

## Some Carriers Require Complete Cessation of Operations

# Business Is Interrupted, But Coverage Doesn't Apply

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How would you feel if you placed business-interruption insurance for a client only to find that the insurer with which you placed the coverage denied a claim for a multimillion-dollar business-interruption loss because only a portion of the insured's operations was interrupted?

Would it make you feel better to know that other insurers would have provided coverage for such a loss under the same language that existed in the policy you placed? Believe it or not, some insurers are interpreting the same form of business-interruption coverage in dramatically different ways that can have disastrous results for your clients.

The potentially problematic policy language that quietly has been the subject of several coverage disputes throughout the United States is likely the most commonly used form of business-interruption coverage. The language says that coverage is provided for losses sustained by the "necessary interruption of business."

However, some business-interruption policies are worded differently. Some say they provide coverage for losses sustained by "impairment of operations." Others say they provide coverage for "total or partial necessary interruption of business."

"Impairment"? "Total or partial interruption"? What are the insurers using these forms getting at with such language? Well, it could be that they are reacting to how some carriers interpret the phrase "necessary interruption of business."

Some insurers selling policies using such language argue that in order for an insured to be entitled to any business-interruption coverage, the covered peril at issue must cause a complete cessation of all operations at the insured location.

### **Partial Vs. Total Interruption**

Assume, for example, that the insured's building houses 10 machines that produce widgets, and a fire destroys five of the machines but does not harm the other five, all of which are able to and continue to produce widgets. The insured would perceive the fire as causing a business-interruption loss because its manufacturing capacity is reduced by half during the time it takes to repair or replace the damaged machines.

However, some insurers would interpret the phrase "necessary interruption of business" as not covering this loss because the policyholder's entire operations at the insured location did not cease.

You might be thinking to yourself, I've been placing business-interruption coverage for years (perhaps even decades), and I've never heard of any insurer interpreting its coverage form in such a restrictive manner.

Unfortunately, I am here to tell you that some insurers are, indeed, interpreting the policies in such a manner. I also can tell you that some courts have held that a business-interruption policy using the phrase "total or partial suspension" or "total or partial interruption" provides broader coverage than a policy that uses the phrase "necessary interruption."

I think the best way of avoiding these situations is to place business-interruption coverage that uses language such as "impairment of operations," "total or partial suspension," "total or partial interruption," or words to a similar effect, instead of a policy that refers to "necessary interruption of business." However, such language is not found in many policies, and the carrier with which you can place the coverage might not be willing to amend its policy language.

Nevertheless, there still are measures you can take even when the policy you are placing uses the phrase "necessary interruption of business."

First, discuss this issue with the underwriter. Explain the problem created by certain insurers in the market that have interpreted the phrase "necessary interruption of business" in a narrow way all the way into court. Have the underwriter confirm in writing, or you confirm to the underwriter in writing, that the underwriter does not interpret the phrase "necessary interruption of business" as providing any different coverage than does the phrase "total or partial necessary interruption of business."

Or have the underwriter confirm in writing, or you confirm to the underwriter in writing, that the underwriter does not interpret the phrase "necessary interruption of business" as requiring a total shutdown of the insured's operations in order for business-interruption coverage to be triggered.

In other words, confirm that a partial shutdown of operations or impairment

of operations can trigger coverage under the policy.

### **Papering the File**

Second, if the underwriter is not willing to confirm such an interpretation in writing, and you cannot place the coverage with any other insurer, you can try to "paper the file" with your client's understanding of the language. In the event of a coverage dispute, a court might look at such a record as evidence of how the insurer understood the insured to interpret the language and apply that understanding. This is not, however, a full-proof solution because not all courts use this rule of insurance-contract construction.

Accordingly, you should discuss this issue with your client and advise that this likely is the best that can be done for now, but that you will continue to look for alternatives during the policy period and try to address the issue again at renewal. When you market the program for renewal, if you find another insurer that is willing to address this issue, you should try to force the incumbent insurer to address the issue as well, or consider moving the program.

There are a host of issues to consider when placing business-interruption insurance, including addressing coverage for interdependent and contingent operations, ensuring that the period of indemnity provided for in the policy is adequate, and checking whether the up-and-coming risks associated with the insured's reliance on computers are covered. Those issues and others will be discussed in future ERRORS & OMISSIONS columns.

For this column, the first in a series that will discuss issues to consider when placing first-party property and time-element coverage, I wanted to address what I perceive is the biggest threat to an insured's expectations under business-interruption coverage. I urge you to take this issue seriously and make sure you are aware of it when placing your client's coverage.

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