

Human Hurricanes

Why Insurers May Treat Riot Claims Different Than Pandemic Claims

The news was bad in the spring of 2020, and then it got worse.

As everyone knows, bars, restaurants, retail stores, service businesses, and other establishments across the U.S. were shut down starting in March 2020 due to government orders issued in response to the Covid-19 pandemic.

Commercial property insurance policyholders soon learned that, in most cases, their “business interruption” (BI) insurance did not pay out for the interruption caused by the coronavirus. This was because contamination by a virus did not constitute the physical damage needed to trigger “BI” coverage, and/or because losses due to viruses were explicitly excluded from coverage.

The country was slowly but steadily reopening when on Memorial Day weekend the tragic death of George Floyd occurred in Minneapolis, precipitating more



than a week of protests and rioting across the country. The damage from the turmoil was extensive, and the collective disturbance was declared a catastrophe by Property Claim Services, a subsidiary of the Insurance Services Office (ISO) that designates events as catastrophes for purposes of reporting insurance losses.

No one would hope for a confluence of such dreadful events. But the riot damage had the ironic effect of triggering business interruption coverage for some business owners who were unable to claim it earlier in the pandemic. Some explanation is in order.

Clarifying terms

The events of 2020 have made almost everyone in American commerce aware of commercial property insurance provisions previously known only by specialists and individuals who had experienced a claim. “Business interruption” insurance is more commonly



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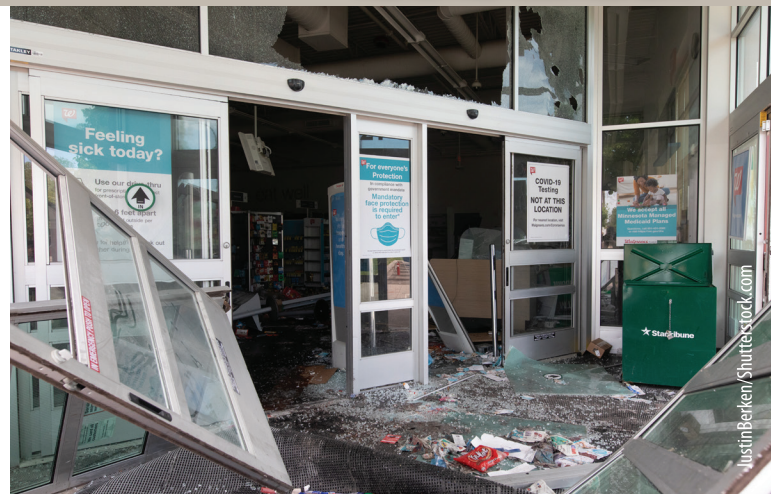
known as “business income” coverage among insurance professionals. Both terms, sharing the same initials, are used as shorthand for indicating coverage for two types of losses:

1. loss of revenue during the period when an operation is completely or partially suspended; and
2. extra expenses incurred to get the operation back up to full capacity.



While media reports may refer to business interruption “policies,” BI coverage is most often provided as an “endorsement,” or “coverage part,” added to a commercial property insurance policy. BI coverage is also built into most “businessowners,” or “BOP,” policies that provide property and liability insurance for small businesses in a single policy.

To understand why insurance companies are taking a different coverage position to affected businesses for



losses due to the pandemic than losses in the wake of civil disturbances, one needs to understand the idea of a “covered cause of loss,” also known as a “peril insured against.”

As its name suggests, a “named perils” property insurance policy provides coverage for losses due to the causes of loss (“perils”) specifically identified (named) in the policy. Named perils policies can be identified as “basic,” “broad,” or some other name, depending on the number and range of perils covered.

As a contrast, an “open perils” policy (called a “special” form by insurers) covers any type of loss to property except for causes explicitly excluded from coverage. Flood, earthquake, and war are among the commonly excluded causes of loss.

Necessary conditions

For BI coverage to be triggered, several conditions are almost always required:

- There must be “direct physical loss or damage” to property at an insured location;
- The loss or damage must have been caused by a covered cause or loss; and
- The loss or damage must be the reason for the suspension of operations.

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In the case of the coronavirus, insurers have taken the position that infection by a virus does not constitute direct damage to property. Moreover, since the “SARS” virus outbreak of the early 2000s, property insurers have implemented provisions explicitly excluding coverage for losses arising from viruses.

As this is written in June 2020, insurers’ positions are being challenged in federal and state courts, especially since public authorities ordered businesses to close as the pandemic first flared in the U.S. Claimants argue that BI insurance is supposed to respond when civil authorities close off an area. That’s generally true, but only if the order results from damage to a property (not necessarily the insured’s property) caused by a peril covered under the insured’s policy.

Again, the presence of a virus, or of an order prompted by a virus, did not qualify, according to insurers. It should be noted that claims professionals, attorneys and government entities are all actively challenging this position.

Rampage coverage

When communities erupted in anger and anguish in late May and early June of 2020, observers went to great pains to distinguish between peaceful



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demonstrators and those who violently attacked property.

That’s not necessary for insurance purposes, however, as losses due to “riot and civil commotion,” as well as vandalism and burglary, are covered under nearly all commercial property insurance policies, including BOPs. Those four terms, along with fire, are listed as covered causes of loss in a “broad” named perils form, and not excluded (hence covered) in a “special” (open) perils forms.

Because damage from fire, burglary, vandalism, riots, and civil commotion is typically covered, BI coverage is usually triggered during a suspension of operations due to such losses (presuming BI coverage has been purchased). Even if an insured has not sustained damage itself, it would be eligible for BI coverage if civil authorities order a shut down because of such damage at another location.

None of this is to suggest that recovery from the 2020 disturbances will be simple. In addition to the particular factors to a claim, policyholders and insurance claim adjusters will face this central question:

What will be the basis for determining what insureds recover for business income loss? Will it be the amount



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of revenue they typically earn in the weeks following Memorial Day, the amount they were earning during the pandemic shutdown, or the amount they anticipated receiving as they reopened?

Not an enviable task.

Those “human hurricanes”

So, why is a suspension due to a riot damage covered, but not a suspension due to a pandemic? After all, the victimized owner of a property or business was not at fault in either case?

The title of this piece is “human hurricanes,” and it will help readers to understand how riots are similar to windstorms, whose damages are covered under property policies, but different in nature from pandemics, which insurers consider to be “uninsurable.”

Like windstorms, riots arise occasionally and randomly, and strike a geographic area. The 2020 disturbances can be compared to a series of tornadoes during a season. The devastation can be great but is usually localized.

Also, like windstorms, riots will leave behind a mix of partial and total losses to property, mostly the former.

Some properties will be burned to the ground during a riot, and some victims will be traumatized by being targeted, but most property owners will clear the debris, replace broken windows, equipment, and merchandise, and resume operations once circumstances permit. If they have BI insurance, it may, for a time, pay the difference between a lower level of earnings after the riot and what it would normally have earned.



To clarify further, riots and hurricanes, which are deemed to be insurable, are very different than earthquakes and floods, which are considered uninsurable, for the most part. Floods and earthquakes wreak devastation on vast numbers of properties and require long periods of restoration to allow waters to recede, properties to be dried out, and major structural repairs to be undertaken.

In all of these examples, however, property owners and businesses can take steps before and after an event to limit the amount of loss and reduce the time needed to get back in operation. To ensure that commercial accounts have incentive to take such steps, commercial property policies will impose deductibles and may include “warranties” (loss control measures the insured must implement and maintain). The deductibles can be based on dollars or on time.

None of these steps are possible regarding a pandemic, during which a pathogen circulates in a manner almost entirely outside the control of a business and its insurer. For that reason, insurance trade associations are supporting a public approach to addressing pandemics that is not linked to private insurance policies.

We’ll see where that leads.