

Emerging Issues in Commercial Property Insurance

by

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I. SELECTED RECENT CHANGES TO THE ISO CP FORMS

A. ADDITIONAL COVERAGE – FUNGUS

1. Causes of Loss – Special Form

The 2002 edition of form CP 10 30 (Causes of Loss – Special Form) excludes loss due to the presence of fungus, wet rot, dry rot or bacteria unless such loss results from fire or lightening or coverage is provided by this new coverage. The purpose of the change is to define and limit mold coverage. See IRMI CPI – Annotated CP 10 30 (available at <http://www.irmi-online.com>). The changes result from the surge in mold-related insurance claims during the last few years before the revisions.

This coverage applies to (a) direct physical loss, (b) the cost of tearing out and replacing property to gain access to the fungus, etc. and (c) the cost of testing performed after restoration if there is a reason to believe fungi, wet or dry rot or bacteria are present – subject to a \$15,000 annual aggregate limit. See *id.* If the policy includes business income a/k/a business interruption (“BI”) or extra expense coverage and the insured’s operations are suspended as a result of a covered loss other than fungus, etc., but mold remediation increases the period of restoration, BI and extra expense coverage is increased up to an additional 30 days. *Id.* If the loss that caused the mold does not require cessation of operations, but the mold loss does, BI or extra expense coverage is available for a maximum of 30 days. *Id.*

This additional coverage is limited to \$15,000 for all loss or damage occurring within a 12-month period beginning on the annual inception date of the policy. *Id.* According to the policy form, this sublimit applies even if the fungus, etc. continues or recurs in a subsequent policy period. *Id.* This coverage can be increased by including the changes fungus, wet rot, dry rot, and bacteria endorsement (CP 04 31) as part of the policy. *Id.* The new limits associated with the cover will be set forth in the “Revised Limit” section of the changes endorsement. The changes endorsement can also be used to extend fungus additional coverage to separate premises or other locations by scheduling such other locations in the endorsement. *Id.* If separate premises or locations option is selected, the \$15,000 aggregate limit (or revised limit if purchased by endorsement) applies separately to each scheduled location. *Id.* The change endorsement can also be used to increase the period applicable to BI or extra expense coverage under the fungus additional coverage form from 30 days to the number of days stated in the endorsement. *Id.*

The special causes of loss form also includes the following related 2002 changes:

- A new Group 1 exclusion that eliminates coverage for loss from fungus, wet and dry rot and bacteria, except as provided in the new fungus additional coverage. This exclusion does not apply to such losses resulting from fire or lighting or ensuing loss from any of the “specified causes of loss”.¹

¹Defined in the policy form as “fire, lightening, explosion, windstorm or hail, smoke, aircraft or vehicles, riot or civil commotion, vandalism, sprinkler leakage, sinkhole collapse, volcanic action; falling objects, weight of snow, ice or sleet, and water damage.” See IRMI CPI – Annotated CP 10 30 (available at <http://www.irmi-online.com>).

- The word “fungus” has been eliminated from the “wear and tear” exclusion.
- The Group 2 exclusion for continuous seepage or leakage over a period of 14 days or more has been revised to specifically apply to the “presence or condensation of humidity, moisture, or vapor” that occurs over a period of 14+ days.
- The definitions section of the form now defines fungus to mean any type of fungus, including mold or mildew, and any mycotoxins, spores, scents or by-products produced or released by fungi.

Id.

2. Causes of Loss – Basic and Broad Form

The 2002 editions of form CP 10 10 (Causes of Loss – Basic Form) and form CP 10 20 (Causes of Loss – Broad Form) also exclude loss due to the presence of fungus, wet rot, dry rot or bacteria unless such loss results from fire or lightening or coverage is provided by this new coverage. The fungus additional coverage provision in both forms are the same, except for the language contained in paragraph 5. *See* IRMI CPI – Annotated CP 10 20 (available at <http://www.irmi-online.com>). The broad form stipulates the fungus additional coverage does not increase or decrease the coverage provided by the (a) sprinkler leakage peril, (b) the water damage peril and (c) collapse additional coverage. *Id.* The basic form includes the same stipulation with regard to the sprinkler leakage peril only.² *Id.* Another minor difference between the forms is the paragraph numbering resulting from the different coverages afforded by the basic and broad forms. *Id.*

The basic causes of loss form and the broad causes of loss form also include the following related 2002 changes:

- Like the special cause of loss form, both forms include a new Group 1 exclusion that eliminates coverage for loss from fungus, wet and dry rot and bacteria, except as provided in the new fungus additional coverage. This exclusion does not apply to such losses resulting from fire or lighting or ensuing loss from any of the “specified causes of loss”.
- With regard to the water damage peril contained in the broad form, the exclusion for loss from continuous seepage or leakage over a period of 14 days or more has been revised to specifically apply to the presence or condensation of humidity, moisture, or vapor that occurs over a period of 14+ days, comparable to the revision in the Group 2 exclusions in the special cause of loss form.
- The appliance leakage exclusion contained in the basic form has been revised to exclude loss from continuous seepage or leakage of water, or the presence or condensation of humidity, moisture or vapor that occurs over a period of 14+ days – even if it results from covered damage to a system or appliance.

²The basic form does not include the water damage peril or the collapse additional coverage. *See* IRMI CPI – Annotated CP 10 20 (available at <http://www.irmi-online.com>).

- Both forms also define fungus to mean any type of fungus, including mold or mildew, and any mycotoxins, spores, scents or by-products produced or released by fungi.

Id. Other than the foregoing differences, the fungus additional coverage available under the basic cause of loss form and broad cause of loss form mirrors that provided by the special cause of loss form discussed above.

B. ELECTRONIC DATA

The 2002 edition of CP form 10 00 (“Property Not Covered”) was revised primarily to address the status of electronic data. *See* IRMI CPI – Annotated CP 10 00 (available at <http://www.irmi-online.com>). Paragraph 2.n. was added to the list of property not covered to demonstrate electronic data is not covered except as provided under electronic data additional coverage, also a new edition to the 2002 form.³ *Id.* Disputes about whether electronic data qualified as covered property, and if so, what constitutes direct physical damage to such property prompted these revisions. *Id.*; *see also*, *American Guar. & Liab. Ins. Co. v. Ingram Micro, Inc.*, No. 99-185, 2000 U.S. Dist. LEXIS 7299 (D. Ariz. 2000)(holding “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.”)

Electronic data additional coverage under each of the three causes of loss forms provides coverage for the cost of replacing or restoring electronic data destroyed or corrupted by a covered cause of loss (including computer virus) subject to an annual aggregate limit of \$2,500. *See* IRMI CPI – Annotated CP 10 00. None of the causes of loss forms extends this coverage to loss caused by the manipulation of a computer system or computer data by an employee, whether permanent, temporary or leased, or by an entity that is retained by or for the insured to inspect, design, install, or otherwise work on the system. *Id.* Coverage under the special causes of loss form is limited to loss from one of the “specified causes of loss” or collapse pursuant to collapse additional coverage. *Id.* Similarly, under the broad causes of loss form, collapse additional coverage extends electronic data coverage to losses from collapse. *Id.* Notably, electronic data additional coverage does not apply to loss to electronic data from covered causes of loss added by endorsement. *Id.*

This annual aggregate limit for this coverage cannot be increased by endorsement. *Id.* However, form CP 04 30 (the electronic commerce endorsement) extends coverage for direct damage and time element losses caused by destruction or corruption of electronic data from a covered loss (subject to various limits and provisions), but only if the insured uses the electronic data in its e-commerce activities; loss to electronic data used by the insured in other areas of its business is not covered by the e-commerce endorsement. *Id.*

³The 2006 edition of the BOP form 00 03 provides comparable electronic data additional coverage subject to an annual aggregate limit of \$10,000.

II. THE “DIRECT PHYSICAL LOSS” DEBATE

Generally, commercial property coverage (including time element coverages) requires the insured sustain direct physical loss of or damage to Covered Property in order to trigger coverage. *See, e.g.*, ISO CP form 00 10 (Building and Personal Property Coverage form); *see also*, ISO CP 10 30 (Special Causes of Loss Form – Covered Causes of Loss); ISO CP 00 30 (Business Income Coverage (and Extra Expense) Coverage Form); ISO CP 00 32 (Business Income Coverage Form (without Extra Expense)); CP 00 50 (Extra Expense Coverage Form) and CP 00 60 (Leasehold Interest Coverage Form). This requirement is further evidenced by the exclusion for “delay, loss of use or loss of market” in the Special Causes of Loss Form which reinforces the coverage grant in the building and personal property coverage form (CP 00 10) (“We will pay for *direct physical* loss of or damage to covered property”)(emphasis added). This exclusion applies to preclude coverage even if the delay, loss of use, etc. results from covered physical damage to covered property. *See* IRMI CPI – Annotated CP 10 30 (available at <http://www.irmi-online.com>). Despite this seemingly unambiguous requirement, courts struggle with the physical damage issue. This struggle is best demonstrated by a recent case from the Eighth Circuit Court of Appeals: *Source Food Technology, Inc. v. United States Fidelity & Guaranty Company*, 460 F.3d 995 (8th Cir. 2006), superseded by *Source Technology, Inc. v. United States Fidelity & Guaranty Company*, 465 F.3d 834 (8th Cir. Oct. 13, 2006).

Source Food is a beef wholesaler. In the spring of 2003, it obtained all product from a single Canadian supplier. Around that same time, the USDA closed the border to all Canadian beef and beef products triggered by concern about Mad Cow disease. At the time of the embargo, the Canadian supplier had a shipment prepared and loaded for delivery to Source Food, but did not ship the order because of the embargo. Source Food temporarily ceased operations to secure an alternative supplier and lost a key customer in the process. Source Food subsequently filed a BI claim, which USF&G denied because of a lack of “direct physical loss”.⁴ The parties stipulated the lost shipment of beef was not contaminated. The trial court granted the insurer’s motion for summary judgment, reasoning the policy did not provide BI coverage for a loss resulting from the embargo of an uncontaminated product. The appellate court reversed, explaining:

Under Minnesota law, ‘direct physical loss’ can exist without actual destruction of property or structural damage to property; it is sufficient to show that insured property is injured in some way. The district court’s interpretation of [the] insurance policy denies Source Food the coverage that it purchased. The policy was a business interruption policy meant to cover the actual loss of business income when Source Food’s business was suspended because of loss of property. Source Food’s business was stopped when the . . . government closed the border . . . prohibiting Source Food from using beef it had purchased . . . Whether Source Food’s beef was actually tainted is not controlling; it was treated as tainted by the United States government.

⁴Source Food relied upon the Business Income and Action by Civil Authority provisions in its policy. *See Source Food*, 460 F.3d at 996.

Source Food, 460 F.3d at 997 (internal citations omitted). In reaching its conclusion, the appellate court distinguished various Minnesota cases requiring direct physical loss, reasoning those cases did not depend upon contamination as much as its effect; *i.e.*, the functional impairment of the property. *Id.* The court also distinguished *Pentair* (discussed below) reasoning that the insured in that case only lost power for a period of time and did not sustain any direct physical loss of property unlike *Source Food* who lost the use of its product as a result of governmental regulation. *Id.* at 997-98. Notably, Judge Gruender dissented because the unambiguous policy language required direct physical loss:

To characterize *Source Food*'s inability, due to a government order, to transport its truckload of beef product across the border and sell the beef product in the United States as "direct physical loss to Property" would render the word 'physical' meaningless. I also note that the Court's analysis either ignores the policy's use of the word "to" in the policy language "direct physical loss to Property" or substitutes the word "of" for "to", as in "direct physical loss of property" or even "direct loss of property", which are not phrases found in the policy. I find that the policy's use of the words "to property" further undermines the Court's conclusion that functional impairment . . . due to a border crossing triggers insurance coverage under this insurance policy.

See id. at 999 (emphasis in original). Judge Gruender authored the opinion on rehearing.⁵ Not surprisingly, the court reversed and superseded its original opinion, finding the cases upon which the prior opinion relied involved physical contamination. On rehearing, the court concluded the embargo applicable to *Source Foods*' loss could not constitute a direct physical loss because it did not involve physical contamination or damage, reasoning to hold otherwise would render the word "physical" meaningless since the beef product had not been physically damaged in any way. *Source Food*, 465 F.3d at 838.

Another recent case, *United Air Lines, Inc. v. Insurance Company of the State of Pennsylvania*, 439 F.3d 128 (2nd Cir. 2006), adhered to the policy requirement of direct physical loss to deny coverage for business interruption resulting from lost earnings at any ticket office other than the office actually located in the World Trade Center following the September 11, 2001 terrorist attacks.

III. BUSINESS INCOME FROM DEPENDENT PROPERTIES A/K/A CONTINGENT BUSINESS INTERRUPTION

A. WHAT IT DOES

Business Income from Dependent Properties a/k/a Contingent Business Interruption ("Contingent BI") coverage is often purchased as an addition to the insured's commercial property insurance policy. Contingent BI insures against loss of profits caused by physical loss or damage to third-party property upon which the insured's business depends. Typically, this type of coverage is often used by businesses that:

⁵The judge who authored the original opinion retired in the interim and did not participate in the matter on rehearing. *See Source Food*, 465 F.3d at 834 n. 1.

- rely upon a single supplier or a few suppliers for materials;
- obtain most of their merchandise from a single supplier or a few suppliers; and
- depend upon a neighboring business to draw customers to its own business.

Daniel T. Torpey, et al., *THE BUSINESS INTERRUPTION BOOK* 271 (2004). Dependent property is divided into the following general categories:⁶

Contributing locations	those that delivery materials/services to the insured or on its behalf ⁷
Recipient locations	those that accept the insured's products/services ⁸
Manufacturing locations	those that manufacture products for the insured's customers under a contract of sale ⁹
Leader Locations	those that attract customers to the insured's business ¹⁰

There are three general categories for Contingent BI coverage: (1) standard form, (2) company form and (3) broker/manuscript form. Daniel T. Torpey, *CONTINGENT BUSINESS INTERRUPTION: GETTING ALL THE FACTS* (2003) (available at <http://www.irmi.com>). Standard forms, such as those promulgated by ISO, are most common, but usually offer the least comprehensive coverage. *Id.* Company/manuscript forms provide the broadest coverage and are typically used by Fortune 100 companies. *Id.*

Generally, an insured usually must establish the following in order to present a valid Contingent BI claim:

- an actual loss of business income
- caused by the necessary suspension of operations
- as a direct result of physical loss or damage occurring
- to a dependent property
- which is caused by a covered peril.

See ISO CP 15 0 8 04 02 (Business Income from Dependent Properties – Broad Form).¹¹

⁶*See* ISO CP 15 08 04 02 (available at <http://www.irmi-online.com>).

⁷Alan R. Miller, *Business Interruption Coverage for Damage to Other Property*, 53 FED'N DEF. & CORP. COUNS. Q. 343, 347 (2003).

⁸*Id.*

⁹ISO CP 15 08 04 02.

¹⁰*Id.*

To obtain Contingent BI coverage, the insured should schedule the dependent properties because the standard form provides such coverage only to the extent physical loss or damage occurs at dependent properties expressly scheduled therein. *See* ISO CP 15 08 04 02. However, an insured may receive limited Contingent BI coverage for unscheduled properties under the following additional coverage grant found in most policies:

We will pay for the actual loss of Business Income you sustain due to a direct physical loss or damage at the premises of a “dependent property” not described in the Schedule caused by or resulting from any Covered Cause of Loss. But we will not pay more than .03% of the Limit of insurance for each day’s “suspension” of “operations” due to loss arising from any one location.

See, e.g., ISO CP 15 08 04 02. Arguably, an insured should schedule all dependent properties to achieve maximum coverage.

B. SAMPLE CASES

- ❖ *Snelling and Snelling, Inc. v. Federal Ins. Co.*, No. 05-11402, 2006 WL 3019188 (5th Cir. Oct. 23, 2006).

The insured sought Contingent BI coverage following the terrorist attacks on September 11, 2001, that affected several of its clients. Specifically, several clients to whom the insured provided temporary workers sustained physical loss and damage as a result of the attacks which adversely affected the insured’s business at its office located near the World Trade Center. The policy included Supplementary Declarations for Dependent Business Premises with aggregate limits of \$250,000 for any single Snelling office. The parties agreed the policy provided Contingent BI coverage for this loss; however, they disagreed on the amount of coverage available under the policy.¹² The policy stated:

¹¹The 2006 revisions to the BOP form include the following change to Contingent BI coverage, which restricts the Contingent BI coverage afforded by the BOP policy:

Policy Change Area	Businessowners 2002	Businessowners 2006
5.m. (1) Business Income from Dependent Properties	Provides coverage for loss of business income from dependent properties caused by property damage to electronic data at dependent properties	Provides coverage for loss of business income from dependent properties when caused by (a) property damage to electronic data <i>and</i> (b) other property at the dependent properties ¹¹

¹²The insured argued alternatively that even if the applicable limits were \$250,000, it was entitled to collect \$250,000 per occurrence (*i.e.*, per each customer who sustained physical loss or damage) not to exceed \$4 million per the Declarations. *Snelling* at *12. The court dismissed this argument, explaining the injury and damage to each customer resulted from a single cause – airplanes flying into the Twin Towers. *Id.* at *13-14.

we will pay for the actual business income loss . . . you incur due to the actual or potential impairment of your operations . . . not to exceed the Limit of Insurance for Dependent Business Premises shown under Business Income in the Declarations.

Id. at *7. The insured argued it was entitled to policy limits (\$4 million) per the Declarations, whereas the insurer argued the Supplementary Declarations dictated the limits for this coverage. The court agreed with the insurer because the only section in the entire policy that specified “Limit of Insurance for Dependent Business Premises” was the Supplementary Declarations, rather than the initial Declarations.

❖ *Pentair, Inc. v. American Guar. & Liab. Ins. Co.*, No. 06-3696, 2003 WL 21804874 (D. Minn. 2003 (not designated for publication)).

The insured sought Contingent BI coverage following an earthquake in Taiwan that affected two foreign manufacturers from whom the insured’s subsidiary purchased portable power supply units and battery chargers. Specifically, both manufacturers lost power because the earthquake damaged an electrical substation, which resulted in a two-week delay in the manufacturing process. The insured experienced increased shipping costs because the manufacturers shipped the finished goods via air rather than by sea to guarantee delivery by Christmas and sought to recover the increased costs because the policy insured against “loss resulting from damage to or destruction by perils insured against, of: . . . property of a supplier of goods and/or services to the insured.” *Id.* at *2. On cross-motions for summary judgment, the insurer prevailed because the damage to the substation was not a “peril insured against” under the policy because it did not involve “direct physical loss or damage” to a “supplier of goods and/or services to the Insured.” *Id.* at *3. Contrary to the insured’s argument, the insured’s loss resulted from physical damage or loss to the substation that supplied electricity to the insured’s suppliers, and the substation was not a supplier of goods or services to the insured. *See id.*

IV. CIVIL AUTHORITY COVERAGE

A. WHAT IT DOES

Civil authority coverage extends BI coverage to the insured where its premises have not been physically damaged, but the insured nevertheless sustains a loss of income from the interruption or suspension of its business operations as a result of an order of a civil authority. *See, e.g., Travelers Indem. Co. v. Pollard Friendly Ford Co.*, 512 S.W.2d 375, 382 (Tex. Civ. App. – Amarillo 1974, no writ); *U.S. Airways, Inc. v. Commonwealth Ins. Co.*, No. 03-587, 2004 WL 1094684 (Va. Cir. Ct. May 14, 2004). For example, in the face of an oncoming hurricane, a governmental authority may issue an evacuation order. Even if the insured’s business does not sustain physical loss or damage as a result of the hurricane, the insured still experiences an economic loss caused by the cessation of business as a result of the evacuation. Commercial property policies do not provide coverage for this type of loss because BI coverage applies only when the interruption results from physical damage to the insured’s premises. A typical civil authority provision is found in the ISO Civil Authority Coverage Extension, which states:

We will pay for the actual loss of Business Income you sustain . . . caused by action of civil authority that prohibits access to the described premises due to direct physical loss or damage to property, other than at the described premises, caused by or resulting from any Covered Cause of Loss.

ISO CP 00 30 10 91. Generally, an insured must establish the following in order to present a valid Civil Authority claim:

- an order of civil (or military) authority prohibiting the insured from accessing its premises
- which results from direct physical loss of or damage to property other than the insured's property
- which is caused by a covered peril and
- results in actual loss of business income.

Brown & Borow, BUSINESS INTERRUPTION AND EXTRA EXPENSE COVERAGES: STRATEGIC CONSIDERATIONS IN CATASTROPHIC LOSSES, 205 Texas Ins. Law Symposium at pp. K-7 – K-8 (2005). Of course, forms other than the ISO form may be more restrictive or expansive with regard to this type of coverage.¹³ The scope of coverage available is dictated by the policy and may also include other limitations, such as a separate sublimit, a specific time limit (often two weeks to thirty days) and/or a waiting period (often 24 to 48 hours after the order), in addition to other policy exclusions.

B. SAMPLE CASES

❖ *U.S. Airways, Inc. v. Commonwealth Ins. Co.*, No. 03-587, 2004 WL 1637139 (Va. Cir. Ct. May 14, 2004).

Following the September 11 attacks and in the wake of the federal government's order closing Reagan National Airport immediately thereafter, U.S. Airways sought coverage for business interruption under the "Interruption by Civil or Military Authority" clause in its policy which covered "loss sustained during the period of time, not to exceed 30 consecutive days when, as a direct result of a peril insured against, access to real or personal property is prohibited by order of civil or military authority." *Id.* at *1. The insurer denied coverage, arguing the order was not the result of a peril covered by the policy, but rather was a "precautionary measure taken to prevent property damage and injury that had not yet occurred." *Id.* at *3. In addition, the insurer argued the policy required the insured's property suffer actual damage. *Id.* at *4. The

¹³For example, some policies do not require physical damage. See, e.g., *Fountain Powerboat Indus., Inc. v. Reliance Ins. Co.*, 119 F.Supp.2d 552, 557 (E.D. N.C. 2000)("[t]he policy is extended to cover the loss sustained during the period of time when, as a direct result of a peril not excluded, access to real or personal property is prohibited by order of civil or military authority."). Others impose a physical damage requirement with an additional proximity requirement. See, e.g., *United Airlines, Inc. v. Insurance Co. of State of Pa.*, 439 F.3d 128 (2nd Cir. 2006)(requiring that civil authority order be the direct result of damage to "adjacent premises"); cf. *City of Chicago v. Factory Mut. Ins. Co.*, No. 02-C-7023, 2004 WL 549447 *3 (N.D. Ill. Mar. 18, 2004)(interpreting ingress/egress provision to deny coverage following FAA's ground stop order because the damage that resulted in the order did not occur at or within 1,000 feet of the insured property.)

insured argued not only did the plain language of the policy provide coverage for BI resulting from the intervention of civil authority, but also it did not specify actual damage to its property was required to trigger coverage. *Id.* at *3. The insured also argued it suffered a direct physical loss to its airport facility and its ability to serve its customers in light of the order. *Id.* The court denied the insurer's motion for summary judgment, finding the policy did not require damage to the insured's property prior to intervention by a civil authority in order to trigger coverage. *Id.* at *5. During the subsequent bench trial the court held the order closing the airport and the FAA's order closing the country's air space constituted covered events under the civil authority provision of the policy. *Id.*

In contrast, a federal court sitting in the Northern District of Illinois rejected a similar claim made by the City of Chicago for BI losses sustained at each of the City's three airports in the wake of the September 11 attacks in *City of Chicago v. Factory Mut. Ins. Co.*, No. 02-C-7023, 2004 WL 549447 (N.D. Ill. Mar. 18, 2004). There, the insured sought coverage under the Ingress/Egress and "Protection and Preservation of Property" provisions, rather than the civil authority provision. *Id.* at *2. The court held the ingress/egress provision excluded "indirect or remote loss or damage" and specifically required the prevention of ingress and egress result from physical damage to nonexcluded property, which the policy defined as including real property in which the insured has an insurable interest "or within 1,000 feet" of such property. *Id.* at *3. Because the physical damage occurred more than 1,000 feet from Chicago, the policy did not provide coverage under the ingress/egress provision. The "Protection and Preservation of Property" provision did not apply because coverage afforded thereunder was limited to BI "caused by temporary actions 'to prevent immediately and pending physical loss or damage insured by this policy'" and the ground stop order was not specifically aimed at protecting Chicago's air fields from a pending threat of attack *Id.* at *4.

❖ *Abner, Herrman & Brock, Inc. v. Great Northern Ins. Co.*, 308 F. Supp.2d 331 (S.D.N.Y. 2004).

Following the September 11 attacks, the insured sought BI and extra expense coverage because access to its business premises in lower Manhattan (which did not sustain physical damage itself) was limited by civil authority through September 14, 2001. From September 17, vehicle traffic was restricted to the area, but pedestrian access was permitted and public transportation was available. The insured argued the restrictions made it difficult of its employees to get to the property and to attend business meetings in the downtown area. Most notably, the insured's chairman complained the restrictions limited his ability to use the full-time driver his firm provided to him. *Id.* at 333-34. The insured's claim encompassed not only the time during which all access was restricted, but also the time during which access was available, but limited arguing the policy provided coverage when a civil authority "prohibits access to your premises." *Id.* at 334. The court granted the insurer's motion for summary judgment finding coverage existed up through September 14 only, because after September 17, access to the insured's premises was not prohibited by civil authority. *Id.* at 336-37.

- ❖ *Southern Hospitality, Inc. v. Zurich Am. Ins. Co.*, No. Civ. 02-923-C, 2003 WL 23416117 (W.D. Okla. Sept. 30, 2003).

Following the September 11 attacks and the FAA’s ground stop order, the insured sought BI coverage for lost hotel business under the civil authority provision that provided coverage for loss of business income “caused by action 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. . . .” *Id.* at 2. The insured argued the FAA’s order closing the airports hindered access to its hotels. The court rejected the claim because the order “did not have a direct effect on [the insured’s] hotels; rather the Order’s effect was tangential . . . The policy requires a civil order which bars access to the property on which [the] . . . hotels sit.” *Id.* The order did not prevent people from getting to the hotels; it merely limited the means by which potential patrons could travel to the hotels.

V. OTHER SELECTED PROPERTY CASES

- ❖ *Certain Underwriters at Lloyd’s v. KKM, Inc.*, No. 13-05-031-CV, 2006 WL 3803462 (Tex. App. – Corpus Christi Dec. 28, 2006)

The insured owned a building that collapsed as a result of corrosion of the steel reinforcement of the concrete beams and columns and sought coverage under its commercial property policy. The insurer denied the claim based upon the following provisions:

2. We will not pay for loss or damage caused by or resulting from any of the following:
 - d. (2) rust, corrosion, fungus, decay, decomposition, hidden or latent defect or any quality in property that causes it to damage or destroy itself.

* * *
2. We will pay for direct physical loss or damage to Covered Property, caused by collapse of a building . . . that is insured under this Coverage Form . . . if the collapse is caused by one or more of the following:

* * *

 - b. Decay that is hidden from view, unless the presence of such decay is known to an insured prior to collapse;

Id. at *4. The dispute centered on whether the policy provides coverage for a collapse caused by corrosion. The insurer argued the use of the terms “rust, corrosion, fungus, decay, decomposition, hidden or latent defect” demonstrated each term carries its own unique meaning such that rust is not corrosion; fungus is not decay, and so on, so the exception allowing coverage for collapse caused by hidden decay is not the same as collapse caused by corrosion.¹⁴ *Id.* The insured argued it was entitled to coverage because the policy was ambiguous because corrosion could mean decay, something similar to decay or something completely different from

¹⁴The court dismissed the insurer’s argument that “corrode” applies to metal substances and “decay” applies to organic materials. *Certain Underwriters at Lloyd’s*, 2006 WL 3803462 at *5.

decay. *Id.* Relying upon the plain meaning of “corrosion” and “decay” (which are not defined in the policy), as well as Texas Supreme Court precedent¹⁵ that “corrosion” and “contamination” are not synonymous as a matter of law, the court concluded the meaning of the policy was uncertain and the issue had been properly submitted to the jury (who found coverage). *Id.*

❖ *TRB Invests., Inc. v. Fireman’s Fund Ins. Co.*, 145 P.3d 472 (Cal. 2006).

The insured owned a commercial building that it leased to the Salvation Army beginning December 1, 2000. The Salvation Army left the property before the end of 2000, and the insured did not secure another tenant. It is undisputed the property lacked “enough business personal property to conduct customary operations” after the Salvation Army vacated the property. *Id.* at 474. In April 2001, the insured entered into negotiations with another potential tenant. By June 20, 2001, the insured hired an architectural firm and general contractor to renovate the building. By July 2, 2001, the insured entered into a lease agreement with the new tenant. Between June 20 and July 14, the general contractor and various subcontractors performed numerous tasks at the property. On the morning of July 16, workers found significant water damage at the property after a water heater or waterline burst sometime between July 14 and their arrival on the 16th. When the insured submitted a claim for water damage, the insurer denied it citing the following vacancy exclusion:

If loss or damage occurs to a building that has been vacant for more than 60 consecutive days prior to the occurrence of that loss or damage, we will:

a. not pay for any loss or damage caused by:

* * *

4. water damage;

* * *

Buildings under construction are not considered vacant.

Id. The trial court granted the insurer’s motion for summary judgment. On appeal, the insured argued the exclusion did not apply because a building is “under construction” during renovations and the work performed at its property constituted “construction”. The insurer argued the cancellation provision in the policy (which allowed it to cancel the policy “if the building ‘has been vacant or unoccupied 60 or more days’ but not if the building was ‘in the course of construction, renovation or addition.’”) demonstrated the term “construction” did not include “renovation.” *Id.* at 478. Although the intermediate appellate court agreed with the insurer’s interpretation of the policy, the supreme court disagreed, explaining:

Under such interpretation, if the insured conducted a “renovation” of the building and specified loss occurred during the renovation, then the insurer would not be obligated to pay under the vacancy exclusion since the “under construction” exception would not apply. At the same time, however, the insurer would not have the power to cancel the policy since the cancellation endorsement excludes “renovation[s].” This interpretation, which binds an insurer to a contract in which it is not obligated to provide coverage for lack of occupancy, makes little sense.

¹⁵ *McConnell Constr. Co. v. Ins. Co. of St. Louis*, 428 S.W.2d 659, 661 (Tex. 1968).

There would no principled reason why, if vacancy for purposes of renovation violates a provision of the insurance contract such that the insurer need not provide coverage, then the insurer should not also be empowered to cancel the contract based upon the same violation of the contract terms.

We believe the more reasonable interpretation is that the term “under construction” as used in the vacancy exclusion was meant to be the functional equivalent of “construction, renovation or addition” as used in the cancellation endorsement. . . .

Id. The supreme court then determined the appropriate inquiry should have been whether the building project resulted in “substantial continuing activities” at the premises during the relevant time period because “[w]hen there is substantial construction activity on the premises, the risk of loss becomes roughly equivalent to that of an occupied building, thus giving the insurer the benefit of its prior risk assessment.” *Id.* Not having sufficient information in the record to address this question, the supreme court remanded the matter.

❖ *Evergreen Nat’l Indem. Co. v. Tan It All, Inc.*, 111 S.W.3d 669 (Tex. App. – Austin 2003, no pet.).

TIA sought coverage under its commercial property policy (ISO CP 00 10 10 91) after tanning equipment was stolen from its truck which was parked in the parking of the shopping center in which TIA leased a suite. The parties agreed TIA suffered a direct cause of loss, theft is a type of loss covered by the policy and the stolen equipment was business personal property pursuant to the policy. However, the dispute centered on whether the stolen equipment constituted covered business personal property under the policy. Pursuant to the policy, “Covered Property” included “Your Business Personal Property” defined as:

Your Business Personal Property located in or on the building described in the Declarations or in the open (or in a vehicle) within 100 feet of the described premises consisting of the following . . . (2) Machinery and equipment . . . (4) All other personal property owned by you and used in your business

Id. at 673 (emphasis in original). At the time of the theft, the truck was parked in TIA’s designated parking area within 100 feet of the shopping center, but 280 feet from TIA’s salon. The Declarations listed the insured premises as “13945 North Highway 183, Suite C-5, Austin, TX 78717.” *Id.* at 674. Finding the policy ambiguous, the district court granted TIA’s motion for partial summary judgment after concluding the definition of “premises” included the common area parking lot. *Id.* at 676. The appellate court reversed, rejecting TIA’s interpretation of “described premises” because it eliminated the suite from the description contained in the Declarations. Thus, TIA was not entitled to coverage because the policy unambiguously “states on its face that it covers business personal property in or on Suite C-5 or within 100 feet of Suite C-5.” *Id.* at 678.

VI. POTENTIAL FUTURE ISSUES?

The use of ARTs (such as Captives, Risk Retention Groups, Self Insurance Groups and Risk Purchasing Groups), used more frequently for liability coverage, may increase in the commercial property field.

In addition, ISO released a list of issues it considers to be emerging issues,¹⁶ which includes the following relevant to commercial property coverage:

- Blanket property coverage which affects property coverage under both the CP and BOP policies
- Sub-microscopic property damage liability
- High-powered electromagnetic (EMP) bombs that produce very short but intense electromagnetic shock waves that destroy telecommunications and computer equipment.
- SARS/Avian flu pandemic that could affect property coverage.
- Climate changes that could increase climate-related disasters that could affect property coverage.

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¹⁶ Available at <http://www.iso.com/ils/0000/isl0011.html>.