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EDITOR'S NOTE

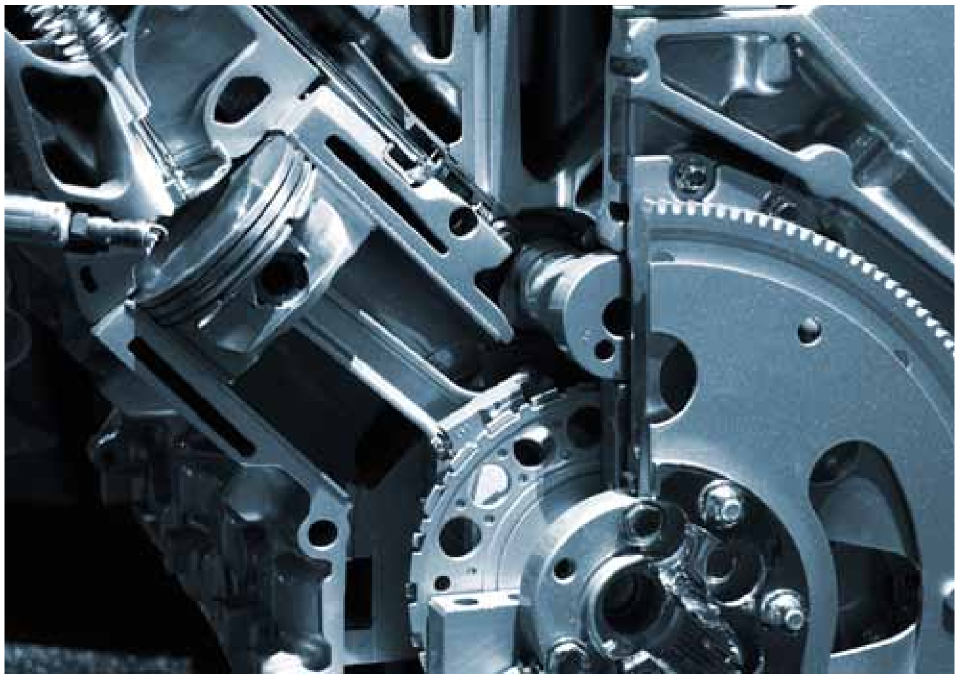
Equipment Breakdown Insurance: Few Coverages Create as Much Confusion and Misunderstanding

Even the most seasoned insurance professional will admit that the depth and complexity of equipment breakdown policies can be overwhelming. Yet the protection they afford can be crucial to a company's ability to recover from a serious accident stemming from an equipment malfunction.

Originally called boiler and machinery insurance, this topic was first addressed in an earlier issue of Adjusting Today *authored by Paul O. Dudey, CPCU. For this new and updated edition, we welcome Donald S. Malecki, CPCU, who goes where few insurance writers dare to go by taking an in-depth look at this coverage, including how it has evolved, the latest definitions, what's covered and what's not—even deductibles and policy conditions. He also discusses how valuation differs from a standard commercial policy, as well as the importance of integrating equipment breakdown coverage with an overall commercial property insurance program.*

From agents and brokers, to attorneys and managers, this piece will enlighten anyone with a need to know about reducing exposures from equipment breakdown losses.

—Sheila E. Salvatore, Editor



Equipment Breakdown Insurance: Too Important to Ignore!

By Donald S. Malecki, CPCU

The term "boiler and machinery" insurance has become an anachronism—just like "fire and extended coverages of property" policies and "comprehensive general liability" policies. The new, modern term is **"equipment breakdown"** insurance.

This change did not happen overnight. Many insurers writing boiler and machinery insurance started using the new term in the late 1990s. One of the last organizations to follow the leader and begin referencing the newer term is the Insurance Services Office (ISO), when it introduced its 2006 changes. The fact that the origin of boiler and machinery insurance dates back over 100 years, to 1866, means that it may be awhile before insurance veterans get used to the new term.

Equipment breakdown insurance is fairly straight forward, connoting coverage for explosion and/or breakdown of steam, water tube, and fire tube boilers and accessory machinery. Undoubtedly, the change in terms was made because of the numerous other kinds of equipment that became eligible for insurance against accidental breakdown. Currently, this equipment can be categorized as: (1) equipment built to operate under internal pressure, such as boilers and pressure vessels, (2) electrical or mechanical equipment used in the generation, transmission or utilization of energy, (3) communication and computer equipment and (4) the equipment in (1), (2) and (3) used by utilities to supply its (sic) services.[1]

Equipment breakdown coverage commonly is written under a separate policy. It is not unusual, however, for insurers writing highly protected risks (HPR) policies to also include equipment breakdown coverage. Insurers of package policies, such as business owners forms, also accommodate insureds with some coverage, and some coverages can be automatically included or added by endorsement to property forms. It also may be possible to purchase equipment breakdown coverage in lieu of purchasing equipment maintenance insurance, the latter of which is intended to pay for losses to equipment that are not covered by any warranty, guarantee or service contract.

With the exception for steam, water tube and fire tube boilers used for heating and generating power in public places, and equipment requiring inspections, such as elevators, coverage for other equipment is purely voluntary. Whether this latter equipment

presents a significant enough exposure to warrant insurance will depend on the nature of the equipment and its cost. It may turn out to be cost-effective where it is purchased along with mandatory coverage for boilers and other equipment.

Most states have laws regulating the inspection of boilers used for heating and generating power in public places. These laws generally require annual inspections. When one considers the cost of a governmental inspection, it often turns out that the cost is less than what an insurer charges for its inspection and insurance. Although the purpose of an inspection is to reduce the chances of loss, explosions and breakdown still occur. If such a loss was to occur and the owner had only a governmental inspection, the owner might be without insurance for resulting bodily injury or property damage, or both. It often turns out better, however, to purchase an equipment breakdown policy on the boiler so as to obtain not only an annual inspection by the insurer's engineer, but also insurance to protect against a loss.

Equipment Breakdown Entails Many Different Objects

"Object" is a term that has its genesis with boiler and machinery policies. It referred to the general category of equipment covered and defined in more precise terms of what "object" included. In the case of *National Union Fire Insurance Company of Pittsburgh, PA. v. The Travelers Indemnity Company, 210 F. Supp.2d 479 (S.D.N.Y. 2002)*, for example, electrical fixtures and components in an insured's plant were held to be objects for purposes of a boiler and machinery endorsement to a property policy.

Briefly, the insurer issued a property policy to the named insured, a paper carton manufacturer. The coverage forms consisted of a building and personal property form and a special causes of loss form, both remarkably similar to the ones offered by ISO. Accompanying these forms was a boiler and machinery endorsement covering: (1) direct physical loss or damage to property of the insured and to others in the care, custody or control of the insured, (2) loss and expense resulting from necessary interruption of business resulting from an "accident" to an "object," (3) extra expense, and (4) spoilage.

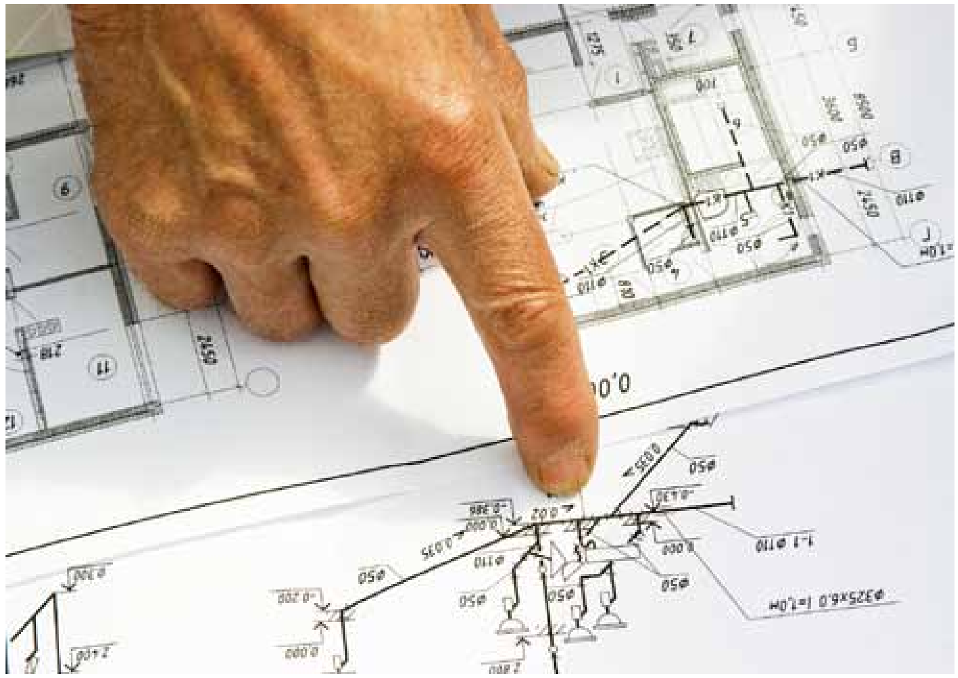
1. ISO Form EP 00 20 09 07, Copyright, ISO Properties, Inc. 2006.

Travelers entered into an agreement to reinsure the boiler and machinery endorsement of National Union. (These reinsurance agreements are common.) This allowed National Union to spread risks and permit a reduction in the amount of reserves National Union would otherwise have been required to maintain.

The problem arose when an off-premises power transformer supplying electricity to the named insured malfunctioned, causing a power surge. The surge, in turn, caused small fires and resultant damage to various electrical fixtures and components throughout the plant, requiring repair and replacement. Both National Union and Travelers disagreed over the cause of the malfunction. According to Travelers, vandalism caused damage to the transformer.

In the final analysis, the court held that since the transformer was owned by the power company and not the insured (the paper carton manufacturer), the transformer could not have been considered an object for purposes of the boiler and machinery endorsement. However, that endorsement did include in the definition of object a "mechanical or electrical machine or apparatus used for the generation, transmission or utilization of electrical power," which the court said aptly described the named insured's damaged electrical equipment and fixtures. The loss also qualified as an accident.

A number of insurers offer equipment breakdown coverage. For the larger risks, Hartford Steam Boiler (HSB) is undoubtedly



the predominate insurer. In fact, some insurers that write this insurance will sometimes have the HSB reinsure their accounts. This discussion of equipment breakdown coverage, however, is based on the latest (2006) provisions of Insurance Services Office (ISO).[2]

Standard ISO Coverage Approach

A basic policy declarations page, a policy conditions form, an equipment breakdown declarations page and an equipment breakdown form EB 00 20 are used along with one or more individual endorsements available to modify the coverage to meet the insured's or underwriter's needs. The equipment breakdown declarations page EB DS 07 is an important part of the policy, considering that insurance applies only to the coverages listed and for the limits designated. This means that the data on this page should be checked carefully to be sure it is correct and complete.

ISO form EB 00 20—equipment breakdown protection coverage—is the latest coverage document. The covered cause of loss is "breakdown" to "covered equipment." The term "breakdown" is defined in the definitions section of the form. This definition includes what a covered breakdown is, what it is not and what losses are included. The first criterion of coverage is that there is direct physical loss that causes damage to covered equipment which necessitates its repair or replacement. The nature of the physical loss is: (1) failure of pressure or vacuum equipment, (2) mechanical failure and (3) electrical failure.

The term "covered equipment" is defined to include the above four categories of equipment mentioned earlier in this article, namely: (1) equipment built to operate under internal pressure, such as boilers and pressure vessels, (2) electrical or mechanical equipment used in the generation, transmission

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or utilization of energy, (3) communication and computer equipment, and (4) the foregoing equipment in (1), (2) and (3) used by utilities to supply its services.

ISO form EB 00 20 lists the following coverages which, if selected, apply only to that portion of the loss or damage that is a direct result of a covered cause of loss:

1. Property damage – to “covered property” at the described premises. “Covered property” encompasses property the named insured owns, as well as property in its care, custody or control and for which it is legally liable.
2. Expediting expenses – comprising the extra costs necessarily incurred to make temporary repairs and to expedite permanent repairs.
3. Business income and extra expense or extra expense only. If the latter is the only one designated, then business income coverage is not provided.
4. Spoilage damage – to raw materials, property in the course of processing, or finished products in storage. Loss must be due to lack or excess power, light, heat, steam or refrigeration, and the property must either be owned or belonging to someone else for whom the named insured is legally liable under a written contract.
5. Utility interruption – which is only available if the insured has selected business income and extra expense or extra expense only or spoilage damage.
6. Newly acquired premises – applies to newly purchased or leased property, subject to notice as soon as practicable and an additional premium. Coverage will be the same as coverage applying to other covered premises.
7. Ordinance or law coverage – applies despite the ordinance or law exclusion otherwise applicable.
8. Errors and omissions – coverage applies for loss not otherwise payable because of an error or unintentional omission in the way the insured property was described; any failure through error to include any premises owned or occupied by the named insured at the policy’s inception; or an error or unintentional omission that results in the cancellation of any insured property.
9. Brands and labels – provides coverage similar to separate

insurance available under that name. In other words, if covered property that is branded or labeled merchandise is damaged through a breakdown, the insurer may take all or any part of that property at an agreed or appraised value. The named insured, however, has to do certain things as conditions warrant, such as stamp the insured property with the word "salvage."

10. Contingent business income and extra expense or extra expense only.

The base limit is $500,000. Each of the above coverages can be written subject to a separate limit or included as part of the base limit for direct damage (property damage) to covered property. Since "covered property" coverage not only encompasses property owned by the named insured but also property damage to property in the insured's care, custody or control, and over which the named insured is legally liable, it is important that the limits be selected wisely. If a $500,000 base limit is selected and the other coverages are designated in the declarations as being included, coverage will hinge on how much is left after paying for damage to property the named insured owns or has in its care, custody or control.

One of the perennial sources of confusion within the realm of property insurance, which includes equipment breakdown, is the difference between expediting expenses and extra expenses. For a more comprehensive discussion of both subjects, refer to the article on page 10 of this issue.

Exclusions

With the expansion of equipment breakdown insurance, it is only natural to see the number of exclusions likewise increase. Currently, there are 21 exclusions. About six of these apply because the losses can be handled by property insurance. The other exclusions apply unless the coverages are selected under this policy. What can be referred to as new exclusions are those that also have been added to other property and liability policies, namely, fungus, wet rot and dry rot.

The coverage is excluded whether loss or damage is caused directly or indirectly from an exclusion and also from a concurrent cause; that is, an exclusion applies regardless of any other cause or event that contributes concurrently or in any sequence to the loss. It also does not matter whether the loss event results in widespread damage or affects a substantial area.

The 21 exclusions, as they appear in the ISO form EB 00 20—equipment breakdown protection coverage form—are as follows:

1. Ordinance or law. (If coverage is not purchased, this exclusion applies.) It excludes the increase in loss from the enforcement of any ordinance, law, regulation or ruling which restricts or regulates the repair, replacement, alteration, use, operation, construction, installation, clean-up or disposal of "covered property."
2. Earth movement, including but not limited to earthquake, landslide, land subsidence, mine subsidence or volcanic action. What is not clear here is whether this exclusion applies solely to natural movement or includes human movement as well.
3. Water. This includes flood, surface water, mudflow, mudslide, water that backs up from sewers, and water that discharges or leaks from a sprinkler system or domestic water piping.
4. Nuclear hazard.
5. War or military action.
6. Explosion. (This cause of loss is commonly covered by commercial property policies. But property policies do not cover explosion from steam boilers, electric steam generators, steam piping, steam turbines, steam engines, gas turbines or moving or rotating machinery when the explosion is caused by centrifugal force or mechanical breakdown.) To the extent this type of equipment is covered by the equipment breakdown policy, this exclusion will apply, unless endorsed to the contrary.
7. Fire or combustion. Including fire and combustion that result in, occur at the same time as, or ensue from the breakdown. Fire or combustion would be covered by the commercial property policy.
8. Fungus, wet rot and dry rot. This exclusion was introduced with the 2006 amendments. If a breakdown occurs, coverage will apply to the resulting breakdown.
9. Any virus, bacterium or other microorganism that induces or is capable of inducing physical distress, illness or disease. The rationale for this exclusion, also introduced in 2006, which applies to property

Equipment Breakdown Insurance Coverage in Brief

Importance

Because it ranks high among the more exotic and frequently misunderstood property and casualty coverages, equipment breakdown coverage is often not adequately addressed in insurance programs. Yet it is too important to ignore in planning a comprehensive insurance program because not only does such a policy provide broad valuable protection, it complements a well-designed general commercial property insurance program to help ensure that a business or organization will survive and continue to prosper after a major loss.

Pricing

Unlike most property and casualty coverages—where payment of losses and claim expenses is the largest part of the cost—with equipment breakdown insurance, if the inspection services are done properly and followed up to assure the correction of hazards, the largest cost factor is the underwriting, inspection and loss prevention service.

Key Considerations

Key factors to consider in integrating this coverage into an overall insurance program are:

— Except when the same insurer is providing both the general commercial property coverage and equipment breakdown insurance (and not reinsuring the equipment breakdown elsewhere), the need can best be met through the use of a joint loss agreement on both the commercial property and equipment breakdown insurance. This attempts to eliminate joint coverage situations.

— The equipment breakdown declarations page is an important part of the policy, and the data on this page should be checked carefully to make sure it is correct and complete. There are references to the data shown on the declarations page throughout the other portions of the policy, so any errors or omissions on the declarations page can be damaging to the intended coverage.

Limits

How much equipment breakdown insurance should be carried? The amount and limits of coverage can only be estimated by examination of the particular situation and making a "worst case" evaluation or loss projection. Avoid the common practice of insuring only for the value of the object being covered. For most items, a covered loss can also cause damage to property beyond the object itself. The cost of the additional coverage does not rise proportionally with the increased risk, so it is better to estimate on the high rather than the low side—and insure accordingly.

damage, time element and other coverages, is the concern over pandemic or other unorthodox transmission of infectious material that may generate claims in the future. This exclusion, in other words, is being added as a precautionary step. If a breakdown occurs, however, such a resulting breakdown is considered to be covered.

10. Explosion within the furnace of a chemical recovery type boiler or within the passage from the furnace to the atmosphere. Furnace explosion is a covered cause of loss under commercial property policies.
11. Damage to covered equipment undergoing a pressure or electrical test. This type of a hazard requires an additional premium to the extent that the insurer is willing to cover it.
12. Water or other means used to extinguish a fire, even when the attempt is unsuccessful. This exposure is covered by commercial property policies.
13. Depletion, deterioration, corrosion, erosion or wear or tear. But a resulting breakdown is covered. These are considered to be losses that are not fortuitous. It also is a potentially very troublesome exclusion.
14. A breakdown caused by the listed causes of loss, if covered by another policy: aircraft, vehicles, freezing, lightning, sinkhole collapse, smoke, riot, civil commotion, vandalism, weight of ice, snow or sleet. These causes of loss are commonly covered in relation to the broad and special causes of loss forms.
15. Breakdown caused by windstorm or hail. These are covered perils of the broad and special causes of loss forms.

16. A delay in or the interruption of any business, manufacturing or processing activity, except as provided by the business income or extra expense, extra expense only or utility interruption coverages.
17. With respect to when business income or extra expense, extra expense only or utility interruption coverage apply, there is no coverage if the business could not or would not have been carried on if the breakdown had not occurred, or the named insured failed to use due diligence and dispatch and all reasonable means to continue operation as normally as practicable.
18. Any indirect loss following breakdown that results from lack or excess power, light, heat, steam or refrigeration, except to the extent that business income or extra expense or extra expense only or utility interruption coverage applies.
19. With respect to utility interruption coverage, any loss resulting from the following: acts of sabotage, collapse, deliberate acts of load shedding, freezing, impact of aircraft, missile or vehicle, lightning, riot, civil commotion, vandalism, sinkhole collapse, smoke or weight of snow, ice or sleet.
20. Any indirect result of breakdown to covered equipment, except to the extent coverage is being provided for one or more of the time element coverages.
21. Neglect by the named insured to use all reasonable means to save and preserve covered property from further damage at and after the time of loss. (This type of an exclusion has been in existence since the 1800s and also can be troublesome to insureds.)

Limits of Insurance

The base limit, as has been mentioned, is $500,000, which can and should be increased considering that in the worse case scenario of an explosion with a building or structure, that amount will not go very far. If any persons were to sustain injuries and surrounding property of others is damaged or destroyed, coverage would apply under the named insured's commercial general liability and umbrella liability policies.

Unless a higher limit or "INCLUDED" is shown in the declarations, the most the insurer will pay for direct damage as a result of a breakdown to covered equipment is $25,000 for each of the following:

A) Ammonia contamination. Ammonia can spoil property that is contaminated. In fact, these types of losses occur fairly regularly. When they do occur, the policy will also pay for any salvage expense.
B) Consequential loss. If part of a product is physically damaged and the rest is unusable, coverage will apply for the reduction in value of the undamaged portion of the product.
C) Data and media. Coverage applies for the cost to research, replace or restore damaged "data" or "media" as defined in the policy, including the cost to reprogram instructions used in any computer equipment.
D) Hazardous substance. Additional cost incurred over and above the amount the insurer would have paid if no hazardous substance had been involved in the loss, when the insured has to clean-up, repair, replace or dispose of covered property.
E) Damage to covered property by water and salvage expenses to property are covered, except leakage from sprinklers or domestic water piping. If fungus, dry rot or wet rot results from such covered water damage, loss or damage attributable to fungus, dry rot or wet rot will not be limited as noted in the exclusions section. Such coverage will, however, be part of the water damage limit.

Deductibles

The base deductible is $500 and applies to any one breakdown. Furthermore, the deductible applies separately to each applicable coverage, except if:

1. A deductible is shown as COMBINED with any of the coverages. When this applies, the insurer will first subtract the combined deductible amount from the aggregate amount of any loss to which the combined deductible applies; or
2. More than one covered equipment is involved in any one breakdown. If this is the case, the highest one deductible shall apply to each of the applicable coverages.

The deductibles that can potentially apply are dollar deductibles, time deductibles, a multiple of a daily value deductible, or percentage of loss deductible.

Apart from the common policy conditions that apply to all standard ISO coverage parts, the equipment breakdown coverage form contains loss conditions and general conditions. Most of these conditions closely follow the comparable conditions on commercial property coverage forms.

Among the loss conditions are those applying to abandonment; appraisal; defense; duties in the event of loss or damage; insurance under two or more coverages; legal action against the insurer; loss payable clause; other insurance; privilege to adjust with the owner; conditions mandating steps to reduce the loss; transfer of the insured's rights of recovery against others; and valuation.

Some conditions apply solely to business income and extra expense coverages. These are:

- Annual report. The named insured is required to complete an annual report of values form each year which must be received within three months of the annual report date shown in the declarations;
- Adjustment of premium;
- Coinsurance requirements.

Among the general conditions of the equipment breakdown coverage form are: additional insured requirements and coverage; bankruptcy; concealment, misrepresentation or fraud; liberalization; mortgage holder; no benefit to the bailee; policy period and coverage territory; premium and adjustments; suspension; joint or disputed loss agreement; arbitration; and final settlement with insurers.

One of the conditions requiring some comment deals with valuation.

Valuation Condition

The valuation method of the equipment breakdown coverage form is quite similar to what applies with commercial property coverage forms. In the event of loss or damage, the insurer will determine the value of covered property in one of two ways.

The first is to determine the cost to repair, rebuild or replace the damaged property with property of the same kind, capacity, size and quality, on the same or another site, whichever is cheaper.

The second way is to determine the cost actually and necessarily incurred to repair, rebuild or replace the covered property. Whichever applies, the insurer will not pay for any damaged property considered to be obsolete and useless to the named insured.

If the named insured elects or the insurer requires that the repair or replacement of damaged covered property be done in such a way that it improves the (1) environment, (2) increases efficiency or (3) enhances safety—but still maintains the existing function—the insurer will pay up to an additional 25 percent of the property damage amount otherwise recoverable and, of course, subject to the limit of insurance.

If it turns out that the damaged covered property is subject to a warranty, maintenance or service contract, and the warranty or contract becomes void because of the breakdown, the insurer will reimburse the named insured for the used costs of nonrefundable and nontransferable warranties or contracts.

Unless the insurer agrees otherwise in writing, if the named insured does not repair or replace the damaged property within 24 months following the date of the breakdown, the insurer will only pay the smaller of (1) the cost it would have taken to repair or replace it or (2) the actual cash value at the time of the breakdown.

Joint or Disputed Loss Agreement

Although perhaps not as important today as before the revision of the boiler and machinery exclusions (and now the equipment breakdown exclusions), controversy would often arise following a loss as to whether the commercial property or the equipment breakdown insurance, or both, should respond.

Except when the same insurer is providing both coverages (and not reinsuring the equipment breakdown elsewhere), this question can best be resolved by use of a joint or disputed loss agreement on both the commercial property and equipment breakdown insurance.

Although not always easy to understand, equipment breakdown insurance is too important a coverage to ignore.

A case in point is *Hartford Steam Boiler Inspection and Insurance Company v. Underwriters At Lloyd's and Companies Collectively, et al., 857 A.2d 893 (Sup. Ct. CT 2004).* (The other insurers involved were: National Union Fire Insurance Company, International Fire Insurance Company, Aetna Casualty & Surety Company, Home Insurance Company, and Zurich Insurance Company.)

This is a long and complicated case. Briefly, however, a catastrophic explosion at an electrical generating plant took place in 1993, causing more than $28 million in damage. The owner of the power and light company submitted claims to the Hartford and to Lloyd's, which provided "all risk" property coverage. After investigating the losses, both the Hartford and Lloyd's denied coverage.

Thereafter, the insured power and light company invoked the joint or disputed loss agreements (referred to in the case as the loss adjustment endorsements) applicable to both policies. These provisions enabled the insured to recover the total loss caused by the explosion by collecting one-half of the amount each from the Hartford Steam Boiler Company and underwriters at Lloyd's. These endorsements also contained a provision enabling the Hartford and the Underwriters, after payment to the insured, to submit any dispute as to respective liability, to arbitration—which they did. Had this joint or disputed loss agreement not been issued to the insured, it would have been caught up in a long and very expensive endeavor. Care, therefore, should be taken that this type of an endorsement is issued on both policies.

• • •

Although not always easy to understand, equipment breakdown insurance is too important a coverage to ignore. Not only does such a policy provide broad, valuable protection, it also complements a well-designed, general commercial property insurance program to help ensure that a business or organization will survive and prosper after a major loss. And that should be everyone's goal.

Extra Expense Coverage Versus Expediting Expense Coverage

Since these terms can be confusing, they are compared here to provide more clarity as to their coverage functions in the equipment breakdown coverage form and in other property insurance forms where they commonly appear.

"Extra expense" is a term used to describe the extraordinary expenses that must be incurred to continue operations following physical loss or damage to covered property, which would otherwise cause the business to close. Generally speaking, there are two types of extra expense coverage.

The first type actually is more appropriately referred to as "expenses to reduce loss" coverage and is only available when business income coverage is not accompanied by extra expense coverage. This coverage pays any necessary expenses incurred to reduce the business income loss, but only to the extent that the expenses incurred reduce the business income loss. This coverage is not available separately for an additional charge. It is automatically included in both business income forms.

The second type of extra expense, which might be more appropriately called "pure extra expense insurance," covers the necessary expenses the named insured incurs during the period of restoration (defined in the policy) that would not have been incurred had there not been direct physical loss or damage to property from a covered cause. Businesses and institutions that *must* continue to operate—such as banks, dairies, hospitals—are candidates for this coverage. Extra expense insurance needs to be purchased for an additional premium. It includes the same expenses to reduce loss coverage found with business income coverage and like business income forms, it is automatically provided without additional cost.

Expediting expense coverage—found in equipment breakdown, builders' risk and some property policies—is appropriately referred to as a mitigating cost provision. In fact, some policies refer to it as a mitigating cost provision or as a sue and labor clause. Sometimes this coverage is automatically included in forms. In others, it needs to be selected, for an additional cost.

Expediting expenses coverage in the equipment breakdown protection form of ISO is a separate coverage that can be purchased. If direct damage to covered property occurs, the insurer will pay for the extra cost necessarily incurred: (1) to make temporary repairs and (2) to expedite permanent repairs or replacement of damaged property. This appears clear enough, but disputes can still arise.

One such case is *R.D. Offutt Company v. Lexington Insurance Company, No. 06-3910 (U.S. Ct. App. 8th Cir. 2007).* The plaintiff (insured) owned a lot of farm land that it leased to tenants on which to grow crops. Under these leases, the insured was obligated to provide water between March 20 and October 19 of every year and to indemnify the tenants for all liability, loss or damage incurred as the result of failure to satisfy its obligations.

One summer there was a switchgear failure at a water pumping station, which cut the water pumping capacity in half. The insured determined within a 48-hour period following the failure that permanent replacement would take weeks—possibly even months. To therefore continue to operate at full capacity, it rented portable generators and bought diesel fuel to supply them. These measures were taken to prevent crop loss and liabilities to tenants. The amount spent was $264,642 for generators, fuel, and related labor and freight charges.

The insured had a property policy that included loss of business income and extra expense coverage. Under the expediting expense clause, the policy covered "the reasonable extra cost of temporary repair and/or replacement and/or expediting the repair and/or replacement of damaged property insured hereunder." Loss or damage to growing crops was specifically excluded. When this claim was submitted to the insurer, it paid $628,262 for the cost to permanently replace the switchgear, but the insurer declined to cover the expenses related to the rental of the generators and purchase of the fuel. The insurer's reason was because the expenses were incurred to save the growing crops.

The district court concluded that the contract's expediting expense clause allowed for a temporary replacement for damaged property and that the fuel and generator rental costs were covered. The

court concluded that the policy contemplated that covered property such as the switchgear had value for the function it performed in addition to its value as a piece of property. The policy provision on expediting expenses, therefore, applied to both the cost of temporarily replacing the switchgear's function and the cost of permanently replacing it.

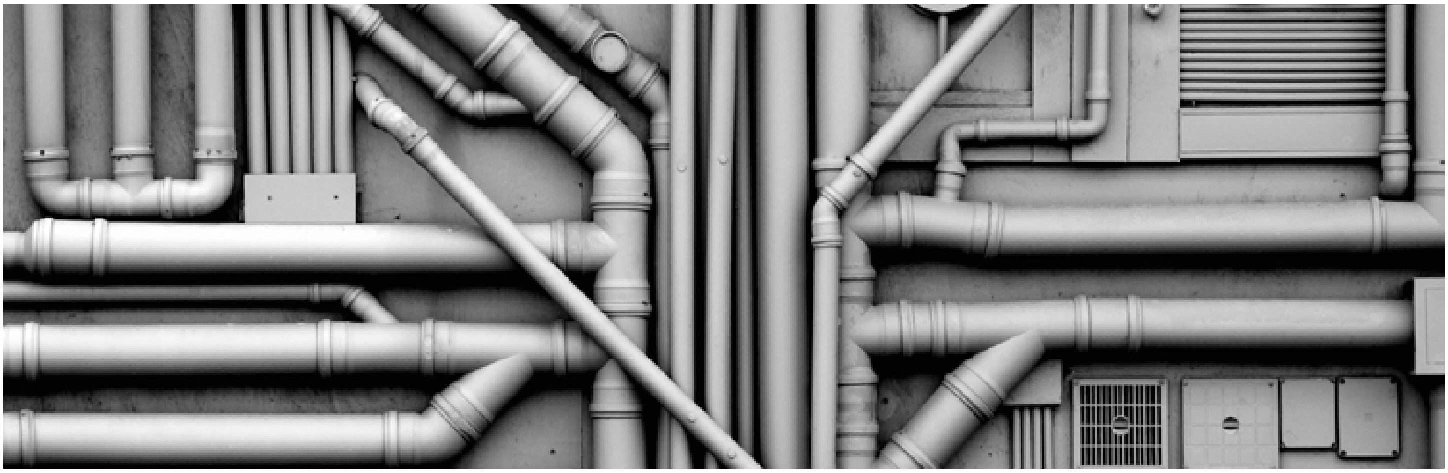
Also, because the rented generators and purchased fuel replaced the switchgear's function of powering the water pump, the court held that the expediting expense clause covered the costs incurred in obtaining them. The court also decided that the policy's growing crops exclusion did not apply because it barred coverage for physical loss or damage to crops—not for costs incurred to replace covered property in order to save or protect the crops. The court of appeals affirmed the district court's decision.

In the majority of cases involving expediting expenses, the big question is whether expediting expenses incurred are truly for temporary repair or for permanent repair. Representative of such cases is *Detroit Edison Company v. Protection Mutual Insurance Co., 134 F.3d 790 (U.S. Ct. App. 6th Cir. 1998).*

It was held there that the insured electric utility's cost of installing temporary replacements for damaged transformers and cables was not covered by an expediting expense provision of its property policy, which included boiler and machinery coverage. This policy covered the extra costs of temporary repair of damage to property and the extra costs of expediting permanent repair or replacement of such damaged property.

The question under consideration was whether the policy obligated the insurer to pay, as extra costs of temporary repair, the cost of installing temporary replacements for damaged transformers and cables. The district court answered the question "no," concluding that to replace the damaged property temporarily was not to repair it temporarily. The court of appeal affirmed the district court's decision.

What is interesting to note in this case was the testimony of the insurer's chief underwriter who



stated the following with regard to expediting expense coverage:

> It was developed at a time when boiler and machinery policies were written as separate policies on a specific object basis. If such a policy covered production equipment, for example, and a piece of equipment of that type were damaged in a fire or other peril insured against, the policy's expediting expense provision would obligate the insurance policy to pay "additional costs to fly in the new permanent object or the extra cost of temporary repair of the damaged object."
>
> When conventional boiler and machinery policies were replaced by comprehensive all risk policies, many insurers incorporated "expediting expense" language in the new policies. As a result, expediting expense coverage was provided for all damaged objects within the ambit of the expanded policies, including objects—electronic data processing equipment, e.g., or communications equipment—that might not have been covered under the older policies. But the adoption of the comprehensive all risk forms produced no change "in the nature and extent of expediting expense coverage…."

According to the court, the logic of this unrefuted testimony of the insurer's chief underwriter was that expediting expense coverage was not somehow transformed into extra expense coverage. The record reflected in this case that the named insured utility specifically requested expediting expense coverage but not extra expense coverage, which was not purchased.

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