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The war exclusion in the world of ISIS and Al-Qaeda

By John K. DiMugno, ***Insurance Research Group***

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Decades ago, it was commonly understood that war was a military action between government forces of sovereign nations. But that was before any of us had heard of Al-Qaeda, ISIS, the Taliban or any of the other armed groups controlling various jurisdictions like pseudo-governments.

The proliferation of these quasi-governmental groups has created insurance coverage issues for businesses operating in volatile regions of the world.

When the activities of these organizations disrupt a business's operations or otherwise inflict damage or injury, it often is difficult to know whether the loss results from an act of war, which typically is excluded, or an act of terrorism, which is a covered risk.

The proliferation of quasi-governmental groups such as Al-Qaeda, ISIS and the Taliban has created insurance coverage issues for businesses operating in volatile regions of the world.

The Ninth Circuit recently grappled with these questions in *Universal Cable Productions LLC v. Atlantic Specialty Insurance Company,* 929 F.3d 1143 (9th Cir. 2019), which held that the war exclusion did not preclude coverage for costs incurred by a television production company when rocket attacks launched by Hamas into Israel forced the company to move locations and delay production.

Applying California law, the circuit court held that the district court improperly interpreted the war and warlike action exclusions in a television production company's production interruption insurance policy according to their ordinary and plain meaning.

The district court should have given the terms "war" and "warlike action" their "special meaning" or customary usage in the insurance industry, where the terms are understood to mean "hostilities between *de jure* or *de facto* governments."

The rocket launches were terrorist attacks, which the policy covered, not acts of war.

FACTUAL BACKGROUND

Before going to Israel to film a television series in Israel, the insured purchased insurance for production delays from Atlantic Specialty Insurance Company.

The insurance policy was negotiated by the insured's broker, who originally proposed 3 war exclusions to the insurer. The insurer then made some edits and added a fourth war exclusion.

The policy covered losses that were "a direct result of an unexpected, sudden or accidental occurrence entirely beyond" the control of the insured, including "[i]mminent peril, defined as certain, immediate and impending danger of such probability and severity to persons or property that it would be unreasonable or unconscionable to ignore."

The policy covered loss caused by terrorism if that loss was not otherwise excluded.

Shortly after production started in Jerusalem, Hamas started firing rockets from Gaza into Israeli civilian populations. Israel responded by launching a military campaign against Hamas.

The hostilities forced the insured to delay production for one week, and the insured sought coverage for the resulting costs from Atlantic Specialty.

The insurer denied coverage based on two exclusions — the war exclusion and the warlike action exclusion.

The war exclusion precluded coverage for losses caused by "[w]ar, including undeclared or civil war." The warlike action exclusion precluded coverage for "[w]arlike action by a military force, including action in hindering or defending against an actual or expected attack, by any government, sovereign, or other authority using military personnel or other agents."

POLICY INTERPRETATION QUANDARY

The parties disagreed about how to interpret the exclusions and whether they applied to the rocket attacks and Israel's response. The insurer argued that exclusions should be understood in their popular and ordinary sense.

The insurer maintained that the common understanding of "war" or "warlike action" includes rocket attacks into Civilian areas by

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Hamas, whose avowed purpose is the destruction of Israel, and counterattacks by the sovereign state of Israel.

The insured argued the terms war and warlike activities have acquired specialized meaning within the insurance industry. Specifically, the insured asserted that specialized meaning limits the reach of the exclusions to losses caused by "hostilities between *de jure* or *de facto* governments."

Although Hamas provides social services in the Gaza strip, Hamas has agreed to give up any formal responsibility for governing Palestine, and Hamas members no longer serve as government ministers. Moreover, the United States has never recognized Hamas as a sovereign or quasi-sovereign authority, refuses to negotiate with Hamas, and designates Hamas as a terrorist organization.

The Universal Cable decision serves as a reminder that the rules of insurance policy interpretation should never be applied reflexively.

The insured therefore maintained that Hamas did not qualify as a *de jure* or *de facto* government within the meaning of the exclusion.

The trial court adopted the insurer's position and concluded that the rocket launches and Israeli retaliation "easily would be considered a 'war' by a layperson." The court therefore entered summary judgment against the insured.

NINTH CIRCUIT

The Ninth Circuit reversed, finding that the district court misapplied the rules of insurance policy interpretation.

This was not a case in which the court needed to resort to the principle of contra proferentum to resolve policy ambiguity in favor of the insured or prevent the insurer from imposing an overly technical meaning.

The insured and the insurer each understood both the customary usage within the insurance industry and a layperson's likely understanding of the terms. The issue was which interpretation should control.

California Civil Code § 1644 provides that the terms in an insurance policy are "understood in their ordinary and popular sense, rather than according to their strict legal meaning; unless used by the parties in a technical sense, or *unless a special meaning is given to them by usage, in which case the latter must be followed.*" (emphasis added).

Thus, ordinary and popular meaning applies, *unless* the parties intend a technical meaning *or* the term has a customary usage in the context of the dispute.

Unless both parties are engaged in the trade in which the usage is customary, the party offering the usage must show the parties to the dispute had actual or constructive knowledge of the customary usage.

Here, the insured met that burden by providing unrebutted expert testimony, stating:

(1) that the customary usage of "war" and "warlike activity" requires hostilities between *de jure* and *de facto* governments; and,

(2) the insured would reasonably expect coverage for attacks by a nongovernmental organization when its policy does not contain a separate terrorism exclusion.

The court rejected the insurer's argument, and the district court's ruling, that the insured's burden required it to introduce specific drafting or negotiations history evidence reflecting the parties' intention to use the customary meaning of "war" within the insurance industry.

Such a rule, the court reasoned, "would conflate § 1644 's distinction between customary usage and technical meaning." Only the latter requires evidence of intent.

Having established the policy's meaning, the court next held that Hamas does not qualify as a de jure or de facto sovereign.

Among the reasons cited by the court:

- Multiple countries, including the United States do not recognize Hamas as a legitimate authority in either Palestine or Gaza;
- Hamas does not engage in formal relations on behalf of Palestine or Gaza;
- there was no evidence that Hamas controlled Palestine's borders, airspace, or immigration; and
- Hamas recognized the Palestinian Authority's control over all governing functions.

In applying the "warlike action" exclusion, the district court had ruled that Israel's retaliatory actions also triggered the exclusion, and Israel is a sovereign government.

The Ninth Circuit disagreed, pointing out that the insurer must show that Israel's retaliation was the efficient proximate cause of the insured's decision to stop production.

The court found no evidence in the record and no factual finding by the trial court to support the conclusion that Israel's retaliation was the efficient proximate or predominant cause of the loss.

Indeed, the insurer's own denial letter cited Hamas's rocket attacks as the reason for the loss.

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COMMENT

The *Universal Cable* decision serves as a reminder that the rules of insurance policy interpretation should never be applied reflexively.

While insurers are inclined to seek refuge behind the "technical" meaning of words and phrases and policyholders typically resort to popular and ordinary meanings, here the parties' interests dictated the opposite approach.

Universal Cable's attorneys wisely turned the technical meaning of "war" to their client's advantage rather than attempt to persuade the court that the term was ambiguous in the context of the policy.

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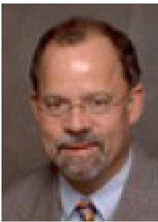
ABOUT THE AUTHOR



John K. DiMugno of **Insurance Research Group** in Cameron Park, California, has testified as an expert witness on a wide variety of insurance coverage and bad-faith issues for both policyholders and insurance companies. He is the author of numerous articles and the co-author of six treatises and periodicals published by Thomson Reuters including Insurance Litigation Reporter (https://tmsnrt.rs/2v0TbIb), California Insurance Law and Regulation Reporter (https://tmsnrt.rs/3aw3Ut9) and California Insurance Law Handbook (https://tmsnrt.rs/2TNVPcq). He can be reached at jd@dimugnolaw.com.

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