

Client Alert

June 2016

FLOOD WARNING: Are You Covered?

Last week's torrential rains have caused widespread flooding in West Virginia and surrounding areas. It is important that policyholders in these and other areas remain mindful of the substantial benefits that may be available to them for resulting economic and physical losses under ordinary business insurance policies. Policyholders also should be mindful of the interplay between coverage for flood under business insurance policies and assistance that may be available from state and federal agencies (e.g., FEMA). Finally, policyholders also should stand ready to enforce their rights when insurers attempt to limit coverage for flood, since insurer tactics sometimes do not hold water.

Power outages, roof collapses, landslides and road closures, among other things, will invariably result in business interruptions, supply chain and logistics disruptions, event cancellations and, consequently, lost earnings and extra expenses. Likewise, damage to vendors, customers and markets, including their supply and distribution chains, will in turn lead to production slowdowns and delays, sometimes many miles away from the location of any actual physical damage. Finally, damage to properties under construction or renovation may have a significant impact on contractors, property owners and developers, while damage to occupied properties may give rise to claims against property owners, landlords, building managers and condo/property-owners associations.

Quick action after the loss has occurred is critical to ensuring that timely and appropriate steps are taken, since any delay in reporting a covered loss may limit or altogether jeopardize otherwise available coverage.

Flood Losses for Which Insurance May Be Available

Flood waters do not discriminate: all businesses are vulnerable. Whether a business is a retailer, restaurant, manufacturer, distributor or service provider, damage caused by flooding can wreak havoc on operations and business income. And, different businesses are affected differently by flooding, even by the same physical damage. For instance, physical damage to a part supplier might impact that business as a property loss and a consequential loss of business income, whereas that same event might indirectly impact a product manufacturer that relies on the part supplier for parts or supplies. Likewise, the same event might also affect a supplier of raw materials used by the parts supplier, since the parts supplier's need for raw materials will be diminished during the time it takes to repair the physical damage. Companies supplying transportation, logistics and other essential support services also might be impacted, even though none has suffered physical damage.

Insurance can help pay for these losses. Commercial property policies often contain a number of specialized coverages that potentially apply to flood losses. Depending on the facts of the loss, one or more of those coverages may apply:

- **Physical Loss or Damage to Insured Property:** There is generally coverage for the cost to repair, replace or rebuild property that suffers physical loss or damage. Covered premises are usually listed and scheduled in the policy and may include not only buildings but also equipment and business personal property such as furniture, machinery and stock.

- **Flood**: Unlike standard homeowners' policies, commercial property policies often include coverage for loss caused by flood. This coverage is often subject to a sublimit or sublimits that offer different levels of coverage based on the flood zone(s) in which the affected property is located. It is critical to ensure that insurers properly apply any sublimits or flood zone limitations.
- **Wind v. Flood**: Virtually all property policies cover wind damage. Many property policies contain substantially reduced sublimits, or exclusions, for flood damage. It is important that policyholders examine the "cause" of their loss, and evaluate whether there are multiple causes, before submitting a claim. Property owners may also want to consider obtaining separate flood coverage, where available.
- **Collapse**: Some property policies will cover damage caused by collapse. Others may not afford that coverage, while still others may do so at a reduced sublimit. Knowing the cause of the loss here can be outcome determinative.
- **Expenses Incurred in Attempting to Mitigate or Stop the Damage**: Property policies typically cover the cost to avoid further loss. In fact, many policies affirmatively require that the insured safeguard the property and prevent further damage. Those costs should be reimbursed under the insurance policy.
- **Extra Expense Coverage**: Repairing or replacing damaged property is not the only expense when property is damaged. Often the cost of operating the business also goes up during the time when the business is affected by the storm or its aftermath. Extra expense coverage is intended to indemnify the insured for above-the-norm expenses caused by the insured event. Examples may include the cost of a generator when electricity is lost or costs incurred to operate at a temporary location.
- **Business Interruption Coverage**: Property policies generally cover lost income or profits caused by the interruptions, including slowdowns, of business activities, due to physical damage to the insured's property. The basic purpose of the coverage is to make the insured whole during the period it takes to rebuild or replace the property destroyed.
- **Contingent Business Interruption Coverage**: Even if a company's own property has not been damaged, its business may be interrupted by damage to the property of others, such as suppliers, customers or other business partners. In such circumstances the company's lost income often is covered by contingent business interruption coverage.
- **Orders of Civil Authority**: Coverage may also be available when business income is lost as a result of governmental directives preventing or restricting access to property. These losses may be recoverable even if the company's own property has not been damaged.
- **Ingress/Egress Coverage**: Similarly, many policies cover losses when ingress to or egress from a covered property is prevented or hindered by the event. This coverage may come into play in the event of road closures, the closing of mass transportation and other transportation problems.
- **Service and Utility Interruptions**: Losses and expenses caused by power, water and telecom outages can also have a significant impact on business operations and resulting losses may be covered under property insurance policies.
- **Builders' Risk Losses**: Contractors, building owners and developers may sustain losses potentially covered under builders' risk insurance. Such losses may arise from damage to buildings under construction or renovation, damage to staged construction materials,

contamination caused by hazardous materials on the job site, or general soft-cost losses caused by construction delays attributable to weather conditions or storm damage.

- **Landlord Liability:** Landlords may also face claims asserted by tenants for bodily injuries, damage to personal property and loss of use and related losses of rent. Likewise, claims may be asserted by third parties injured on leased or managed properties as a consequence of storm-related conditions. Such claims may be covered under landlord liability policies and/or general liability policies.
- **Building Association Liabilities:** Condo and building-owners associations may also face storm-related claims in the context of alleged failures to properly maintain roofs, doors, windows and walls in a manner that could weather the storm. Such claims may implicate coverages under associations' errors and omissions policies and directors and officers liability policies as well as property policies maintained by the associations for common building elements and systems.

The precise terms of the policy and applicable law govern the existence and extent of coverage. In addition, policies are often endorsed or contain exclusions that may expand or reduce coverage. Some applicable limitations on policies include sublimits on certain losses that limit the total available insurance for a particular type of damage, exclusions for flood or water damage, earth movement exclusions, government action exclusions that may not permit recovery for interruptions in business where government authorities limit access, etc. The burden is on the carrier to prove the terms and applicability of any exclusion of coverage in a policy. Exclusions are read narrowly and, where found to be ambiguous or not sufficiently notorious in the policy, they will be disregarded or construed in the light most favorable to the insured and in favor of coverage.

To maximize coverage, insureds are best served by a careful analysis of their policies, the law that will apply to any questions under those policies and a precise documentation and presentation of their loss during the claim process. Experienced coverage lawyers can help.

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Hunton & Williams LLP's insurance recovery lawyers assist policyholders secure the full benefits to which they are entitled in the event of any type of loss, including amounts spent to defend or settle large-scale litigation. For more information, please contact the members of the firm's Insurance Coverage Counseling and Litigation team.

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