

Commentary

Insurance Coverage – A Valuable Asset For Businesses With Losses Arising Out Of The Deepwater Horizon Explosion And Gulf Oil Spill

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resulting from alleged environmental contamination and property damage and business interruption claims, including claims resulting from the September 11, 2001 terrorist attacks and Hurricanes Katrina and Rita. Additionally, he has handled substantial commercial litigation matters, including breach of contract, product liability, and fraud claims. His client representations include litigation in both state and federal courts and all forms of alternative dispute resolution. Mr. Trotter currently is co-leader of the Firm's Property and Business Interruption Insurance Coverage Initiative. He may be reached at trotterk@dicksteinshapiro.com. Copyright 2010 by Selena J. Linde and Kenneth Berline Trotter.]

Since the explosion at the Deepwater Horizon drilling platform in the Gulf of Mexico on April 20, 2010, millions of gallons of oil have spilled into the Gulf each day. A government panel of scientists has reported that the ruptured well is leaking between 1.47 million and 2.52 million gallons of oil per day. The total amount of oil that has leaked so far could be as many as 127 million gallons, making it the largest oil spill and environmental disaster in U.S. history. The oil already has contaminated the Gulf and miles of Alabama, Florida, Louisiana, Mississippi, and Texas coastline. The oil threatens to contaminate even more shore lands, possibly reaching the Florida Keys and the Eastern Seaboard, and potentially reaching as far north as North Carolina. The 1989 Exxon Valdez spill, by comparison, discharged 11 million gallons of oil along more than a thousand miles of Alaska's coastline.

The long-term damage is estimated to be significant. The oil, fishing, tourism, and shipping industries already have been affected. Offshore drilling has been halted in some regions; fishing has been restricted by the National Oceanic and Atmospheric Administration's closure of 86,985 square miles — about 36 percent of the Gulf's federal waters; most of the lakes and marshes east and south of Lake Pontchartrain have been closed by the Louisiana Department of Wildlife and Fisheries; tourism has been impacted due to beach closures and restricted water access; and navigation has been disrupted by action of civil authority, including the closure of Perdido Pass and Pensacola Pass at high tides.

As businesses and communities try not only to respond to the disaster, but also to recover from its impact, their financial needs will be tremendous. BP PLC has set up a \$20 billion fund, providing \$5 billion per year for the next four years, to compensate victims of the oil spill. President Obama has appointed Kenneth R. Feinberg as the independent administrator of the fund. Mr. Feinberg and his law partner, Michael Rozen, have provided some information about the fund, but it remains unclear how quickly businesses will be paid, whether businesses will be fully compensated, or whether some businesses will be able to recover at all from the fund. For example, Mr. Feinberg has cast doubt on whether companies that lost revenue because of a decline in tourism will be eligible for compensation. Thus, in addition to potential recovery from the BP fund, businesses also should pursue other sources of recovery, including insurance.

Insurance Recovery For Damage Or Losses

Insurance is a valuable resource that can play an important role in helping companies recover from this disaster. During a recent conference on the Gulf oil spill that was held in Atlanta on June 24, Mr. Rozen announced that the fund would accept subrogation claims from insurers. In plain terms, this means that a policyholder may pursue claims against its insurer and, if the insurer pays the claim, the policyholder may assign to the insurer the right to pursue a claim against the BP fund. Policyholders, therefore, should strongly consider pursuing insurance claims under all applicable insurance policies. In some instances, these policies may provide policyholders with quicker and greater recovery.

Applicable Insurance Policies

Several types of insurance might respond to pay for losses stemming from the oil spill, including insurance policies for: First-Party Property (including Business Interruption and Extra Expense coverage); Directors & Officers; Event Cancellation; Trade Disruption; and, Commercial General Liability insurance policies.

First-Party Property Policies

The extent of property damage from the Gulf oil spill so far is unclear. First-party property policies protect a policyholder's place of operations and inventory, and provide coverage for lost or damaged property. Many property insurance policies are sold on an "all risk" basis, meaning that they cover losses to real property caused by any peril not expressly excluded. Because of the breadth of coverage afforded by an "all risk" policy, once a policyholder shows that it has suffered a loss, the burden of proof shifts to the insurer to show that the loss is not covered. By comparison, a second type of property insurance — a "named peril" policy — covers only those perils expressly listed. Both types of policies may contain exclusions to coverage. It is important to carefully review all aspects of a policy to determine if coverage for the specific loss is clearly excluded.

Additional Coverages, Including Business Interruption And Extra Expense

In addition to covering property damage, many property policies also provide some or all of the following coverages that may help the policyholder recover for other losses caused by the oil spill. In order to be implicated, policies typically require damage by a covered peril to property.

Business Interruption: reimburses the policyholder for the amount of gross earnings minus normal expenses (i.e., its profits) that the policyholder would have earned but for the interruption of the policyholder's business. Such coverage may be implicated, for example, for businesses in the fishing industry which are forced to cease operations due to contamination. In the context of municipalities, this coverage may be implicated if the municipality experiences a decrease in tax revenue. The city of Biloxi, Mississippi, for example, obtained reimbursement for millions of dollars of lost tax revenue when Hurricane Katrina caused casinos to shut down and Biloxi experienced an ensuing loss of tax revenue. Business interruption coverage generally requires that

an “interruption” result from damage to covered real or personal property. Policyholders, for example, have obtained reimbursement under such coverage when widespread disasters such as Hurricane Katrina and the 9/11 terrorist attacks caused business interruption.

Contingent Business Interruption: protects against economic losses caused by the inability of the policyholder to receive a supplier's goods or services or the policyholder's inability to supply goods or services to customers, thereby preventing the policyholder from producing or selling its product in the marketplace. Such coverage may be implicated, for example, when port and harbor operations are interrupted, altering the flow of trade goods.

Civil Authority: protects the policyholder from losses caused by the inability to access its premises when a civil authority denies such access because of covered damage to, or destruction of, property belonging to third parties. Some civil authority coverages require physical damage to the policyholder's own premises; others do not. Here, orders restricting access to property by numerous federal and state authorities may implicate Civil Authority coverage.

The U.S. Coast Guard, for example, has issued orders restricting access to navigable water channels such as the Pensacola Pass, the main entry from the Gulf of Mexico into Pensacola Bay. This could impact the ability of vessels to access marinas and other facilities. The National Oceanic and Atmospheric Administration closed about 86,985 square miles — about 36 percent of the Gulf's federal waters — which may prohibit businesses from accessing property, such as leased oyster beds or mineral interests. Local and state authorities also have closed beaches, which may prevent access to beachfront businesses. Finally, the U.S. Department of the Interior's moratorium on new deepwater drilling in the Gulf of Mexico also could implicate Civil Authority coverage for oil rig operators and service providers who have been, or will be affected by the moratorium. On July 6, 2010, in a filing on behalf of the Interior Department, Solicitor Hilary C. Tompkins argued that a Louisiana federal district court, which struck down the drilling ban last month, “misperceived Interior's authority, the rationale for the suspensions and the relative harms present in the gulf.” The fate of the moratorium and its impact on business remains

unclear, but impacted policyholders should carefully examine its impact on their business and potentially applicable Civil Authority coverage.

Ingress/Egress: protects the policyholder against lost business income and extra expense when the policyholder's premises are inaccessible for reasons other than an order of civil authority. This type of coverage typically requires that the property damage be located within a certain radius of the policyholder's premises. Such coverage may be implicated if, for example, access to a business' premises is precluded due to property damage in the immediate area.

Extra Expense: indemnifies the policyholder for the reasonable and necessary increased costs of conducting its business operations due to property damage caused by an insured peril. One example of such an expense would be the increased costs of raw materials and transportation as a result of the oil spill. For example, a restaurant might need to obtain seafood from Asia or Latin America due to a lack of supply from the Gulf.

Directors & Officers Policies

Directors & officers policies may provide defense and indemnity coverage for companies and their directors and officers who face claims regarding their preparation for, or response to, the crisis. For example, claims may be made against directors and officers for failure to have proper procedures and plans in place for dealing with the oil spill.

Event Cancellation Policies

Event cancellation policies are designed to compensate policyholders for losses arising out of the cancellation, interruption, or postponement of specified events. These policies typically specify that coverage is triggered if the cancellation, interruption, or postponement is caused by factors that are beyond the policyholder's control. They typically insure a wide range of events, including concerts, sporting events, conventions, conferences, exhibitions, and trade shows. These policies have provided coverage, for example, when a policyholder incurred losses arising out of the cancellation of music concerts in the aftermath of the 9/11 terrorist attacks.

Trade Disruption Policies

Trade disruption policies are designed to protect against loss of earnings and extra expenses caused by disruption

in the supply chain, even when there is no physical loss or damage to the policyholder's assets. This coverage was designed specifically for businesses that depend on global supply chains.

Commercial General Liability ('CGL') Policies

CGL policies may provide coverage for defense costs and judgments or settlements that the insured pays due to "bodily injury" or "property damage" alleged by customers or other third parties. In particular, individuals may allege that they became sick or suffered other damage because the insured failed to take necessary precautions to prevent exposure to various components of crude oil that may pose health risks, particularly for individuals with pre-existing health conditions such as asthma. In the absence of manifest bodily injury, some lawsuits may even seek to require a business to fund medical monitoring programs for the benefit of local residents. Medical monitoring claims raise the issue of whether they seek "damages" because of "bodily injury" within the meaning of the CGL policies. Courts have acknowledged that medical monitoring claims seek "damages" on account of "bodily injury," and thus have ruled that CGL policies cover at least the costs of defending such claims. Businesses in the medical, hotel, travel, and entertainment industries, for example, may be more vulnerable to third-party claims, because individuals may allege that businesses in such industries had an obligation to have proper procedures and plans in place to help protect third parties, such as patients and customers, from unreasonable risk or exposure.

Policy Conditions And Requirements

Most insurance policies require that a policyholder notify its insurance carrier "as soon as possible" or "as soon as practicable" after a loss or other insured event. Some policies may contain provisions which require that notice be given within a certain number of days (e.g., 30 or 60 days). Here, the exact date of the commencement of the loss is unknown at this time.

As part of this notice (which should be in writing), the policyholder usually must identify itself and provide information about the time, place, and circumstances of the loss. This notice requirement is intended to give an insurer a chance to investigate a loss or claim while the evidence is still fresh. It also provides some assurance to the insurer that it can take steps on behalf of the policyholder to minimize future damage and helps the

insurer to assess its obligations and determine whether the policy applies to the particular loss or claim.

The consequences of failure to give prompt notice differ, depending on the type of policy and the jurisdiction. Many jurisdictions also require that if an insurance company uses late notice as a defense to coverage, the insurer must prove that it was prejudiced as a result of the late notice. Prejudice can take many forms, including lost ability to gather evidence or interview witnesses. Other jurisdictions either have no prejudice requirement, or place the burden on the policyholder to prove that the insurer was not prejudiced by the late notice.

A policyholder may have legitimate reasons why notice cannot be given immediately after a loss, for example, lack of knowledge of an actual loss. To the extent possible, however, a policyholder should do what the policy requires and give notice as soon as practicable or within any time limits set by the policy. An experienced coverage attorney can assist a policyholder with identifying policy deadlines, determining the proper time to give notice, and providing notice of a claim.

Mitigation Costs

Even if the oil from the spill does not reach a business' property, insurance policies nevertheless might provide coverage for mitigation costs (i.e., costs that the policyholder incurs to prevent or mitigate imminent or actual losses). Many companies already have expended, or soon may expend, substantial sums to minimize their risk of loss associated with the oil spill. For example, companies may purchase equipment, such as booms, in an effort to protect property from contamination. Insurers may be obligated to pay for these measures to help prevent property damage, just as they often must pay for the costs of boarding up a building's windows when a hurricane is approaching. The legal theory is simple: policyholders should take reasonable steps to minimize or reduce their losses, thus saving money for themselves and their insurers, and their insurers should pay for these steps. These costs might be covered even if the policyholder never actually incurs losses due to the oil spill.

Insurer Defenses to Coverage

When a policyholder makes a claim for coverage, insurers may raise challenges to the availability of

coverage. These challenges may include disputes regarding: (a) whether physical damage to insured property is required to trigger time element coverage such as business interruption coverage, and, if so, what may qualify as property damage; (b) whether there is coverage for amounts spent to prevent or mitigate damages, even if property damage never takes place; and (c) whether coverage for claims related to the oil spill is barred by any policy exclusions.

Companies should not assume that insurer defenses necessarily will defeat coverage. For example, a policyholder may be able to argue that damage to a hotel's grounds and beaches caused by the oil slick constitutes property damage. Further, amounts spent to mitigate damage may be recoverable if the policyholder can demonstrate that it incurred these costs in a reasonable effort to protect against a covered loss and that the threat of loss was sufficiently imminent. Finally, whether coverage is provided or barred by any exclusion requires a careful analysis based on the specific policy language involved, the facts of a company's particular losses, and the law of the applicable jurisdiction.

Scope Of Losses And Coverage

It is critical that policyholders assess as quickly as possible the extent of any losses and the scope of coverage

for those losses. Insurers will seek detailed proof of the loss claimed under the policy and documented evidence of the expenses incurred in responding to that loss. Policyholders will need to understand fully the scope of coverage afforded by their policies in order to maximize the potential for recovering all covered losses.

Obtaining And Maximizing Insurance Recovery

Pursuing an insurance claim following a disaster often is a complex and challenging process, especially when management and employees are faced with post-disaster challenges both at work and at home. Policyholders should consider obtaining the assistance of coverage counsel, because there are many issues that can affect significantly the existence or amount of recovery under an insurance policy. For example, certain causes of loss may be excluded from coverage, while others are not. Resolution of that issue may depend not only on the law of a particular state that will be applied and the facts presented by a claim, but also on the way in which the facts are presented to the insurance company or, ultimately, to a court, if insurance litigation is necessary. An attorney may be able to analyze how the resolution of these issues will impact insurance recovery. An attorney also may help the policyholder provide notice of its claim and present its claim in a way that maximizes recovery. ■