Order Code RS21158
Updated June 14, 2002

September 11 Insurance Litigation

Christopher Alan Jennings
Legislative Attorney
American Law Division

Summary

Insurance litigation arising out of the events of September 11 is already underway. Disputes involve claims for losses ranging from several thousand dollars to the billions. While some claims are involved in litigation, many are being resolved through alternative forms of dispute resolution. How much litigation will arise from September 11 remains unclear. At least two lawsuits deal with business interruption claims. Another cluster of suits involves the World Trade Center itself; the legal issues underpinning these cases will settle whether insurance companies owe $3.54 or $7.08 billion in coverage. This report summarizes these cases and will be updated.

While Congress responds to the wide spread exclusion of terrorism risks from insurance coverage through "The Terrorism Protection Act," H.R. 3210, placed on the Senate Legislative Calender on December 3, 2001, and "The Terrorism Risk Insurance Act," S. 2600, laid before the Senate by unanimous consent on June 13, 2002, the courts are responding to disputed insurance claims arising out the events of September 11.

Business Interruption. Business interruption insurance covers loss of income resulting from the suspension of business operations. While property insurance pays for damage to property, it does not pay for consequential damages stemming from that loss. For example, if a candy store burns down the week of Valentines Day, its property insurance will cover damage to inventory, equipment, display cases, and other insured items, but it will not cover the loss of business income suffered as a result of ceasing operations during a time when candy is in high demand. However, business interruption insurance could potentially cover those losses. While the purpose and function of business interruption insurance are straightforward, the technical issues raised by interpreting the policies are complex. These complexities make it difficult to generalize, in the abstract, about the scope of business interruption coverage and to determine whether, in particular cases, an event is an insurable event and whether a loss triggers coverage.

730 Bienville Patner Ltd. v. Assurance Co. of America is a case before the Louisiana Civil District Court of New Orleans. Case No. 2001-19830 (filed Dec. 3, 2001). The case involves a claim for $203,000 in business interruption losses suffered by two New Orleans hotels as a result of the federal government shutting down the nation's airports.

The insurance company denied coverage on the grounds that the hotel sustained no physical damage. The insured alleges, on the other hand, that it specifically purchased the policy to cover losses that resulted from happenings off site. As of June 3, this case has not been dismissed, nor set for trial.

Zurich American Insurance Co. v. ABM Industries Inc. involves a motion for declaratory judgement. No. 01-Civ.-1246 (S.D.N.Y. filed December 12, 2001). ABM Industries provided business services to clients at 1, 2, 3, 4, 5 and 7 World Trade Center, as well as other buildings in lower Manhattan. It filed a claim in excess of $10 million for its business interruption losses. In its petition for relief, Zurich maintains that its exposure under the policy is capped at $10 million. On February 28, 2002, this case was settled.

Coverage on the WTC Towers: World Trade Center Properties v. Travelers Indemnity. The primary issue involved in this cluster of cases concerns the meaning of the term "occurrence" as used in property insurance contracts covering the World Trade Center. When underwriting a risk, insurance companies generally budget for worst-case-scenario calamities. Reflecting this budget, property and casualty insurance contracts set the maximum sum insurers are obligated to pay per insurable event. Contracts tend to specify the limit as a cap "per event or occurrence." The insurance contracts covering the 99-year leaseholds on the World Trade Center Towers and buildings 4 and 5 cap exposure at approximately $3.54 billion dollars per insurable event.[1] At least $3.54 billion will be paid out under these contracts. Whether an additional $3.54 billion should be paid is the subject of this litigation.

Whether the events of September 11 should be construed as one event, or two is far from certain. Part of the problem is that WTC Properties – the policy holder – took control of the WTC in July, but at that time the insurance policies had not been finalized. Though WTC Properties and the insurance companies had agreed on basic terms, they were still negotiating over details on September 11. It is not clear what language will control the cases – it may be that different contract language will be applied to different insurance carriers.

The insured and the insurers interpret the events of September 11 very differently. For the insured, two events caused its losses: two separate airliners separately crashed into each of the Twin Towers some eighteen minutes apart. They assert that these acts resulted in separate fires that caused the separate collapse of each Tower and the subsequent damage to buildings 4 and 5. For the insurers, one event caused the losses: the attack constituted the execution of a plan to destroy an internationally recognized symbol of Western and American culture – using a common methodology, two groups acting under a unified purpose and intent carried out their objective in a relatively short period of time.

---

[1] Twenty-five insurance companies participate in a single program of property insurance for the WTC. The name of the insurers and the extent of their participation in the insurance scheme covering the WTC is detailed in the Appendix A. Major life, property and casualty companies handling claims covering loses associated with the WTC are listed in Appendix B.

If alternative forms of dispute resolution fail,[2] contract law will settle the dispute. Under New York law, an insurance policy is a contract that the court will construe in light of the mutual intent of the parties.[3] The courts strive to ascertain the actual intent of the parties. To do this, courts will first interpret the contract's plain language and then consider extrinsic evidence (e.g., market norms and negotiation history). If these methods do not work, that is, if the contract's language remains ambiguous, the courts will construe the contract in a way that would be consistent with the reasonable expectations of the insured at the time of contract.[4] If this method does not work, then the clause is generally construed against the party responsible for the imprecise language.

Though WTC Properties and its insurers agreed to a "per occurrence" cap on insurer liability as a basic term, they had not agreed, by September 11, on its precise meaning. If a court finds the plain language of the "per occurrence" clause ambiguous, it will consider whether extrinsic evidence resolves what the parties meant by that clause. Some WTC insurers, like Swiss Re, have offered extrinsic evidence as to what the parties intended by the term "occurrence." In their October petition for declaratory relief, Swiss Re asserts that the term "occurrence" was understood to mean:

> . . . all losses or damages that are attributable directly or indirectly to one cause or to one series of similar causes. All such losses will be added together and the total amount of such losses will be treated as one occurrence irrespective of the period of time or area over which such losses occur.[5]

Under this definition, the events of September 11 appear to constitute "one event or occurrence." However, whether this understanding accurately describes the *mutual* understanding of the parties is far from certain.

If resort to extrinsic evidence does not resolve the ambiguity, the courts will turn to default tests found in precedent. A variety of tests aid courts when construing ambiguous "per occurrence" clauses.[6] These tests include the "cause test," the "effects test," and the "unfortunate event test."[7] The "cause test," which is the majority rule, holds that multiple injuries arising *directly* from one action or event are treated as one "occurrence," regardless of the number of injuries or harms that arise from that action or event. Under this test, the court focuses on the underlying circumstances behind the claims, rather than the claims in themselves. The cause test tends to minimize the finding of "multiple occurrences." The "effects test," which is a minority rule, looks at the individual claims or individual damage to property to determine the number of "occurrences." This test tends to maximize the number of "occurrences" found.

---

[2] E.g., arbitration and negotiation.

[3] See, e.g., *Marino v. New York Telephone Co.*, 944 F.2d 109 (2d Cir. 1991).

[4] See *Haber v. St. Paul Guardian Ins.* Co., 137 F.3d 691, 697 (2d Cir. 1998).

[5] See *SR International Business Insurance Co., Ltd v. World Trade Center Properties LLC*, No. 01-CV-9291, ¶ 31 (S.D.N.Y., filed October 22, 2001).

[6] See *Uniroyal v. The Home Insurance Company*, 707 F. Supp. 1368, 1380 (2d Cir 1988).

[7] See, Ostrager, INSURANCE, EXCESS, AND REINSURANCE COVERAGE DISPUTES 133, 140-156 (1988).

New York has adopted the "unfortunate event" test – another minority rule – but has not defined what constitutes such an event.[8] Instead, New York courts resolve the question by adopting the "average man" aphorism, asking whether an average person in the shoes of the insured would regard the event as "unfortunate." The number of "unfortunate" events an "average man" would identify corresponds to the number of *insurable* events under the test.

Under the test, the court examines a set of interrelated events and surrounding circumstances leading up to the happening of the insurable event(s). Though the approach is not entirely clear, it does appear to fall in between the "cause" test and the effects "test," neither minimizing nor maximizing the number of insurable events covered by a general "per occurrence" clause.

While the test does not provide clear guidance, its use in prior cases suggests what an "unfortunate event" is not. It is not the "injury to the victim," nor is it the "negligent act or omission" giving rise to the loss.[9] In this regard, WTC Properties would not appear to be able to characterize the events of September 11 as multiple, discrete "occurrences" by counting the number of its injuries (e.g., "two towers collapsing equals two insurable events"). Nor, would the number of "occurrences" multiply by counting the number of wrongful or negligent acts (e.g., "two highjackings equals two insurable events").

If the unfortunate event test proves ineffective in resolving the WTC claims, the court would likely, as a last resort, strictly construe the ambiguity against the party responsible for it, which is generally the insurer.[10] However, this canon of construction assumes that the insured did not play an active role in negotiating the terms of the contract, which, in the case of WTC Properties, may not be a safe assumption. To avoid this canon, insurance companies will have to "prepare a good factual case on negotiation, economic duress, drafting, and who proffered the contested wording."[11]

Current situation. On February 16, Larry Silverstein, head of WTC Properties, announced a settlement with two major Bermuda-based insurers. Ace Bermuda and XL Insurance agreed to pay $298 million and $67 million respectively, which, incidently, is the full amount of coverage those companies owed for a singe disaster (see appendix A).[12] On January 9, WTC Properties sought summary judgement against Travelers Indemnity

---

[8] See *Arthur Johnson Corp v. Indemnity Insurance Company* 164 N.E.2d 704 (N.Y. 1959)(adopted the "unfortunate event" test for construing ambiguous uses of "accident.") See also, *Hartford Accident and Indemnity Company v. Wesolowski* 305 N.E.2d 907 (N.Y. 1973)(finding no material difference between the use of "occurrence" and "accident" in an insurance contracts before the court.).

[9] *Uniroya*l, 707 F. Supp at 1382, *citing Arthur Johnson*, 164 N.E.2d at 706 *and Wesolowski*, 305 N.E.2d at 912.

[10] See *Breed v. Insurance Co. of North America*, 385 N.E.2d 1280 (N.Y. 1978)("Well-recognized is the general rule that ambiguities in an insurance policy are to be construed against the insurer.")

[11] Graydon Staring, LAW OF REINSURANCE §13:2 (1993).

[12] See, Jonathan Glater, *Holder of Trade Center Lease Settles with Two Insurers*, THE NEW YORK TIMES, B-3 (Feb. 16, 2002). Their contracts reportedly defined "occurrence" to include all losses attributable "directly or indirectly to one series of similar causes."

Co. and other insurance companies on the number of occurrences involved in the terrorist attack.[13] On June 3, the court ruled that the term "occurrence" as contemplated by the parties negotiating coverage for the twin towers was ambiguous, and that extrinsic evidence must be considered before deciding how much WTC Properties should be compensated for the destruction. This ruling paves the way for a jury trial on the issue.

[13] See, *World Trade Center Properties LLC et al. v. Travelers Indemnity Co., et. al.*, No. 01 cv 12738 (S.D.N.Y., filed Jan. 9, 2002). In response, insurers argue that not only did the events constitute one occurrence, but that they will try to prove that the second tower would have collapsed or would have been rendered uninhabitable if only one plane had hit the World Trade Center complex.

Appendix A: Insurance Carrier Coverage for Leaseholds on the WTC Towers and Buildings 3 and 4*

Carrier	Maximum Payout Per Occurrence (in U.S. dollars)	% of total (Appx.)	Primary	Layer 2	Layer 3	Layer 4	Layer 5	Layer 6	Layer 7	Layer 8	Layer 9	Layer 10	Layer 11	Layer 12
Swiss Re	$778,096,000	22%		**$8,800,000**	**$5,500,000**	**$11,000,000**	**$27,500,000**	**$55,000,000**	**$110,000,000**	**$110,000,000**	**$218,460,000**	**$168,740,000**	**$21,611,765**	**$41,484,235**
Lloyds	$667,840,483	19%							**$312,500,000**	**$92,000,000**		**$151,144,483**		**$112,196,000**
Allianz (Scor)	$354,680,001	10%	**$1,000,000**	**$4,000,000**	**$2,500,000**	**$5,000,000**	**$12,500,000**	**$25,000,000**	**$50,000,000**	**$50,000,000**	**$99,300,000**	**$76,700,000**	**$9,823,530**	**$18,856,471**
Ace	$298,000,000	9%								**$248,000,000**	**$50,000,000**			
Chubb	$254,307,300	7%									**$254,307,300**			
IRI	$237,238,000	7%									**$237,238,000**			
Travelers	$210,620,990	6%	**$800,000**		**$6,075,949**		**$50,000,000**	**$60,000,000**				**$93,745,041**		
Royal Indemnity	$178,204,081	5%	**$800,000**	**$2,000,000**							**$50,404,557**	**$124,999,524**		
Swiss Re UK	$99,407,000	3%									**$83,300,000**	**$16,107,000**		
Allianz	$77,898,734	2%			**$7,898,734**			**$70,000,000**						
XL	$66,799,999	2%											**$66,799,999**	
Gulf	$65,000,000	2%										**$65,000,000**		
Liberty Mutual	$64,894,000	2%	**$2,000,000**									**$62,894,000**		
Zurich US	$45,670,000	1%		**$8,000,000**			**$30,000,000**					**$7,670,000**		
Great Lakes	$38,000,000	1%			**$1,000,000**	**$2,000,000**	**$5,000,000**	**$10,000,000**	**$20,000,000**					
Hartford	$32,000,000	<1%				**$32,000,000**								
St. Paul	$30,000,000	<1%						**$30,000,000**						
Wurt	$16,028,000	<1%												**$16,028,000**
TIG	$9,100,000	<1%		**$9,100,000**										
QBE	$7,500,000	<1%							**$7,500,000**					
Lexington	$5,000,000	<1%	**$5,000,000**											
COP Re	$4,000,000	<1%		**$4,000,000**										
Twin City	$2,500,000	<1%		**$2,500,000**										
Houston	$2,425,316	<1%	**$400,000**		**$2,025,316**									
Tokio Marine	$1,600,000	<1%		**$1,600,000**										
TOTAL	**$3,546,809,904**	~100%	**$10,000,000**	*$40,000,000*	**$24,999,999**	*$50,000,000*	**$125,000,000**	*$250,000,000*	**$500,000,000**	*$500,000,000*	**$993,009,857**	*$767,000,048*	**$98,235,294**	*$188,564,706*

* Compiled from court documents filed by World Trade Center Properties, Ace, Swiss Re, XL, and Allianz with the United States District Court for the Southern District of New York.

Explanation: Insurance companies participating in the primary layer provide the initial $10 million in coverage per occurrence, with WTC Properties paying a $1 million deductible per occurrence. When a particular loss exceeds $10 million, those insurance companies participating in the second layer of coverage provide excess coverage up to a set limit per occurrence for that layer. As losses per occurrence increase, different layers of coverage trigger different payments by participating insurers. This process proceeds through 12 layers of coverage. Adding the 12 layers of coverage together yields the maximum cap, $3.546 billion per occurrence.

Example: Assume a storm hit lower Manhattan damaging the WTC, causing $9 million in losses covered by the property and casualty insurance policy. Only those insurance companies participating in the primary layer of coverage would be obligated to pay a proportionate share of the $9 million. Swiss Re, which covers 22% of the losses when a claim proceeds through all 12 layers of coverage, pays nothing because it does not participate in the primary layer of coverage. While Lexington, which provides .15% of aggregate coverage, pays $4.5 million or 50% of the claim.