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A Look Back at Insurance Law in 2008: New York's Highest Court Confirms that Insurance Companies are Liable for Consequential Damages Just Like Anyone Else

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As insurance lawyers and public adjusters look back on 2008, one of the most significant developments was the New York State Court of Appeals' decision in *Bi-Economy Market, Inc. v. Harleysville Ins. Co. of New York,* 10 N.Y.3d 187 (2008). This article reviews the *Bi-Economy* claim and litigation and discusses how this landmark decision should make the playing field more level for policyholders and improve the way that insurance claims are handled in New York State.

Historically, insurance companies subjected New York policyholders who suffered consequential damages when the insurance company breached its duties under an insurance contract to a different set of rules compared to the victims of any other sort of contractual breach. Whereas breach of a typical contract generally entitles the victim to recover damages flowing from the breach (i.e., consequential damages), insurance companies sought to limit a policyholder's claim to the losses covered under the terms of the insurance contract (i.e., contractual damages). Moreover, because New York law generally makes it difficult for a policyholder to obtain an award for punitive damages against an insurance company that acts in bad faith when adjusting that policyholder's claim (unless such bad faith also harmed the wider marketplace), insurance companies guilty of bad faith claims handling generally have been insulated from the adverse consequences (i.e., judgments in excess of policy limits) they face in other states. Thus, even in cases where the insurance company caused extensive harm to a policyholder through egregious claims handling practices, the policyholder's recovery generally would be limited to the terms, including the policy limits, of the insurance contract.

The status quo came into question before New York State's highest court in 2008. The result, in a pair of cases decided the same day in February, is new and important law holding that an insurance company can be liable for consequential damages, in excess of policy limits, caused by the insurance company's bad faith breach of contract. *See Bi-Economy Market, Inc. v. Harleysville Ins. Co. of New York,* 10 N.Y.3d 187 (2008); *Panasia Estates, Inc. v. Hudson Ins. Co.*, 10 N.Y.3d 200 (2008).

The Claims Adjusting

The Bi-Economy saga began when the insured premises, a local grocery store and meat market, was heavily damaged by fire. The policyholder

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who's who

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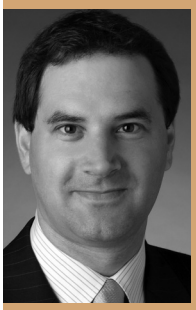

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reached out to National Fire Adjustment Co., Inc. as their Public Adjusters—who discovered that the insurance company's offer of the building damages was woefully inadequate. They demanded an appraisal according to the terms of the insurance policy. The appraisal award came in at more than double the insurance company's offer, but the insurance company then refused to pay for the down time the business sustained during the unreasonable delays throughout the adjustment process. Ultimately, the insurance company's refusal to make a full and prompt payment of the policyholder's property and business interruption claim caused the policyholder's business to fail.

The Litigation

Forced out of business by the insurance company's unreasonable delays and measure of the fire loss, Bi-Economy was left with no choice but to seek redress in court. In deciding a motion for partial summary judgment brought by the insurance company, the trial court dismissed Bi-Economy's claim for consequential damages, and Bi-Economy appealed. After the intermediary appellate court affirmed the trial court's decision, Bi-Economy brought its case to the court of appeals. At risk of losing the benefit of New York's pro-insurance company law regarding consequential damages, the insurance industry—through the New York Insurance Association, National Association of Mutual Insurance Companies, American Insurance Association, and Property Casualty Insurers Association of America—submitted supplemental briefs to the court of appeals in addition to the arguments made by Bi-Economy's insurance company. On the other side, Anderson Kill & Olick filed a brief in support of Bi-Economy's position on behalf of a not for profit group—United Policyholders—that acts as an advocate for consumers in the insurance marketplace The issue before the court was whether a policyholder can assert a claim for consequential damages where an insurance company's claims handling has caused that policyholder to suffer losses not otherwise covered by the insurance contract—including the failure of its entire business.

The Result

The court of appeals ruled that insurance companies that cause harm to their customers are treated just like everyone else—they are liable for the consequential damages they cause. Under the holding in *Bi-Economy,* consequential damages are recoverable based on a

traditional foreseeability analysis (*Bi-Economy*, 10 N.Y.3d at 192-93), and not only where the requirements for an award of punitive damages are met. The ruling further stated that under the foreseeability analysis, an insurance company is liable "for those risks foreseen or which should have been foreseen at the time the contract was made," looking to "the nature, purpose, and particular circumstances of the contract known by the parties." Thus, New York law now clearly recognizes that "limiting an insured's damages to the amount of the policy, i.e., money which should have been paid by the insurer in the first place, plus interest, does not place the insured in the position it would have been in had the contract been performed."Surprisingly, Florida's Law and Ordinance paper did not explain the nuance of this "at the time" of loss provision. Even more surprising is that Florida made significant code changes in 2005, yet no notice was sent to policyholders with an explanation of how those changes may affect homeowners still struggling to recover from the four 2004 CAT events.

The court of appeal's ruling was especially noteworthy for its reaffirmation of the core purpose of business interruption insurance: **The purpose served by business interruption coverage cannot be clearer—to ensure that Bi-Economy had the financial support necessary to sustain its business operation in the event disaster occurred.**[1] Certainly, many business policyholders, such as Bi-Economy, lack the resources to continue business operations without insurance proceeds. Accordingly, limiting an insured's damages to the amount of the policy, i.e., money which should have been paid by the insurer in the first place, plus interest, does not place the insured in the position it would have been in had the contract been performed.[2]

Thus, the very purpose of business interruption coverage would have made Harleysville aware that if it breached its obligations under the contract to investigate in good faith and pay covered claims it would have to respond in damages to Bi-Economy for the loss of its business as a result of the breach.[3]

Furthermore, contrary to the dissent's view, the purpose of the contract was not just to receive money, but to receive it promptly so that in the aftermath of a calamitous event, as Bi-Economy experienced here, the business could avoid collapse and get back on its feet as soon as possible. Thus, this insurance contract included an additional performance-based component: the insurer agreed to evaluate a claim, and to do so honestly, adequately, and—most importantly—promptly. The insurer certainly knew that failure to perform would undercut the very purpose of the agreement and cause additional damages that the policy was purchased to protect against in the first place. Here, the claim is that Harleysville failed to promptly adjust and pay the loss, resulting in the collapse of the business. When an insured in such a situation suffers additional damages as a result of an insurer's excessive delay or improper denial, the insurance company should stand liable for these damages. This is not to punish the insurer, but to give the insured its bargained-for benefit.[4]

Based on our respective experience as a public adjuster and a policyholder attorney, we see this as a very important case. In various claims handled over the years, the same adjusters working for the same insurance companies have tended to be much more responsible with regard to how they treat the policyholder in states where the insurance company would be subject to extra-contractual liability if the claim was not handled properly. Prior to *Bi-Economy*, if the case was in New York, the insurance company's adjuster often would be more brazen in its dealings with the policyholder, because he or she knew that the insurance company would never have to pay any more than what it owed in the beginning. The lack of an effective check on such behavior gave the unscrupulous adjuster or insurance company cause for arrogance and delay.

Although the ruling in Bi-Economy is a quantum leap towards making the claims adjusting process more fair for policyholders in New York, it does not negate the need for punitive damage legislation that would hold unscrupulous insurance companies accountable for their unreasonable actions against less sophisticated and less well-funded "opponents"—their own policyholders. That said, a quantum leap is a quantum leap, and it is our hope that Bi-Economy helps policyholders get the full benefit of the insurance coverage they pay for, and holds unscrupulous insurance companies accountable when they fail to deliver the coverage they owe and harm their customers in the process. ■

[1] *See* Howard Stores Corp. v. Foremost Ins. Co., 82 A.D.2d 398, 400, 441 N.Y.S.2d 674 (1st Dept. 1981) ("The purpose of business interruption insurance is to indemnify the insured

against losses arising from inability to continue normal business operation and functions due to the damage sustained as a result of the hazard insured against."), *aff'd*, 56 N.Y.2d 991, 453 N.Y.S.2d 682, 439 N.E.2d 397 (1982); 3-36 Bender's New York Insurance Law § 36.06.

[2] *See generally* Brushton-Moira Cent. Sch. Dist. v. Thomas Assoc., 91 N.Y.2d 256, 261, 669 N.Y.S.2d 520, 692 N.E.2d 551 (1998) ("Damages are intended to return the parties to the point at which the breach arose and to place the nonbreaching party in as good a position as it would have been had the contract been performed."); Goodstein Constr. Corp. v. City of New York, 80 N.Y.2d 366, 373, 590 N.Y.S.2d 425, 604 N.E.2d 1356 (1992), citing Restatement (Second) of Contracts § 347 cmt. a; § 344 ("Contract damages are ordinarily intended to give the injured party the benefit of the bargain by awarding a sum of money that will, to the extent possible, put that party in as good a position as it would have been in had the contract been performed.").

[3] See Sabbeth Indus. v. Pa. Lumbermens Mut. Ins. Co., 238 A.D.2d 767, 769, 656 N.Y.S.2d 475 (3d Dept. 1997).

[4] Id. at 194–95 (emphasis added).