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Protecting Business Income When Disaster Strikes

Whether a pipe bursts or there is a category 5 hurricane approaching, the hospitality industry faces unique challenges when disaster strikes (or even threatens). Beyond the damage to property accompanying any such disaster, hotels and on-site restaurants, spas and other resident vendors face lost earnings in the time it takes to repair and remediate damage or even just gain access to the affected area. Fortunately, policyholders can procure business interruption insurance that is designed to specifically address these loss scenarios. This coverage is designed to cover lost income or profits caused by the interruption of business activities due to physical damage to property. The damage need not be to the insured property — it may be enough that the damage occurred at the property of a key vendor or customer, or simply in the vicinity of the business. Most policies, do however, require that the physical damage be of the type covered under the applicable policy.

Typical business interruption provisions provide that the insurer “will pay for the actual loss of Business Income you sustain due to the necessary suspension of your operations during the period of restoration.” The “period of restoration” is the time necessary to rebuild, repair or replace the damaged property. This period typically begins within 24–72 hours following the physical damage and usually continues until the affected property is repaired or replaced to its pre-loss condition or, when the property is not repaired or replaced, the period lasts for the amount of time it would have taken for such repairs.

Where coverage disputes typically arise, however, is in determining the level of interruption needed to trigger coverage under the particular policy at issue. Most business interruption coverages require a “necessary suspension” of operations. However, most policies do not define what a “necessary suspension” entails. Thus, interpreting what constitutes “necessary suspension” of operations sufficient to trigger coverage is often a point of contention, with insurers arguing that a total cessation is required. Whether a policy requires a total cessation of operations or something less will turn on a number of factors, including the particular language at issue, the state’s law under which the insurance policy is to be interpreted, representations made during the underwriting and procurement of the policy and the parties’ prior dealings on similar type claims.

Until these and any other relevant factors are considered, policyholders should not presume that their lost income is not covered simply because

portions of their business continued to operate following the physical damage. Thus, policyholders in the hospitality industry should review their property policy to determine whether the business interruption provisions require total cessation of business or whether the policy defines suspension to include when a business is partially suspended or reduced, and consult with a legal professional about the way those terms have been construed by the courts. Likewise, at renewal time, policyholders should consider endorsements that redefine “suspension” for maximum coverage even where operations are only reduced due to a covered loss.

In addition to traditional business interruption coverage, policies may also provide coverage for circumstances in which an insured’s business is interrupted by damage to someone else’s property, regardless of whether the insured’s property was damaged at all. Contingent business interruption coverage will afford coverage for loss of income where a supplier, customer or business partner suffers property damage that results in lost income to the insured. Additionally, your property policy may include civil authority coverage that provides coverage for when business income is lost as a result of governmental orders preventing or restricting access due to property damage occurring elsewhere. Finally, policies may provide coverage for lost business income due to when ingress to or egress from your property is prevented by an event or when service and utility outages impact business operations.

When disaster strikes and a claim arises, be sure that you’re prepared by working with experienced coverage attorneys now to identify any gaps in your existing coverage and to ensure that you’ve purchased the maximum coverage necessary to protect your business.

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