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Hurricane Harvey Threatens Huge Losses, but Insurance Can Help Weather the Storm

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Coastal areas in Texas have already begun evacuating as Hurricane Harvey heads for the Gulf Coast. Weather experts anticipate that the windstorm will reach Category 3 or Category 4 status by the time it makes landfall on the Texas coast late Friday night or early Saturday morning, making it the first Category 3 or higher storm to make landfall in the United States since Hurricane Wilma hit South Florida in October 2005.

As the winds diminish and floodwaters recede, significant damage to property and resulting interruptions to businesses are expected. Loss can be expected in areas affected directly and indirectly by the storm.

The devastation is expected to be extraordinary. For example, the last time a hurricane of this expected magnitude hit the U.S., the ***National Hurricane Center estimated*** that property damage alone exceeded \$20 billion.

Structural damage will run the gamut: water damage caused by storm surge, floodwaters or wind-driven rain; broken windows and damaged or missing roofs caused by wind or debris; and in many instances, total destruction of property caused by storm surge, floodwaters or the storm's 111-plus mile per hour winds.

These physical losses will, in turn, result in business interruptions and, consequently, lost earnings. Damage and destruction to property will in many cases lead to losses in business revenue and event cancellations. Damage to supply chains, vendors, customers and markets may lead to production slowdowns and delays. And damage to physical property may lead to increased building costs due to continually evolving building codes.

With damage and lost income estimates running into the billions, insurance policyholders should review their policies to determine whether or not their losses will be covered.

Types of weather-related losses which insurance may cover

Different businesses may be affected differently by the same storm and even the same physical damage. For instance, a physical loss to a part supplier caused by flooding or a lost roof might impact that business as a physical property loss and as a consequential loss of business income. That same event might also indirectly impact a product manufacturer that relies on the part supplier for components in its product.

Likewise, the event might also affect a supplier of raw materials used by the

part 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 is a resource to pay for these losses. Today's commercial property policies often contain a number of specialized coverages. 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 or scheduled in the policy and may include not only buildings but also equipment and business personal property such as furniture, machinery and stock.
- *Wind versus flood:* Many property policies contain substantially reduced sublimits, or exclusions, for flood damage. Commercial property policies in coastal regions may also exclude windstorm or provide a sublimit applicable to windstorm damage. Some businesses may have separate windstorm-specific policies that complement their commercial property insurance. Thus, it is important that policyholders carefully examine the "cause" of their losses and evaluate whether there are multiple causes before submitting a claim.
- *Debris removal:* Many commercial property policies provide coverage for the costs incurred in the removal of debris of covered property damaged by an insured peril, such as windstorm. The maximum policy benefit for this coverage is usually expressed as a percentage of the total loss.
- *Water damage caused by burst pipes and water mains:* In general, water damage from a burst pipe inside a business will be covered. If an outside pipe or main bursts and causes damage, it also should be covered. But it may be necessary to demonstrate that the damage did indeed result from the burst pipe. If the insurer concludes that poor drainage—which is often a noncovered maintenance problem—caused the break or resulting damage, coverage may be denied. A claim also might be denied if policyholder negligence, such as leaving a vacant building without heat, caused the break. Further, even if the insurer does pay for the water damage, it may refuse to pay to repair the pipe itself, contending that the pipe was damaged by "wear and tear," which is often an excluded peril.
- *Expenses incurred attempting to mitigate or stop the damage:* Property policies typically cover expenses incurred in taking preventative measures to avoid loss or, where some loss has already occurred, further loss. In fact, many policies say the policyholder must take steps to safeguard the property and prevent further damage. A failure to do so could jeopardize coverage.
- *Extra expense coverage:* Repairing or replacing damaged property is not the only expense item 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 policyholder 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:* This insurance is designed to cover lost income and profits resulting from the suspension of operations due to covered property damage. This would also include operating expenses that must be paid even if the business is not operational. Typically, this coverage does not apply until the expiration of a "waiting period" designated in the policy—typically 72 hours after the property damage occurs.
- *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 and 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.

The precise terms of the insurance 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, and government action exclusions that may not permit recovery for interruptions in business where government authorities limit access.

The burden is always upon 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.

Policyholders are always best served by a careful analysis of the terms of their policies and the controlling law governing their insurer's obligations, as well as a precise documentation and presentation of their loss during the claim process.

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