

03-9064

In The
United States Court of Appeals
FOR THE SECOND CIRCUIT

DUANE READE, INC.,
Plaintiff-Counter-Defendant-Appellee,
-against-
ST. PAUL FIRE AND MARINE,
Defendant-Counterclaimant-Appellee.

ON APPEAL FROM THE UNITED STATES DISTRICT COURT
FOR THE SOUTHERN DISTRICT OF NEW YORK

**BRIEF OF AMICI CURIAE, UNITED POLICYHOLDERS,
IN SUPPORT OF THE PLAINTIFF-COUNTER-DEFENDANT-
APPELLEE'S PETITION FOR REHEARING**

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TABLE OF CONTENTS

<u>Section</u>	<u>Page</u>
I. This Court Erred in Finding That the Period of Restoration Provision in the Policy Is Not Tied to the Location of Duane Reade’s WTC store.....	1
A. Tying the Hypothetical Period of Restoration to the Original Location of the Operations of the Policyholder Is the Only Way to Protect the Earnings the Policyholder Would Have Enjoyed Had There Been No Catastrophe.....	1
B. An Insurance Company Tenant of the WTC Agreed with Duane Reade that the Original Location of a Policyholder’s Operations Is Critical To Determining the Period of Restoration.....	7
C. This Court’s Decision Conflicts with the Off-Stated Purpose of Business Income Coverage	9
II. Because the Leasehold Coverage Provision in the Duane Reade Policy is Extremely Broad, this Court’s Conclusions as to that Coverage Will Not Affect Most Policyholders	11

TABLE OF AUTHORITIES

<u>Cases</u>	<u>Page</u>
<u>American Alliance Ins. Co. v. Keleket X-Ray Corp.,</u> 248 F.2d 920, 928 (6 th Cir. 1957)	10
<u>American Auto. Ins. Co. v. Fisherman’s Paradise Boats, Inc.,</u> No. 93-2349, 1994 WL 1720238, at *2 (S.D. Fla. Oct. 3, 1994)	9
<u>Archer-Daniels-Midland Co. v. Phoenix Assurance Co.,</u> 975 F. Supp. 1124, 1127 (S.D. Ill. 1997) (applying Illinois law)	9
<u>Beautytuft, Inc. v. Factory Insurance Association</u>	1
<u>Dictiomatic, Inc. v. United States Fid. & Guar. Co.,</u> 127 F. Supp. 2d 1239, 1243 (S.D. Fla. 1999)	9
<u>Duane Reade Inc. v. St. Paul Fire & Marine Ins. Co.,</u> No. 03-9064, 2005 WL 1460641, at *9 (2d Cir. June 22, 2005)	5
<u>Fireman’s Fund Ins. Co. v. Holland Am. Line-Westours, Inc.,</u> No. 00-35059, 2002 WL 21924, at *1 (9 th Cir. Jan. 4, 2002) (noting the purpose of Business Income is to protect “the earnings of the insured would have enjoyed had their been no interruption”)	9
<u>Fireman’s Fund Ins. Co. v. Mitchell-Peterson, Inc.,</u> 578 N.E.2d 851, 855 (Ohio App. Ct. 1989)	9
<u>Keetch v. Mutual of Enumclaw Ins. Co.,</u> 831 P.2d 784, 786 (Wash. App. 1992)	10
<u>Linnton Plywood Ass’n v. Protection Mut. Ins. Co.,</u> 760 F. Supp. 170, 172 (D. Or. 1991) (applying Oregon law)	9
<u>Lumbermens Mut. Cas. Co. v. Factory Mut. Ins. Co.</u>	8
<u>Protection Mut. Ins. Co. v. Mitsubishi Silicon Am. Corp.,</u> 992 P.2d 479, 481 (Or. App. 1999)	10
<u>Prudential LMI Comm’l Ins. Co. v. Colleton Enters., Inc.,</u> 976 F.2d 727, 1992 WL 252507, at *2 (4 th Cir. 1992) (applying South Carolina law)	9
<u>Quality Molding Co. v. American Nat. Fire Ins. Co.,</u> 272 F.2d 779, 780 (7th Cir. 1959))	9

<u>Steel Products Co. v. Millers National Insurance Co.</u> 209 N.W.2d 32 (Iowa 1973)	2
<u>Streamline Capitol, L.L.C. v. Hartford Casualty Insurance Co.</u> No. 02 Civ. 8123, 2003 WL 22004888 (S.D.N.Y. Aug. 25, 2003).....	4, 5
<u>Zurich Am. Ins. Co. v. ABM Indus., Inc.</u> 397 F.3d 158 (2d Cir. 2005)	6

I. THIS COURT ERRED IN FINDING THAT THE PERIOD OF RESTORATION PROVISION IN THE POLICY IS NOT TIED TO THE LOCATION OF DUANE READE'S WTC STORE

A. Tying the Hypothetical Period of Restoration to the Original Location of the Operations of the Policyholder Is the Only Way to Protect the Earnings the Policyholder Would Have Enjoyed Had There Been No Catastrophe

For all businesses, location is important, and for some it is critical.

Historically, courts have found that the paramount importance of location interacts with the hypothetical Period of Restoration as follows: (1) if the policyholder relocates and restarts business at a different location, the hypothetical Period of Restoration is still applied and the policyholder receives any difference between projected earnings at the original location and actual earnings at the replacement location during the Period of Restoration; but (2) if the policyholder rebuilds at the original location prior to the end of the hypothetical Period of Restoration, the actual period of interruption is applied.

Accordingly, in Beautytuft, Inc. v. Factory Insurance Association,¹ the court agreed that “the contract language ‘such described property’ was [the policyholder’s] ‘real or personal property’” at the original location: “[a]lthough a substitute plant of potentially equivalent capacity was promptly

¹ 431 F.2d 1122 (6th Cir. 1970) (applying Georgia law).

obtained, [the policyholder's] actual losses as shown by the proofs continued beyond that date; and [the policyholder] [was] entitled to reimbursement for such losses for the term of the theoretical replacement period as provided by the contract."² Similarly, in Steel Products Co. v. Millers National Insurance Co.,³ the court recognized that the Period of Restoration was tied to the actual premises of the policyholder:

A business interruption policy provides use and occupancy coverage tied to the insured premises. It is the effect of interruption of such use and occupancy on gross earnings of the business which is insured. Interruption of use and occupancy continues from the date of damage to the date of substantial restoration of the insured premises. Where the premises are actually restored, the period for computation of reduced gross earnings ends with such restoration unless that period exceeds the theoretical period of repair. The theoretical period defined in the policy is the length of time required with the exercise of due diligence and dispatch to rebuild, repair or replace the damaged premises. Where the actual restoration period exceeds the theoretical period or where the premises are not restored, the theoretical period becomes the computation period. In the present case the period of business interruption is the time it actually took to restore the insured premises.⁴

² Id. at 1124.

³ 209 N.W.2d 32 (Iowa 1973).

⁴ Id. at 38.

This rule is a salutary one, and is most likely to compensate policyholders for their actual loss. For instance, if a policyholder is one for whom space is fungible, and who can relocate without adverse affect, its loss will disappear quickly and, although the insurance company is obligated to pay loss through the full Period of Restoration measured by the hypothetical rebuilding period for the original location, there will be little or no loss to pay at the tail end of that period. On the other hand, a policyholder for whom a particular space is critical may relocate and find its loss continues to be severe after relocation; its loss should continue to be covered throughout the full Period of Restoration measured by the time needed to rebuild the original location.

This Court's decision is a radical departure from this established rule. In short, this Court rejected the argument that the Period of Restoration was tied to operations at the site of the WTC store because the policy was sold on a blanket basis, covering all of the policyholder's stores without specifically identifying the location of any of those stores.⁵ Accordingly, if the policy at issue had listed the policyholder's WTC store this Court would, presumably, have affirmed the District Court. *Amicus Curiae* points out that

⁵ Duane Reade Inc. v. St. Paul Fire & Marine Ins. Co., No. 03-9064, 2005 WL 1460641, at *9 (2d Cir. June 22, 2005).

for policyholders such as that in Duane Reade – who have hundreds of stores – such listings in the body of the policy are either impossible or overly cumbersome particularly because insurers locations may change during the policy period; accordingly, the first-party policies they purchase identify a list of locations “on file with the company” in the Declarations. Nonetheless, specific locations can be as important for large companies with multiple locations as they can be for smaller companies with one location; indeed, the store at issue in Duane Reade was the highest grossing store in the chain. At the very least, whether the parties intended site specific coverage is an issue of bad faith that should not be decided against a policyholder when its locations are referenced in the policy, particularly since additional premium is typically paid for each location.

Next, this Court agreed with Streamline Capitol, L.L.C. v. Hartford Casualty Insurance Co.⁶ that “the business income coverage only applies to the suspension of the [the policyholder’s] ‘operations’ indicates that it is dependent only on replacing what is necessary to resume those operations – namely, the plaintiff’s personal property, not a specific office at a specific location”:

⁶ No. 02 Civ. 8123, 2003 WL 22004888 (S.D.N.Y. Aug. 25, 2003).

We agree with Judge Buchwald's reasoning and find it equally applicable to the present case. As in *Streamline*, the [insurance company] policy says nothing about the specific location of the interrupted business. It simply provides coverage until [the policyholder] can “repair, rebuild, or replace” the property that was damaged and resume operations. Also in line with *Streamline*, the damaged property is the property [the policyholder] had located in the premises it leased from the WTC.

Doubtless, if awaiting the rebuilding of the WTC and moving [the policyholder's] WTC store to a new location were roughly equivalent tasks, the BI coverage would extend to whichever task [the policyholder], in its discretion, chose to do. The rebuilding of the WTC, however, will be a herculean undertaking far exceeding the rebuilding of a [policyholder] store in an existing building, or even in an as-yet-to-be built Manhattan office building, and involving numerous and complex contingencies over which neither [the policyholder] nor [the insurance company] has any control. Under these circumstances, it would be entirely unreasonable to interpret the Restoration Period to include the time it would take for [the policyholder] to resume operations in a store located at its former site where that site was neither the subject of the insurance policy nor expressly provided for in the calculus set forth in the Restoration Period....⁷

There are a number of problems with this conclusion. First, Streamline indicated that its holding was limited to business “run out of office” – *i.e.*, for which space is essentially fungible – which would not apply to the

⁷ Id. at *10.

policyholder in Duane Reade.⁸ Second Streamline based its holding on the ABM District Court's very narrow construction of property which would support a Business Income claim,⁹ which this Court correctly reversed.¹⁰ Third, the Business Income provision of the policy in Duane Reade covered loss stemming from "direct physical loss or damage to any Real or Personal Property **whether insured or not** ... including but not limited to loss or damage to ... property of the Assured"¹¹ and the Period of Restoration was tied **not** to the time necessary to replace or repair "property of the Assured" but rather "such length of time as would be required with the exercise of due diligence and dispatch to rebuild, repair, or replace such property that has been destroyed or damaged."¹² Fourth, the Period of Restoration is a hypothetical period: accordingly, whether or not the policyholder or the insurance company have any "control" over the process is immaterial, as that will affect the **actual** period of reconstruction and not the **hypothetical** Period of Restoration. Fifth, finding the Period of

⁸ Streamline, 2003 WL 22004888, at *9.

⁹ Id.

¹⁰ Zurich Am. Ins. Co. v. ABM Indus., Inc., 397 F.3d 158 (2d Cir. 2005).

¹¹ 279 F. Supp. 2d at 237.

¹² Id.

Restoration tied to the length of time necessary to rebuild at the WTC accurately reflects the policyholder's loss: if it is able to recapture all of its business at a substitute location, then the insurance company's obligations reduce to nothing; if it cannot recapture such business, then this is a genuine exposure for which it paid premium.

B. An Insurance Company Tenant of the WTC Agreed with Duane Reade that the Original Location of a Policyholder's Operations Is Critical To Determining the Period of Restoration

At least one insurance company, which was a tenant of the WTC Complex – Lumbermen's Mutual Casualty Company – filed a complaint seeking coverage for its loss for the length of time necessary to rebuild the WTC. Like most tenants of the WTC Complex, Lumbermens had to relocate after September 11, 2001 during a chaotic real estate market, and ended up paying considerably higher rents than it had previously paid:

As a direct result of the total destruction of WTC 1, Lumbermens was forced to secure temporary leases for office space for many of its New York City employees in a suddenly chaotic real estate market. Lumbermens also moved employees that had been working at WTC 1 to other company office locations in New York and New Jersey, including Elmsford, New York, Melville, New York, Berkeley Heights, New Jersey and Princeton, New Jersey.

... Lumbermens entered into two separate leases for temporary locations in New York City and New Jersey. On or about October 24, 2001, Lumbermens executed a

lease for office space located at 30 Rockefeller Center in New York City (the "Rockefeller Center Lease"). On or about December 20, 2001, Lumbermens executed a lease for office space located at One Exchange Plaza in Jersey City, New Jersey (the "Exchange Plaza Lease").

... Lumbermens' execution of the above leases was an interim measure allowing Lumbermens to attempt to continue to conduct its business in New York City in the wake of the September 11, 2001 catastrophe. The office space secured by Lumbermens is not permanent replacement office space. Lumbermens intends to return to the permanent accommodations it previously enjoyed in lower Manhattan once the World Trade Center complex is rebuilt.¹³

Lumbermens sought its increased lease payments as Extra Expense¹⁴ and sought coverage for these Extra Expenses for the entire period needed to reconstruct the WTC Complex, requesting the court to declare "that the applicable Period of Liability for the Extra Expense coverage provided under the Policy for Lumbermens' loss started on September 11, 2001 and

¹³ Complaint, filed Sept. 10, 2002, in Lumbermens Mut. Cas. Co. v. Factory Mut. Ins. Co., No. 02C 6439 (N.D. Ill.), at 2-3.

¹⁴ Id. at 7 ("The payments Lumbermens has made and will be required to make in the future for temporary office space under the terms of the Rockefeller Center Lease and the Exchange Plaza Lease exceed by millions of dollars the payments that Lumbermens would have made for its permanent office space under the terms of its World Trade Center Lease. Lumbermens contends that the Extra Expense coverage provided in the Policy applies under the circumstances and provides Lumbermens with insurance coverage for these extra temporary office rental expenses.").

will end when with due diligence and dispatch the destroyed building could be replaced and made ready for Lumbermens' operations under the same or equivalent physical operating conditions as existed prior to the damage caused on September 11, 2001."¹⁵ This case has since settled.

C. This Court's Decision Conflicts with the Oft-Stated Purpose of Business Income Coverage

It is universally accepted that the purpose of Business Income coverage is to protect the earnings the business would have enjoyed had there been no catastrophe.¹⁶ Under this Court's decision, policyholders like

¹⁵ Id. at 9-10.

¹⁶ See, e.g., Fireman's Fund Ins. Co. v. Holland Am. Line-Westours, Inc., No. 00-35059, 2002 WL 21924, at *1 (9th Cir. Jan. 4, 2002) (noting the purpose of Business Income is to protect "the earnings of the insured would have enjoyed had their been no interruption"); Prudential LMI Comm'l Ins. Co. v. Colleton Enters., Inc., 976 F.2d 727, 1992 WL 252507, at *2 (4th Cir. 1992) (applying South Carolina law) ("Generally, business interruption insurance 'is designed to do for the insured in the event of business interruption caused by [an insured peril], just what the business itself would have done if no interruption had occurred – no more."); Dictiomatic, Inc. v. United States Fid. & Guar. Co., 127 F. Supp. 2d 1239, 1243 (S.D. Fla. 1999) ("It is also relevant to the resolution of the present motion for fees, that the applicable law is quite clear – business interruption insurance is intended to return to the insured's business the amount of profit it *would have earned* had there been no interruption of the business."); Archer-Daniels-Midland Co. v. Phoenix Assurance Co., 975 F. Supp. 1124, 1127 (S.D. Ill. 1997) (applying Illinois law) ("Business Interruption insurance is insurance under which the insured is protected in the *earnings* which the insured would have enjoyed had there been no interruption of business.") (quoting Quality Molding Co.

Duane Reade will not have protection for the earnings they would have enjoyed had there been no catastrophe; they will be entitled only to a much smaller subset of those earnings.

Indeed, the Duane Reade policy covers the policyholder for amounts it would have earned had not loss occurred, the calculation of that loss must necessarily be tied to the location of the original store. It would make

v. American Nat. Fire Ins. Co., 272 F.2d 779, 780 (7th Cir. 1959)); American Auto. Ins. Co. v. Fisherman's Paradise Boats, Inc., No. 93-2349, 1994 WL 1720238, at *2 (S.D. Fla. Oct. 3, 1994) ("Business interruption insurance or 'use and occupancy' insurance is designed to protect the earnings or profits that a business would have earned, had the event insured against not intervened."); Linnton Plywood Ass'n v. Protection Mut. Ins. Co., 760 F. Supp. 170, 172 (D. Or. 1991) (applying Oregon law) ("The nature of business interruption insurance is to indemnify the insured for any loss sustained because of the insured's inability to continue to use specified premises as a result of the destruction of the premises or parts thereof."); Fireman's Fund Ins. Co. v. Mitchell-Peterson, Inc., 578 N.E.2d 851, 855 (Ohio App. Ct. 1989) ("The purpose of a business interruption policy is to "do for the insured in event of a business interruption * * * just what the business itself would have done if not interruption had occurred.""") (quoting American Alliance Ins. Co. v. Keleket X-Ray Corp., 248 F.2d 920, 928 (6th Cir. 1957)); Protection Mut. Ins. Co. v. Mitsubishi Silicon Am. Corp., 992 P.2d 479, 481 (Or. App. 1999) ("In covering those consequential economic damages, so-called 'business interruption' insurance is 'designed to do for the business what the business would have done for itself had no loss occurred.'"); Keetch v. Mutual of Enumclaw Ins. Co., 831 P.2d 784, 786 (Wash. App. 1992) ("The essential nature and purpose of a business interruption policy is to protect the earnings which an insured would have enjoyed had there been no interruption of business.").

no sense to state that damages are to be computed based on expected earnings at one location, and then to cut off those earnings at a time when the policyholder could establish operations at an inferior location.

II. BECAUSE THE LEASEHOLD COVERAGE PROVISION IN THE DUANE READE POLICY IS EXTREMELY BROAD, THIS COURT'S CONCLUSIONS AS TO THAT COVERAGE WILL NOT AFFECT MOST POLICYHOLDERS

Unlike Duane Reade, most policyholders have Leasehold Coverage that is limited – by definition in the policy – to rents paid on damaged facilities or increased rents for replacement facilities, so they will get no benefit from this Court's holding on Leasehold Coverage.¹⁷ Indeed, this Court's decision opens a whole can of worms. For instance, because the coverage is tied to the length of the lease, under policies limiting Business Income coverage to a Maximum Period of Indemnity – typically, 12 months – can policyholders recover Actual Rental Value for the length of the lease if it is longer than twelve months? Second, if a policyholder's lease has only a short time left, but it can demonstrate that it would have been renewed – as the policyholder in Duane Reade did in a separate trial – is the policyholder nonetheless confined to recover Actual Rental Value for

¹⁷ See Stephen A. Cozen, Insuring Real Property, § 1.06[4][c] (2005) (“Leasehold interest coverage insured the benefit of the bargain that a tenant may have in its long-term lease. It takes effect when the actual rent being paid is less than market rents.”).

the period of its lease? Third, what if the lease is month to month? Fourth, perhaps most important, what if the policyholder owns its location?

Dated: July 13, 2005,

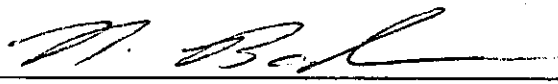
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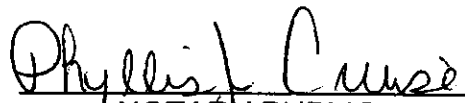
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I declare under penalty of perjury under the laws of the United States of America that the foregoing is true and correct.



Nicholas J. Balsdon

Sworn to before me this
13th day of July, 2005.



NOTARY PUBLIC

PHYLLIS J. CRUISE
NOTARY PUBLIC, State of New York
No. 01CR4904891
Qualified in Bronx County
Commission Expires Oct 5, 2005

