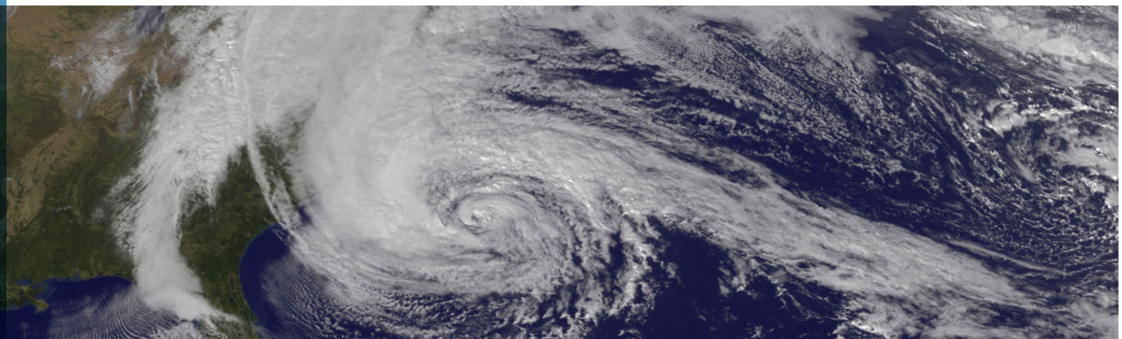

AmWINS Group, Inc.

10 ISSUES IMPACTING HURRICANE INSURANCE COVERAGE

With another hurricane season just a few months away, and memories of last year's catastrophic storms still fresh in the minds of many, now is the time for retail brokers to ensure that they are aware of policy elements and language that can have a significant impact on coverage in the event of a hurricane or named storm loss. This article examines key issues and challenges that may affect coverage and how to address them in order to achieve the best coverage solution for your client.

1. NAMED STORM DEDUCTIBLES

It is important to review and understand the deductible language in your policy. In many cases, this language is only reviewed by insureds after there is a hurricane/named storm loss. The often-confusing wording regarding a percentage deductible can vary from insurer to insurer and apply to both property damage and business interruption (BI) claims.

In addition to understanding the amount of the percentage to be applied, it is essential to understand what the percentage is being applied against – per building, per location, per unit of insurance, per insurable value, or per total insured value – as each can result in different outcomes.

Similarly, while the location may be defined in the policy, it is important to remember that the definition may vary between policies. In one instance, it may mean all the building values at a single street address. If that is the case, brokers need to ensure that the Statement of Values/ Schedule of Values (SOV) submitted and any other endorsements that might consolidate a location into another location are examined and comport/comply to the policy wording. If there are five buildings, whether attached (common wall) or unattached, they may be considered as a location in the values to calculate the deductible.

> *The percentage, shown in the schedule above, of the **sum of all values** listed in the most recent Schedule of Values on file with the Company **for each separately identifiable building** or structure that has sustained a loss or damage and for which a claim is being made under this policy; subject to the minimum deductible shown in the schedule.*

In the example above, the percentage deductible would be calculated against all the values (Building, Business Personal Property, BI) on the line for a particular building on the schedule. The percentage deductible is only being applied on a per building basis. However, it includes all the other values on the SOV for that building line.

It is important to compare and understand how the BI claim will be managed and if there is a separate deductible, or if it is part of the overall deductible by being part of the sum of all values listed.

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CONTACT

To learn more about how AmWINS can help you place coverage for your clients, reach out to your local AmWINS broker.

LEGAL DISCLAIMER

ABOUT THE AUTHOR

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In another situation, the BI percentage may be calculated against the values at the location where the physical damage occurred **plus** that proportion of the values at all other locations where loss ensues that was directly affected by use of such lost or damaged Covered Property and that would have been earned in the 12-month period following the "occurrence." This scenario could apply in the case of a warehouse, with the deductible being calculated against the warehouse BI values and all the stores affected by the loss of the warehouse, effectively rendering the deductible more than the loss.

2. FLOOD DEDUCTIBLE

The Flood deductible, which may come into play in a hurricane, must also be examined in relationship to the whole policy in order to determine the insured's out-of-pocket exposure. Below is a policy wording example:

> *As respects Locations wholly or partially within Special Flood Hazard Areas:*
> *Maximum available limits with National Flood Insurance Program (NFIP), whether purchased or not; plus $100,000 per Occurrence.*

Location is defined as:

> *The location **as specified in the Statement of Values** on file with [the carrier], but if not specified, location means any building, yard, dock, wharf, pier or bulkhead or any group of the foregoing bounded on all sides by public streets, clear land space or open waterways, each not less than two hundred feet wide. Any bridge or tunnel crossing such street, space or waterway shall render such separation inoperative for the purpose of this definition.*

Once again, it is important to understand the meaning of "location." Do not assume that each building on the **SOV is scheduled as an individual location** with its own separate statement of values, as this is not always the case. In the example above, the underwriter interprets it to mean all the buildings that include the street name in the building address, subjecting the insured to multiple maximum $500,000 deductibles (NFIP Max Flood Limit) -- not what may have been anticipated.

It is also important to confirm whether the location is wholly or partially within the Special Flood Hazard Area. If a corner of the building is within a flood zone, it may be considered partially within a flood zone and may be subject to the NFIP max limit as a deductible, which is $500,000 on commercial property.

3. WIND-DRIVEN RAIN

Let's consider a scenario in which there was a hurricane and each room on one side of the building has water damage, but there is no visible sign of damage to the exterior of the building. The adjuster inspects the building and points out that there is no exterior damage. It is determined that the wind had driven rain in through space in the window's frames or the packaged terminal air conditioners and heaters unit.

The insurer then points out that the policy has limitations citing that they "*will not pay for loss or damage to the interior of the building caused by or resulting from rain, snow, sleet, ice, sand or dust, **whether wind driven or not**, unless the building or structure first sustains loss by a Covered Peril of Loss to its roof or walls through which the rain, snow, sleet, ice, sand or dust enters.*"

Therefore, if the wind did not damage something on the exterior to allow water to enter, there is no coverage for the interior water damage. Coverage can be purchased for this type of limitation, for a premium.

4. EXCLUSIONS FOR MOLD, FUNGI, BACTERIA, ETC.

What if, in the above example, the insured had purchased the extra coverage to get around the wind driven rain limitation? Water had been driven in past the sliding doors, damaging the rug around the window, and even some sheet rock and trim. But did the water actually reach the furniture and fixtures?

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The adjuster points out that although the furniture was never touched by the water, the room now has moisture in it and the furniture is starting to collect mold. The underwriter then points out that you have an absolute exclusion regardless of causation for mold, fungi, bacteria, etc. In this instance, the best option is to mitigate the damage as soon as possible.

5. OFF-PREMISES POWER FAILURE

Power failures may differ in a variety of ways, including cause, duration, and impact. As a result, many policies have special exclusions related to BI and extra expense (EE). Below is an example of exclusionary policy wording:

> *"We will not pay for (1) any loss caused directly or indirectly by the failure of power or other utility service supplied to the described premises,* ***however caused****, if the failure occurs outside of a covered building."*

As such, any BI loss will only be covered if there is physical damage to the insured's "covered property" which damage prevents them from doing business. Let's contrast that language with the following example:

> *"Excluding the failure of power, communication, water or other utility service supplied to the described premises, however caused, if the failure: (1) Originates away from the described premises; or (2) Originates at the described premises, but only if such failure involves equipment used to supply the utility service to the described premises from a source away from the described premises."*

When there is coverage afforded, the interruption of power generally must be caused by physical loss of the type insured against under the insured's policy at a covered location. Most often, there will be a waiting period, and the duration of the BI will be measured in excess of the waiting period.

6. CIVIL AUTHORITY

When a natural disaster is approaching, residents may be asked to evacuate. As a result, businesses in the affected area will experience a lack of customers both before or after the event. Insureds may think they have a BI claim and make the claim under their civil authority coverage; however, in the example below, the insurer thinks differently and points out policy wording that limits the coverage.

> *When a Covered Cause of Loss causes damage to property* ***other than*** *property at the described premises, we will pay for the actual loss of Business Income you sustain and necessary Extra Expense caused by action of civil authority that* ***prohibits access*** *to the described premises, provided that both of the following apply:*
>
> *(1) Access to the area immediately surrounding the damaged property is prohibited by civil authority* ***as a result of the damage****, and the described premises are within that area but are* ***not more than*** *one mile from the damaged property;* ***and*** *(2) The action of civil authority is taken in response to* ***dangerous physical conditions resulting from the damage*** *or continuation of the Covered Cause of Loss that caused the damage, or the action is taken to enable a civil authority to have unimpeded access to the damaged property.*
>
> *Civil Authority Coverage for Business Income* ***will begin 72 hours*** *after the time of the first action of civil authority that prohibits access to the described premises and will apply for a period of up to four consecutive weeks from the date on which such coverage began.*

The insured confirms with the insurer that the covered property did not sustain any direct damage from the event, but due to the conditions in the area, the insured's business lost 50% of its income. The insured confirms that authorities did not prohibit access to **the described premise**, nor was there a documented evacuation order that displaced customers from the area and **then prevented access** to the insured's business, and/or **any physical damage within a mile** which caused the authorities to prevent access to the insured's premises.

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It is important to note that fear of property damage or injury in advance of or after an event are not coverage triggers. Therefore, **a call to evacuate is not civil authority coverage**.

The best example of a trigger of civil authority coverage is the 2016 Fort McMurray fire in Alberta, Canada. When a forest fire started to consume the town, residents of the town were ordered to evacuate, except for certain needed resources, and the **civil authority then prevented** the residents from returning for a period of time. Therefore, civil authority prevented access to the insured's premises, damage was within one mile of the insured locations, some insureds had direct damage, and the length of time exceeded 72 hours.

7. DEPENDENT PROPERTIES VS INTERDEPENDENCY CLAIMS

Dependent property coverage is sometimes confused with interdependency claims. Dependent property in general is defined *as properties **owned by others** whom the insured depends on to; a) deliver materials or services to the insured (but it does not include water, communications or power supply services); b) accept insured's products or services; c) manufacture insured's products; d) attract customers to insured's business.*

If an insured's location is not able to supply something to another insured location, this coverage **does not** apply.

Conversely, interdependency exists when an insured location suffers a loss that impacts another insured location. It is important to closely examine the policy language regarding interdependency, particularly as it relates to the time element, in order to avoid any unwelcome surprises in the event of a claim. Below is an example of policy language that references time element coverage:

> *If there is a loss at an insured Location that involves interdependency at one or more other insured Locations, the loss, including any resulting interdependency loss, will be adjusted based on the **time element** coverage that applies at the insured Location where the physical loss or damage insured by this Policy occurred.*

In this instance, the time element coverage that applies at the insured location will subject the other insured location to the same coverages that responded to the loss at the originating location **as well as the period of indemnity**. This statement in the policy does not refer to a location limit or even refer to schedule of values (SOV); however, an insurer may feel the intent is to subject the other location to any sub-limits or SOV values at the insured location. Brokers will need to add specific language if they want to avoid this interpretation.

8. CONTINGENT BUSINESS INTERRUPTION

Contingent BI is the go-to coverage when a supplier of a component or product to the insured's business is cut off due to an event that would have been covered under the insured's policy. For example, if the insured's policy has coverage for an explosion and an explosion is the cause of loss at the supplier, then the insured may have coverage for a Contingent BI claim. Since insured's are generally unable to investigate the facts of the supplier's loss themselves, one of the biggest challenges is supporting the cause of loss to the insurer.

Insureds must work with what the supplier will provide. It's also important to note that if there is another supplier who can provide the same material or product, the insured has an obligation to try to utilize that supplier in order to mitigate their loss.

9. REPAIR VS. REPLACE

There is often no easy answer to the question of whether the insurer repairs or replaces the damaged property. Let's consider an example in which the roof of a large commercial building starts leaking following a hurricane. The damage is limited, and the insured quickly has the area patched in an effort to stop the leak.

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When the insurer comes out with their expert to determine whether the roof needs to be replaced, they will take into consideration the age of the roof, prior repairs, normal wear and tear, and the extent of actual visible damage that may have undermined the integrity of the roof.

Finding that the roof repairs have essentially fixed the leak, and the roof is over 20 years old, the question is whether the insured is entitled to a complete replacement. The new patching is not cosmetically pleasing, and the new roof repairs may not last as long as the existing roof would have had no loss occurred. In this scenario, there is no simple solution and a negotiated settlement may be required.

10. BUSINESS INTERRUPTION PERIOD OF RECOVERY MEASUREMENT

While the period of recovery might not seem like an overly complex topic, several issues may arise that can affect coverage -- some of which may be addressed by the purchase of additional coverage. In general, the period of recovery begins immediately after the time of direct physical loss or damage caused by or resulting from any Covered Cause of Loss at the described premises and ends on the date the property at the described premises should be repaired, rebuilt or replaced **with reasonable speed and similar quality**.

Below are some of the issues that may impact the period of recovery:

- Delays due to:
  - Contract or lease issues
  - Lack of power to the insured's location
  - Change in design or upgrades
- Any delay in rebuilding caused by the interference of strikers or other persons
- Expectations for reasonable speed and similar quality

In addition, the period of recovery may not include the increased period due to enforcement of, or compliance with, any ordinance or law that regulates construction or pollution cleanup (building codes). Similarly, the period ends when the premises **should have** been repaired or rebuilt. The insurer's engineering experts will attempt to measure the period of recovery but will not account for unforeseen issues or other problems that may delay construction.

Finally, consideration of the probable increase or decrease in demand for the insured's business, even if from the same event that caused the physical loss, is becoming a contentious issue in the wake of widespread catastrophic events. The issue is of particular concern to insureds whose business is shut down as a result of a natural disaster.

The courts are addressing this issue in two ways. In some instances, they disregard the impact that the event had on the economy and measure the business against pre-catastrophe business levels. In others, they consider the current state of the local economy and seek to put the policy holder in the same position as if had no loss occurred.

CONCLUSION

As natural disasters become more frequent and cause greater damage, hurricane and named storm coverage has become essential in many parts of the country. The devastating nature of many of these storms underscores the importance of understanding how to provide insureds with coverage solutions that address their unique needs. The specialists at AmWINS work closely with retail brokers to ensure that they are aware of and understand policy elements that can have a significant impact on coverage in the event of a hurricane or named storm loss. Contact one of our experts today to learn more about the challenges that may affect coverage and how AmWINS can help you achieve the best hurricane coverage solution for your client.