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Japan's earthquake could trigger contentious insurance disputes

Amanda Bronstad
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Japan's government recently estimated that this month's devastating earthquake and subsequent tsunami may end up costing about $309 billion in damages — nearly four times that of Hurricane Katrina. Companies such as Toyota Motor Corp. and Sony Corp. have shut down domestic assembly plants, causing a ripple effect on U.S. businesses that depend on parts and supplies from Japan. General Motors Corp., for instance, is looking at cutting spending after production was disrupted due to shortages of parts made in Japan. Barry Buchman, a partner at Washington's Gilbert LLP, told *The National Law Journal* that insurance claims for damages arising out of the earthquake could be large and contentious.

This article has been edited for length and clarity.

NLJ: How does $309 billion compare to damages in other disasters?

BB: Clearly, it would make it the largest natural disaster ever on record in terms of dollars. I've also seen competing figures as low as $200 billion. We know it's substantial, but it's going to take some time for the dust to clear so we can start getting our arms around this in a more definitive way in terms of the numbers.

NLJ: What kinds of damages are included in this figure?

BB: This is just meant to encompass all the potential damage — property damage, lost revenue from the disruption in the supply chain. The first type of damage, the most basic type, would be physical property damage to companies that have actual facilities in Japan. Physical damage to factories and buildings are the most basic type of damage that is potentially subject to an insurance claim. The next type would be lost revenue or lost profits as a result of property damage. Obviously, if your factory is damaged and you can't make or sell stuff, you're losing money. And if it's your own property that's been damaged that causes the lost profits, it's a "business interruption" claim. If it's lost revenue and interruption of business caused by damage to supplier or customer facilities, it still has to be property damage. That's a "contingent business interruption" claim. Another type of potential claim is the additional costs or expenses companies are incurring. In addition to losing revenue, they're spending extra money or money they wouldn't spend normally to mitigate further losses or deal with the situation.

NLJ: What kind of claims could we see in the U.S.?

BB: Some domestic companies have facilities in Japan. And even if they don't, they may rely on suppliers and customers in Japan for electronic component parts, plastics, rubber. This has been discussed particularly with regard to automotive companies. Even though Japanese manufacturers have assembly plants in the U.S., most of the parts still come from Japan. So even if a company in the supply chain doesn't have facilities in Japan, if they can't get their component parts or supplies because of damages, there would be a "contingent business interruption" aspect to that.

NLJ: What kinds of exclusions are insurance firms likely to bring up to avoid paying the claims?

BB: Some policies have earthquake exclusions. Also, some policies might have flood exclusions, which could implicate a tsunami. Some could have both. You could have a general grant of earthquake coverage but exclusions for certain areas of the world that the insurer feels are particularly high risk.

NLJ: Where do you see these claims erupting into disputes?

BB: If you have earthquake exclusion but flood coverage, you then get into issues of causation. Suppose you had an earthquake that in turn caused a fire that burned a plant down. Earthquakes were excluded but fires were not. The policy insurer would argue it doesn't matter that the immediately preceding cause of damage was the fire. Without the earthquake, you wouldn't have the fire. So it doesn't matter that fire is covered. The policyholder would say, "The earthquake didn't cause the damage. But for the fire, our building could have survived the earthquake just fine. Therefore, it's covered." I wouldn't be surprised to see some disputes there, and courts have come out differently on that.

NLJ: What about for companies that have lost business?

BB: On the contingent interruption side, sometimes carriers will argue you need a total cessation of business. A temporary interruption is not enough. So you could see some disputes there. Courts have generally been favorable to policyholders on this.

NLJ: Do you predict a lot of lawsuits to come out of this?

BB: Certainly, after comparable disasters like 9/11 and, not just Katrina but all those hurricanes from that intense period of '02 and '05, there was a slew of coverage litigation. It wouldn't surprise me if you saw litigation, particularly if we have disputes over this causation issue.

Amanda Bronstad can be contacted at abronstad@alm.com.

Barry Buchman can be contacted at buchmanb@gotofirm.com.