from perils insured against.;* * *” Bros. v. Liberty Mutual Fire Ins. Co., 268 A.2d 611 (D.C. Ct. of App. 1970).

In Sloan v. Phoenix of Hartford Ins. Co., 46 Mich. App. 46, 207 N.W.2d 434 (1973) (“Sloan”), the Governor of Michigan declared a state of emergency for Wayne County which includes Detroit, following the assassination of Dr. Martin Luther King. The executive order provided that “All places of amusement within the County of Wayne are hereby closed until further notice.” Allen Park Theatre Co., Inc. v. Michigan Millers Mut. Ins. Co.,48 Mich. App. 199, 210 N.W.2d 402, 403(1973)(“Allen Park”). Sloan operated movie theaters in Detroit. While its establishments were not physically damaged it suffered losses of \$11,359.95 which it sought to recover from its business interruption insurance. The insurance company contended that “there is no coverage unless there has been direct and actual physical damage to the insured property.” Sloan, 46 Mich. App. at 48. The policyholder “asserted that the risk insured against was the prohibition of access to their premises by order of a civil authority stemming from one of the enumerated perils, E.g., riot and civil commotion, without any requirement of physical damage to the insured property.” Sloan, 46 Mich. App. at 48

The court looked at the policy as a whole and gave “the words contained therein plain meaning as understood by an ordinary person” and found that the paragraphs of the business interruption policy “contemplate separate and distinguishable business losses.” Sloan, 46 Mich. App. at 49.

“ Paragraphs 1 and 2 are addressed to business interruption losses ‘caused by damage to or destruction of’ the insured property. Paragraph 7 speaks to business-interruption losses occasioned by the denial of access to the premises by order of a civil authority. However, no mention is made of the necessity for physical damage to the premises before paragraph 7 can become operative. Such an omission is conspicuous by its absence.” Sloan, 46 Mich. App. at 50.

The court affirmed the verdict for the policyholder.

The policyholder in Allen Park operated places of amusement. It was subject to the same curfew discussed in Sloan. Allen Park’s property was not damaged. It had riot and strike insurance and a Business Interruption rider which provided:

“(T)his policy covers only against loss resulting directly from necessary interruption of business Caused by damage to or destruction of real or personal property by the peril(s) insured against, during the term of this policy, On premises occupied by the Insured...” 210 N.W.2d at 403.

The court affirmed the decision below granting coverage to the policyholder without property damage.

The policyholder contended that the civil authority clause provided separate and additional coverage; whereas the insurance company contended that the civil authority provision must be read in conjunction with the rest of the policy as providing an additional period of time to during which repairs of damaged property can take place.

“The central issue presented in construing the above-mentioned provisions is whether actual damage to or destruction of the insured premises as a direct result of riot is required under the interruption by civil authority clause in order for owners to be reimbursed of losses suffered.” 210 N.W.at 406.

The Allen Park court read the policy as a whole with the policy covering “damage to or destruction of the premises” with the business interruption endorsement as delineating extra “perils which could result in Direct loss to the insured.” Allen Park 210 N.W.2d at 405.

There was a long dissent which set forth all the issues involved in the question of whether property damage is required. The dissenting judge stated:

“The writer cannot agree with plaintiffs’ contention that the business interruption rider is a separate and independent agreement without reference to either the standard policy of the extended coverage endorsement. It is fundamental that insurance policies must be construed as a whole...” 210 N.W.2d at 406.

While this Michigan Court of Appeals judge noted that “two recent Michigan Court of Appeals cases” arising from the Governor’s same order had decided that property damage was not necessary this judge would have decided to follow the District of Columbia cases that property damage was required for coverage.

Another case by a Michigan an operator of places of entertainment including bowling alleys, motels, restaurants which arose after the assassination of Dr. Martin Luther King is Southlanes Bowl, Inc.v. Lumbermen’s Mutual Ins. Co., 46 Mich.App. 758, 208 N.W.2d 569 (Ct. App. 1973)(“Southlanes”). None of Southlanes’ businesses were physically damaged by the riots, but it suffered a net loss of almost \$50,000 in 1968. Southlanes sought to recover these sums under its business interruption insurance and specifically the clause providing coverage for prohibition to access to their premises by order of a civil authority from an enumerated peril, riots. The insurance company contended that there was no coverage because there had been no “direct and actual physical damage” to Southlanes’ insured property. The trial court agreed with the insurance company that physical property damage was required. The Michigan Court of Appeals, not Michigan’s highest court, reversed holding for the policyholder relying upon Sloan discussed above.

“This Court has recently had occasion to consider whether under the language of the business-interruption policy. . . physical damage to the insured premises is a condition precedent to the insurer’s liability to pay benefits. We 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. *Sloan v. Phoenix of Hartford Insurance Co.*, 46 Mich.App. 46, 207 N.W.2d 434(1973)” *Southlanes*, 46 Mich.App. at 760.

Two identical cases in the District of Columbia reached the opposite result. *Bros., Inc. v. Liberty Mutual Fire Ins. Co.*, 268 A.2d 611(D.C. Ct. of App.1970) (“Bros”); *Two Caesars Corporation v. Jefferson Ins. Co.*, 280 A.2d 305(D.C. Ct. of App. 1971) (“Two Caesars”). Because of the civil disturbances which followed the assassination of Martin Luther King, Jr. the Commissioner of the District of Columbia proclaimed an emergency which imposed a curfew for various times between April 5 and April 12, 1968. The curfew was in effect from 5:30 p.m. to 6:30 a.m. All persons other than fire, police and medical personnel were required to stay off the streets and away from public places in the affected area during the curfew. Sale or dispensing of alcoholic beverages including beer and wine was prohibited. In *Bros* the policyholder claimed a damages for business lost due to restrictions on the sale of alcoholic beverages and the limitation of business hours.

The court denied coverage under both the original Building and Contents’ Form which had been issued with the policy and also under the Business Interruption Form which the insurance company substituted for it under a General Change Form Endorsement during the litigation. It was not disputed that there were no physical damages to the policyholders property or the adjacent property. As the court noted “It is common knowledge that the disturbances were centered miles from the property here involved.” 268 A.2d at 613. Quoting the language of the policy, which is quoted above, the court found that since the loss was not “from damage to or destruction of his[the policyholder’s] property there was no coverage under the standard business interruption portion of the policy. With respect to the order of civil authority coverage the court acknowledged that the loss was the result of the curfew imposed access to the policyholder’s property was not prohibited because of destruction or damage of adjacent property. *Bros, Inc.*, 268 A2d at 614.

“As to the final clause [order of civil authority], though the loss alleged resulted from the curfew and municipal regulations, these did not prohibit access to the premises because of damage to or destruction of adjacent property” Bros.,Inc., 268 A.2d at 614.

In Two Caesars the policyholder sought loss income resulting from the imposition of the same curfew. Policyholder had a restaurant which sold alcoholic beverages and food. The policy had a provided coverage for direct loss from riots and civil commotion but the court did “not construe business ‘fall-off’ due to the curfew as being a direct loss by riot or civil commotion”280 A.2d at 306. Nor did the court find that that the direct loss from riots applied as there was no physical damage to the property.

The court in reliance on its decision in Bros., Inc. v. Liberty Mutual Ins. Co., D.C.App., 268 A.2d 611 (1970) rejected coverage under the interruption by civil authority provision. The court rejected coverage under the order of civil authority provision relying on Bros. Because the curfew did not prohibit access to the premises because of damage to or destruction of adjacent property.

In Two Caesars the policyholder tried to distinguish Bros. on the basis of differences in policy language. The Two Caesars policy stated:

“This policy is extended to include the actual loss as covered hereunder during the period of time, not exceeding 2 consecutive weeks, when, as a direct result of the period(s) insured against, access to the premises described is prohibited by order of civil authority.” The policy also contained a “Special Exclusions: This Company shall not be liable for any increase of loss resulting from: (c) the suspension ***of any license***.” 268 A..2d at 307.

In contrast the Bros. policy provided coverage “when, as a direct result of damage to or destruction of property adjacent to the premises herein described’ access to such property is specifically prohibited.” Two Caesars, 280 A..2d at 306.

The court rejected Two Caesar’s contention that the provision would be meaningless if property damage was still required under that provision:

“Appellant says that if physical damage were required, paragraph No. 7 of the ‘Business Interruption’ endorsement would be meaningless. But, of course, it is not meaningless. Absent paragraph No. 7, there would be no coverage whatsoever for business interruption, if, by order of civil authority, access to the business premises was prohibited because of extensive physical damage or destruction.” Two Caesars, 280 A.2d at 307, fn.2.

The court relied on a Perils not included provision which stated that “This Company shall not be liable for loss by fire or other perils insured against in this policy caused, directly or indirectly, by *(h) order of any civil authority except acts of destruction at the time of and for the purpose of preventing the spread of fire.*”

Here you have two curfews arising from the same incident resulting in different outcomes for the policyholder and the insurance company. In Michigan the policyholder has coverage; in the District of Columbia it has none.

The issue of whether property damage was needed for business interruption coverage in the order of civil authority situation arose again after curfews were imposed following the Rodney King verdict. Syufy Enterprises v. Home Ins. Co., 1995 WL 129229 (N.D. CA, March 21, 1995)(“Syufy”). Syufy owned and operated 56 movie theaters throughout the West Coast. Civil authorities in San Francisco, Los Angeles and Las Vegas imposed general dawn to dusk curfews for two to three day periods after the Rodney King verdict. Syufy closed its theaters during the time of the curfew. The parties stipulated that no civil authority specifically prohibited access to any of the policyholder’s theaters nor was the policyholder’s property or the adjacent property damaged as a direct result of the riots. In fact, no property within two blocks of the theaters was physically damaged. In Syufy the court held that the business loss had to be a direct result of damage to or destruction of property which was not present in this case. The court found that “damage occurring in an unspecified area at least two blocks from a Syufy theater is clearly and plainly not ‘adjacent’ to the theater. . . .The requisite causal link between damage to adjacent property and denial of access to a Syufy theater is absent.” 1995 WL 129229,*2

Furthermore, the Syufy court found that even if the word “adjacent” was ambiguous, there was still no coverage as “no civil authority specifically prohibited any individual from entering a theater; rather, the cities imposed dawn-dusk curfews to reduce the possibility of rioting and looting . . . and resulting property damage.” 1995 WL 129229,*2 The court did not give any weight to the fact that the curfew prevented individuals from being outside and thus going to the theaters.

In a footnote the Syufy court gave an example of a situation which would be covered under the policy:

“Based on the plain and unambiguous language of the provision, the following situation would clearly be covered: A building next door to a Syufy theater is damaged by fire; for safety reasons, the civil authorities issue an order closing the Syufy theater during the repairs to the adjacent building. Any business loss suffered by Syufy for up to two weeks would be covered under the business interruption provision.” 1995 WL 129229,*3.

What Constitutes Business Income Under a Business Interruption Policy?

What Type of Expenses are Recoverable ?

In an early decision, Studley Box & Lumber v. National Fire Ins. Co., 85 N.H. 96, 154 A. 337(1931) a lumber company used horses for its lumber business. A fire occurred in the stable and some of the horses died from the fire. Due to the loss of the horses the lumber plant was partially shut down and extra expenses were incurred to reduce the loss. The insurance company paid for losses from partial suspension of the business, but argued that it only had to pay a portion of the extra expenses based on a fraction the partial suspension bore to the whole business. The court rejected this argument:

“realizing that one element insured was loss of profits, he [the policyholder] would appreciate that in a partial suspension he would be entitled only to the proportion such loss bore to their loss under a total suspension. But, as to expenses incurred incident to the fire and to reduce the loss, he would expect full indemnity up to the general per diem limit, whether the suspension were total or partial.” 154 A. at 339.

In addition to loss of business income, other types of expenses resulting from the incident may be recouped. In Travelers Indemnity Co. v. Pollard Friendly Ford Co., 512 S.W.2d 375 (Ct. of Civil App. Tex.1974), under an extra expense indemnity policy, “of indemnity for ‘extra expenses’ incurred in order to continue as nearly as practicable the normal conduct of the insured’s business” the court permitted the following types of damages. Pollard involved a Ford dealership which was hit by a tornado. Pollard recovered payments for extra compensation paid to employees for working 18 hour days to restore the business, meals purchased for employees in order to continue the business, clean up of debris, watch protection expenses and costs of obtaining other property for temporary use. 512 S.W.2d at 377. The court refused to grant coverage for outside professional consultants such as lawyers or CPAs or additional advertising expenses. 512 S.W.2d 381. Pollard’s claims for fixed expenses such as rent salary and telephones while he could not access the property because of access to its building was blocked by order of the civil authorities. 512 S.W.2d 381. The court refused to award prejudgment interest on the ground that the amount to be paid was not known immediately after the tornado.

Rules of Construction of Insurance Policies

Business interruption policies like other insurance policies are construed in favor of the policyholder when the language is ambiguous. “When an insurance company is susceptible to more than one meaning, the rule of strict construction against the insurer and in favor of the insured is applicable with all doubts resolved against the insurer and for the insured.” Travelers Indemnity Co. v. Pollard Friendly Ford Co., 512 S.W.2d 375, 379(Ct. of Civil App. Tex. 1974)

“Insurance contracts are interpreted as a whole giving to the words used therein plain meaning as understood by an ordinary person. ..In addition, where, as here, the contract of insurance is drawn by the insurer, any reasonable doubts or ambiguities contained in that contract will be construed most favorably to the insured.” Sloan, 46 Mich. App. at 48-49.

In Great Northern Oil Co. v. St. Paul Fire & Marine Ins. Co., 303 Minn. 267, 227 N.W.2d 789 (1975), the jury awarded the policyholder \$776,745.92 for business interruption losses when a crane collapsed damaging its new

construction. “There was no damage to the existing facility and it continued normal operation.” 227 N.W. 2d at 791. The policyholder sued for the earnings it would have made from the expanded facility had no accident occurred. The Supreme Court of Minnesota reversed the jury award since there would have been no profits from the new facility until it was finished.

“Merely because damage to insured property may be shown, it does not follow that a business-interruption loss occurred. By its plain meaning, ‘interruption of business’ is a breaking or suspension of production earnings of an operating business rather than an interruption of a construction schedule. The general purposes of business-interruption coverage is to ‘do for the business what the business would have done for itself had no loss occurred’”(citations omitted). 227 N.W.2d at 792-793.

Conclusion

The overarching principal of these cases is that business interruption insurance is a very specialized type of coverage whose specific prerequisites must be met. The exact parameters may vary from jurisdiction to jurisdiction. Property damage is often required and what will be deemed sufficient physical injury or property damage, or how the loss can fit into the categories, particularly in the computer situation, may be up to the ingenuity of counsel for the parties and the choice of judge.