

NEW YORK COURT OF APPEALS ADDRESSES THE AVAILABILITY OF CONSEQUENTIAL DAMAGES FOR BREACH OF OBLIGATIONS UNDER PROPERTY COVERAGE

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On February 19, 2008, in *Panasia Estates, Inc. v. Hudson Insurance Company*, 2008 N.Y. Slip Op 01419, and *Bi-Economy Market, Inc. v. Harleystown Insurance Company of New York*, 2008 N.Y. Slip Op 01418, a divided Court of Appeals held that a property insurer can be held liable for consequential damages for breach of its contractual obligations under certain circumstances.

In *Bi-Economy Market, Inc.*, the plaintiff family owned market in Rochester, New York, sustained a complete loss of its food inventory and heavy structural damage to its building and equipment as a result of an October 2002 fire. Harleystown was the property insurer, providing Bi Economy with replacement cost coverage on the building and contents loss coverage, as well as one year of business interruption insurance. When Bi-Economy submitted its claim, Harleystown disputed the claim, advancing only \$163,000. More than a year later, following dispute resolution, Bi-Economy was awarded \$407,000 in additional damages. Harleystown also only offered Bi-Economy seven months worth of business interruption cover, even though the policy terms clearly provided for twelve months of cover.

Bi-Economy never reopened and sued Harleystown, alleging bad faith claims handling, tortious interference with business relations, and breach of contract. With respect to the latter, Bi-Economy sought consequential damages for its “complete demise”. It alleged that Harleystown improperly delayed payment and failed to pay the lost business income claim, leading to the collapse of the business.

Harleystown moved for partial summary judgment on the breach of contract claim, asserting that the policy excluded coverage for “consequential loss” and therefore, it had no liability for the consequential damages sought by Bi-Economy.

Similarly, in *Panasia Estates, Inc.*, Hudson issued a builder’s risk policy to Panasia, to cover damage to Panasia’s property during renovations. The roof of the building was opened to perform certain renovation work and rain entered, causing extensive damage to the property. Although promptly notified of the loss, Hudson failed to investigate or adjust the claim for several weeks, and then delayed denying coverage for an additional three months. Hudson disclaimed, asserting the loss was the result of repeated infiltrations and/or wear and tear. Panasia then sued, alleging that Hudson breached its contractual obligation to investigate the loss properly. Hudson also moved for summary judgment, asserting that a contractual exclusion for “any other consequential loss” precluded Panasia’s demand for consequential damages stemming from the alleged breach.

In both *Panasia* and *Bi-Economy*, the majority, in an opinion authored by Justice Pigott, held that consequential damages were available. The *Bi-Economy* opinion, referred to in the *Panasia* decision as determinative, held that although consequential damages are not typically awardable in breach of contract claims, they are available when such damages were within the contemplation of the parties at the time the contract was made. (citing to *Kenford Co. v. County of Erie*, 73 NY2d 312, 319 [1989]). Such a determination involves an examination of “the nature, purpose and particular circumstances of the contract known by the parties. . . . as well as “what liability the defendant fairly may be supposed to have assumed consciously, or to have warranted the plaintiff reasonably to suppose that it assumed, when the contract was made””. *Bi-Economy*, 2008 N.Y. Slip Op. 01418 at *3 - *4 (citing to *Kenford*, additional citations omitted).

Key to the decision in *Bi-Economy* was the nature of the coverage withheld – namely, business interruption insurance. Its purpose, the Court noted, was “to ensure that Bi-Economy had the financial support necessary to sustain its business operation in the event disaster occurred.” *Id.* at *5. Indeed, in the absence of that coverage, Bi-Economy had been unable to reopen following the fire. Based upon the nature and purpose of the coverage, the Court held that Harleystown had to have been “aware that if it breached its obligations under the contract. . . it would have to respond in damages to Bi-Economy for the loss of its business as a result of the breach.” *Id.* Therefore, the damages sought by Bi-Economy are consequential damages which were or should have been within the parties’ contemplation at the time of the making of the insurance contract, rendering Harleystown theoretically exposed to such an award against it.

The *Panasia* Court reiterated its holding that “consequential damages resulting from a breach of the covenant of good faith and fair dealing may be asserted in an insurance contract context, so long as the damages were within the contemplation of the parties as the probable result of a breach at the time of or prior to contracting[.]” 2008 N.Y. Slip Op. 01419 at *2 - *3 (quoting *Bi-Economy*, 2008 N.Y. Slip Op. 01419 at *5). In so doing, it affirmed the lower court’s denial of Hudson’s motion for partial summary judgment, but noting that since the lower courts had “failed to consider whether the specific damages sought by *Panasia* were foreseeable damages as a result of Hudson’s breach[.]”, they needed to do so when reconsidering the motion.

The dissent in both cases is identical. Penned by Justice Smith, and joined in by Justice Read, the dissent argues that that the majority has largely nullified the prior holdings of *Roconova v. Equitable Life Assurance Society of U.S.*, 83 NY2d 603 [1994] and *New York University v. Continental Insurance Company*, 87 NY2d 308 [1995], by authorizing the award of what are, in reality, punitive damages, in the absence of any evidence of egregious tortious conduct directed at the public generally. *Panasia*, 2008 N.Y. Slip Op. 01419 at *3. The dissent distinguishes what it considers true consequential damages (a means of measuring the harm done when a party fails in some non-monetary performance), from the “consequential damages” authorized by the Court, and rejects the majority’s position that such damages were reasonably contemplated by the parties as a potential result of the carrier’s breach of the covenant of good faith and fair dealing. *Id.* at

*4 - *5.

The Court's reasoning, particularly with respect to the business interruption coverage which Bi-Economy had purchased in an effort to avoid exactly the result which ensued, is logical and likely to find many adherents. Regardless of whether you find the dissent's position to be more tenable, be guided accordingly, particularly when adjusting a loss involving business interruption insurance. In theory, significant damages beyond the limits of the policy could be awarded should a court conclude that by failing to timely and properly adjust a claim for property loss, the carrier is obligated to pay for the insured's consequential damage.