One Year Later: The Impact of Super Storm Sandy on Commercial Real Estate, Insurance Law and Other Real Estate Legal Issues

November 14, 2013

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Statutory Provision

New York Real Property Law § 227 is one of the few statutory provisions specifically intended to cover the kinds of situations that arise from major storms or other natural disasters. It reads:

> § 227. When tenant may surrender premises. Where any building, which is leased or occupied, is destroyed or so injured by the elements, or any other cause as to be untenantable, and unfit for occupancy, and no express agreement to the contrary has been made in writing, the lessee or occupant may, if the destruction or injury occurred without his or her fault or neglect, quit and surrender possession of the leasehold premises, and of the land so leased or occupied; and he or she is not liable to pay to the lessor or owner, rent for the time subsequent to the surrender. Any rent paid in advance or which may have accrued by the terms of a lease or any other hiring shall be adjusted to the date of such surrender.

Nearly all professionally drawn commercial leases take advantage of this provision's built in waivability which reads "and no express agreement to the contrary has been made in writing." Indeed, such clauses waiving this statute commonly state, "this provision is an 'express agreement to the contrary' within the meaning of Real Property Law § 227." All cases addressing the issue have upheld such provisions.

Super Storm Sandy Landlord-Tenant Litigation

Maiden Lane Properties v. Just Salad Partners, 056312/13, NYLJ 1202598292879, At *1 (Civ NY Schecter).

Just Salad is also a case construing ¶9 of the REBNY lease. In ***Just Salad***, the tenant gave no ¶9 notice at all, but still claimed the benefits of ¶9 's rent abatement allowances. Even more damning to the tenant's position in ***Just Salad***, the tenant's claim was entirely based on loss of electricity, which was tenant's exclusive responsibility under the lease, and other in which the damage to the premises themselves was light, but the weeks of no public utility provided electricity inspired the tenant to claim an abatement of the rent, ***Maiden Lane Properties v. Just Salad Partners***, 056312/13, NYLJ 1202598292879, at *1 (Civ NY Schecter).

The court in ***Just Salad*** wrote:

> Theses terms establish that loss of electricity was a contingency that was anticipated and accounted for by the parties and not, under the circumstances, a type of casualty damage subject to section nine.

In fact, the lease in question even released the landlord for liability for its own failures to provide electricity except in cases of gross negligence or willful misconduct.

Give the absolute absence of notice under ¶9, together with the lease's specific exculpation of the landlord from responsibility for electricity, the tenant's loss in a suit focused entirely on failure to provide electricity was essentially inevitable.

Super Storm Sandy Landlord-Tenant Litigation

Just two reported landlord-tenant cases have come down from Superstorm Sandy, *4261 Realty v. DB Real Estate*, 2013 WL 4437198 and *Maiden Lane Properties v. Just Salad Partners*, 056312/13, NYLJ 1202598292879, at *1 (Civ NY Schecter).

4261 Realty v. DB Estate, 2013 4437198
In ***4261***, Sandy substantially damaged the premises. ***4261*** had substantial focus on the question of giving notice under the casualty clause of standard Real Estate Board of New York leases, ¶9. New York's leading case in all matters of lease construction, Vermont Teddy Bear v. 538 Madison Realty, 1 N.Y.3d 470, 807 N.E.2d 876, 775 N.Y.S.2d 765, 2004 N.Y. Slip Op. 02257 (2004) specifically deals with the effect and use of ¶9 and its complex mechanism for suspending the rent or terminating the lease in the event of casualty.

In *4261*, the notice was held sufficient under the circumstances. While the court sustained the tenant's notice in *4261*, it did so narrowly. The landlord was shown to have actually received the notice and the court also spoke of exigent notice being allowed in exigent circumstances. The only flaw in the notice was that it was not "return receipt requested." Otherwise, it complied with the lease. Tenants' counsel should seek to avoid reliance upon so tenuous a thread and should always counsel tenants claiming a ¶9 casualty to give the notices called for in the lease's bills and notices clause, whenever possible.

Super Storm Sandy
Landlord-Tenant Litigation

Long before Sandy, Milltown Park v. American Felt & Filter Co., 180 A.D.2d 235, 584 N.Y.S.2d 927 (Third Dept. 1992) required the notice precisely as defined by the lease in spite of the tenant's claim that the landlord had actual knowledge, writing:

> Even accepting defendant's conclusory allegation that the premises were unusable, defendant's failure to give the prompt written notice required by the lease bars defendant from obtaining the benefit of the related provision which would relieve defendant from liability for rent while the premises are unusable.

Thus, the ruling in ***4261*** was by no means a foregone conclusion.

In 4261, Paragraph 9 "Destruction, Fire and Other Casualty" stated:

If damaged by fire or other casualty…Tenant shall give immediate notice thereof to Owner and lease shall continue in full force and effect except…

The notice the tenant sent was by a letter not sent by certified mail, return receipt requested. However, the Court waived the requirement because of the emergency nature of Sandy.

The Landlord claimed that the premises never became wholly unusable so as to trigger a rent abatement and the tenant said the contrary.

If the premises were merely rendered partly unusable, then, according to the Court, the tenant would be entitled to no abatement. Therefore, the court ultimately ruled a trial was needed on whether or not the premises were rendered wholly unusable or merely partially so.

Insurance on Real Property – Decisions

Cashew Holdings, LLC v. Canopius U.S Insurance, Inc., 2013 WL 4735645 (EDNY 2013)

After starting in Queens Supreme Court, the case was removed to the federal courts and in Federal District Court, the insured sought a preliminary injunction requiring payment on the insurance policy as a result of Superstorm Sandy and holding the insurance policy in place.
The court found lack of irreparable injury precluded issuance of a preliminary injunction. It also found lack of likelihood of success as the policy excluded damage due to flood or other causes linked to water. The policy did cover wind damage and that defined the limits of the insurer's liability.
The case was about a three family residential building where Superstorm Sandy caused $210K in damages.

Plaintiff sued for wind damage and moved for injunctive relief to continue the policy after August.

The insurer excluded water damage from policy.
The Policy said:
We will not pay for loss or damage caused directly or indirectly:
Water:
Flood, surface water, waves, tides, tidal waves, overflow of any body of water or their spray all whether driven by wind or not....

The Defendant-Insurer's engineers inspected damage to the property and concluded that some damage to the roof was caused by Sandy's high winds. The Defendant paid this amount.

The Defendant's engineers also found some remaining damage was weather pre-existing and other damage was caused by flood waters and buoyant debris hitting the structure or moving within the structure.

However, the Plaintiff's expert said the damage was from wind.

Insurance on Real Property – Decisions

Cashew Holdings, LLC v. Canopius U.S Insurance, Inc., 2013 WL 4735645 (EDNY 2013) continued…

The court found the insurer more persuasive, ruling:

1. If frame has shifted significantly, the attic walls would have cracked. But there are no cracks in attic walls.

2. Photos showed that exterior did not show wind damage.

3. Misalignment of doors pre-dated Sandy.

4. Building is habitable as is. Two of three units are occupied by paying tenants.

5. A temporary restraining order should be denied as the Plaintiff has money to do repairs now and can wait for insurance money if it is won.

The Court also found that the insurer was under no obligation to renew the insurance policy. The lesson from this case is that the consumer or business should not only be extremely careful in selecting insurance policies, but should be prepared for vastly larger premiums in order to purchase more exotic policies once there is a recovery on insurance because of damage from a large scale storm.

Insurance on Real Property—Complaints

These cases are only reported as complaints. There are no reports of judicial decisions with regard to them.

Manfra, Tordella & Brookes, Inc. V. 90 Broad Owner, LLC, 2013 WL 373327

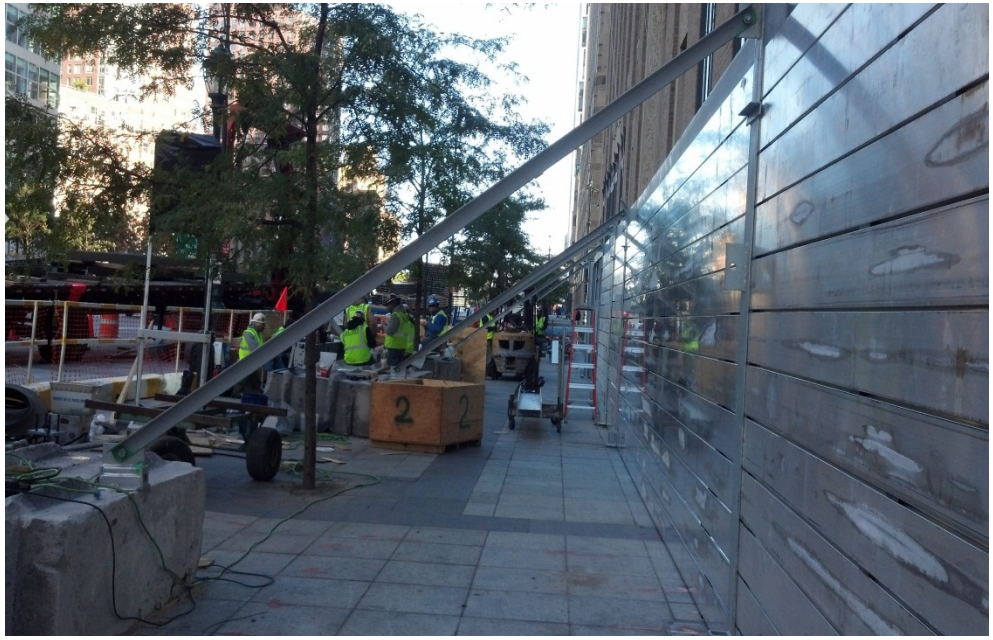
Plaintiff-tenant's theory is that the landlord was liable for neglecting to take supposedly reasonable precautions against flooding caused by Superstorm Sandy such as window boarding and sandbagging.

Amongst the allegations of the complaint were:

> 32. "Because of its history of flooding and location in low lying Zone A, Defendant was well aware that 90 Broad in general, and MTB's offices in Particular, were highly susceptible to flooding and would likely experience severe flooding in the event of a major storm, such as Hurricane Sandy."
>
> 37. Defendant was thus fully aware, and warned of the potential flooding that would occur as soon as Sandy made landfall. Despite this knowledge, and expectation of storm related flooding, Ms. Arce's email did not include any information regarding any steps Defendant took or would take to prevent or at the very least, mitigate, the potential damage to the Building from storm related flooding.

Although no decision is published, the presence of this kind of lawsuit should remind landlords to purchase liability insurance insuring against liability for even the most exotic theories of liability. Without predicting whether the suit would prevail, we do note that the mere defense of the suit is an expensive proposition that could be funded by the insurer's duty to defend.

The other obvious lesson from this suit is that the tenant should have insured itself and the suit, if any, should have sounded in subrogation. Failure of the tenant to be effective in insuring itself is a theme recurring in further cases discussed below.



Insurance on Real Property—Complaints

Lester Schwab v. Great Northern, Index #: 652708/2013

The law firm and Plaintiff, Lester, Schwab Katz & Dwyer, LLP, alleges that its insurance provider and Defendant, Great Northern, breached its insurance policy. The Plaintiff entered into an insurance policy with the Defendant which insured the Plaintiff against any loss of business income it may sustain and against any extra expenses it may incur as the result of a loss to the subject premises by a "covered peril."

As a result of Superstorm Sandy, the Plaintiff and those working for the Plaintiff were unable to carry on its business, specifically because the inclement weather conditions made it nearly impossible for the Plaintiff's employees to enter and leave the premises. The Plaintiff and its employees were, therefore, unable to carry out regular business operations. The Plaintiff sustained a loss of income and incurred additional expenses that it argues justifies coverage by the Defendant.

The Plaintiff argues that the Defendant is legally bound to indemnify the Plaintiff for its losses because the damage that resulted from Hurricane Sandy is a "covered peril." Specifically, the Plaintiff argues that its loss of utilities that prevented it from carrying out regular business activities was caused by an explosion (and not by a flood) to Con Edison's transformer which is a covered peril under the policy. In the alternative, the Plaintiff makes clear that it purchased an additional "Flood Endorsement" policy through the Defendant which provides an additional avenue for coverage if it is discovered that the flood, and not the explosion, caused the loss of utilities.

The Defendant disclaimed coverage and argues that the Plaintiff's loss of utilities (which ultimately led to its inability to carry out regular business operations on the premises) was caused directly by flood damage to the underground utility infrastructure and not by an explosion. Since flood damage does not suffice as a "covered peril," the Defendant refuses to indemnify the Plaintiff. Further, the Defendant argues that because the state of New York did not order an evacuation of Plaintiff's offices, there was no legal inability to ingress and egress from the premises. The Defendant takes the position that the Plaintiff's employees technically could have carried on its regular business activities and, therefore, is under no legal obligation to indemnify the Plaintiff for its losses.

Insurance on Real Property—Complaints

Shapiro v. National Fire, Index # 650037/2013

The law firm and Plaintiff Shapiro, Beilly & Aronowitz, LLP, alleges that its insurer and Defendant, National Fire Insurance Company of Hartford, breached its insurance policy resulting in business losses in excess of $72,975. The Plaintiff's insurance policy included certain covered perils, some losses caused by flood and, significantly, "equipment breakdown" which included coverage for business income and extra expenses including "loss caused by or resulting from breakdown to equipment that is owned, operated or controlled by a local public or private utility…"

The Plaintiff argues that any business losses it suffered are covered by the Defendant's insurance policy. The Plaintiff argues that its employees were unable to carry on normal business operations as a result of an explosion to Con Edison's transformer that severed power and heat to the Plaintiff's offices. Specifically the Plaintiff cites the "Equipment Breakdown" section of the policy which would cover any loss that resulted from a "breakdown" to equipment owned by a public or private utility. Here, Con Edison (a utility) suffered a breakdown as a result of an explosion that severed power to the Plaintiff's offices. The Plaintiff, therefore, demands coverage.

The Defendant argues that the "breakdown" mentioned above was a direct result of a flood and not an explosion and that, therefore, any losses derived from such a breakdown is not covered by the current policy. The Defendant ultimately argues that it is not obligated to indemnify the Plaintiff because the exclusions taken together with the terms of the current policy bar coverage.

Business Expense With Extra Expense Insurance For Law Firms

Additional Coverages

Loss of Utilities

We will pay for the actual:

- **Business income** loss you incur due to the actual impairment of your **operations**
- Extra expense you incur due to the actual potential impairment of your **operations** during the **period of restoration**, not to exceed the applicable Limit of Insurance for Loss of Utilities shown under Business Income in the Declarations.

This actual or potential impairment of **operations** must be caused by or result from direct physical loss or damage by **covered peril** to:

- Building;
- **Personal property of utility** located either inside or outside of a **building**; or **service property.**

Excluding overhead communication, transmission or distribution equipment, necessary to supply your premises with:

- Water supply;
- Communication supply;
- Power supply;
- Natural gas supply;
- Sewage treatment;
- **On-line access,** services.

We will pay such loss provided that the disruption of services:

- Is not due to your failure to comply with the terms and conditions of any contract; and has been reported to the service provider.

We will not pay for the actual **business income** loss you incur until the:

- Applicable waiting period shown in the Declarations for Business Income expires.
- Applicable waiting period shown in the Declarations for Loss of Utilities expries
- First 24 normal business hours following the direct physical loss or damage expires, whichever is longer.

This Additional Coverage does not apply if the direct physical loss or damage is caused by or results from earthquake or **flood**.

Explosion

Insurance on Real Property—Complaints

Neptune Food Corporation v. Federal Insurance Company, 2013 WL 3423065 (E.D.N.Y.)

An insured sued for business losses caused by Superstorm Sandy. The controversy of the case centers around clauses in the insurance policy dealing with covered perils worsened by uncovered perils.

Claiming $3 million in damages and having been paid $1.25 million with an additional $1.8 million still outstanding, the collection of independent stores known as Key Foods sued its insurer claiming that the insurer should provide coverage for Sandy as it was a windstorm and that paragraph was separate and according to the Plaintiff, "repugnant" to the flood waiver in the insurance policy.

Plaintiff claimed that the policy is ambiguous and therefore must be construed in favor of the stores. Plaintiff also claimed that the insurer violated the covenants of good faith and fair dealing.

The Policy read:

Flood
This insurance does not apply to loss or damage caused or resulting from:
Waves, tidal water or tidal waves.
Rising overflowing or breaking of any boundary, of natural or man made lakes, ...oceans, rivers ... regardless of any other cause or event that directly or indirectly:
Contributes concurrent to or worsens...
The loss or damage even if such other cause or event would otherwise be covered.
Windstorm or Hail

We will pay:
The amount of loss or damage in excess of the property damage dollar deductible
And
The amount of loss after the business income waiting Period shown in the Schedule above for business income
If such loss or damage is caused by or results from windstorm or hail, regardless or any other cause or event that directly or indirectly contributes concurrently to, contributes in any sequence to, or worsens the loss or damage.;

Utility Liability—Decisions

Balacki v. Long Island Power Authority, 40 Misc.3d 1220 (Dist. Nas. 2013)

Plaintiff sued in small claims court for loss of food due to loss of refrigeration due to the extended loss of power in the aftermath of Superstorm Sandy. The Court found clear evidence that the Power Authority was negligent. However, prevailing case law exempts a power utility from liability for loss of electricity if the published rates claim such an exemption for mere negligence, as opposed to gross negligence.

Quoting the Moreland Commission that had investigated what went wrong with Sandy and why, the court wrote, "Hurricane Sandy was a unique storm which caused a unprecedented interruption of service to Lipa customers." The resulting "power outage" was "inevitable" and was on a scale which would take days for restoration under optimal conditions."

According to the court, it was unable to find gross negligence because under its reading of the case law, "gross negligence" entails the failure to exercise even slight care. Holding that the entirely inadequate precautions of the utility did not rise to that level, it dismissed the complaint.

Lesson: Since the law immunizes the utility, the only protection for both businesses and consumers is in the purchase of insurance. However, such purchases themselves must be careful so as to cover *all* intended hazards such as business loss, damage due to storm, damage due to flood, damage due to water infiltration, and damage due to wind. Existing case law sustains many disclaimers of coverage. The only way to get away from these disclaimers is to purchase insurance containing no such disclaimers. The following case illustrates this point.

Insurance on Real Property—Complaints

Newman Myers v. Great Northern, Index # 151774/2013

The law firm and Plaintiff, Newman Myers, P.C., alleges that its insurance provider and Defendant, Great Northern, breached its insurance policy. The Plaintiff entered into an insurance contract with the Defendant and the policy specifically covered any lost business income and expenses.

As a result of Hurricane Sandy, the Plaintiff and those working for the Plaintiff were unable to carry out normal business operations. Specifically, the employees could not ingress or egress from the business premises because of the lack of light and heat. The Plaintiff, therefore, lost significant income that it argues should be covered by its insurance policy with the Defendant.

The Plaintiff argues that its inability to carry out its normal business function is a direct result of an explosion to the Con Edison Facility which cut off the Plaintiff's utilities. It argues that any flooding to the Con Edison facility does not constitute direct physical flooding to its business premises. Note: The Con Edison building is inland whereas the Plaintiff's offices are downtown. As a result of this explosion which severed utilities to the Plaintiff's offices and as a result of police officers denying entry, the Plaintiff's employees were unable to ingress and egress, resulting in significant business losses that the Plaintiff argues deserves coverage.

The Defendant affirmatively argues that the Plaintiff's officers were not located in a mandatory evacuation zone and that, therefore, there was no prohibition of access by any civil authority. Essentially, the Defendant argues that because the Plaintiff's could legally enter and leave their offices, any business losses should be attributed to the Plaintiff. The Defendant, therefore, disclaims coverage.