



---

Portfolio Media, Inc. | 111 West 19th Street, 5th floor | New York, NY 10011 | www.law360.com  
Phone: +1 646 783 7100 | Fax: +1 646 783 7161 | customerservice@law360.com

---

## 5 Key Insurance Questions For Wineries Hit By Wildfires

By **Jeff Sistrunk**

Law360, Los Angeles (October 20, 2017, 3:53 PM EDT) -- As northern California wineries look to recover from devastating October wildfires that scorched a wide swath of the state's famed Napa and Sonoma wine country, they will face a host of insurance issues, including whether coverage is available for smoke-tainted grapes and how much they can recover for business interruption.

Here, experts discuss five key insurance questions wineries will grapple with in the wake of the fires.

### Is Smoke Damage Covered?

For wineries whose vineyards were untouched by flame, there is still the threat of smoke damage. Microscopic smoke particles can taint the grapes and make them unfit for wine production.

By and large, Napa and Sonoma vintners had already harvested a large percentage of their grapes for the year by the time the wildfires were sparked in early October, experts say. But some heavier red grapes, such as those used to make cabernet sauvignon, were still on the vine.

Since most property and business interruption policies often have express exclusions for growing crops, winemakers' best resource for coverage of smoke damage is government-backed crop insurance. According to experts, to support a claim a winery must enlist the services of an independent or contracted laboratory to test for chemical indicators of smoke taint before harvesting the affected grapes.

While seeking coverage for grapes lost to smoke damage within the policy period should be fairly straightforward, questions may arise as to whether future problems with grape cultivation due to the wildfires are part of the same single occurrence or constitute a separate occurrence implicating coverage under later policies, experts say.

"Short of burning completely, some vines may have sustained smoke damage, which could taint the future production of grapes for years," Anderson Kill PC shareholder Dennis Artese said. "Coverage for smoke-taint-related losses in later years may come down to whether such losses are found to have resulted from a new occurrence in a later policy year under a continuous trigger or other theory."

### How Much Wine Can Be Recovered?

Aside from grapes on the vine, many northern California wineries likely had large quantities of wine in various stages of production as the wildfires advanced. Unfortunately, because winemaking is such an intricate process, even the slightest amount of smoke infiltration can throw off the composition of the "wine in process" and render it unusable, experts say.

"An important question that will be addressed as business owners gather information and determine the extent of loss or damage that they have experienced will be: if smoke infiltrated the wine in process, whether the wine can be salvaged," Blank Rome LLP partner Linda Kornfeld said. "Winemaking is an art; and thus, even a minimal level of smoke could impact decisions regarding salvage."

If a winery determines that the in-production wine can't be salvaged, it will have to record a financial loss and seek insurance coverage, which is usually included under the "stock" section of property insurance sold within the industry.

However, wineries and their insurers may disagree on how to value the ruined wine, depending on how far along in the process it was. For instance, it may be easier to assign a dollar value to wine that was already well into the fermentation process, as opposed to grapes that have just undergone pressing.

"As is the case in many natural disaster events, questions of valuation may be debated between policyholders and insurers, which here could include differing views regarding how to value wine that is damaged or destroyed long before being bottled," Kornfeld said.

Given the highly fact-specific nature of each business's process, Kornfeld added, winemakers should press their carriers to "account for the unique nature of the winemaking business that the insurer agreed to insure."

### **How Are Business Interruption Losses Calculated?**

At the fires' peak, large portions of Napa and Sonoma counties were under mandatory evacuations, and even in the absence of such orders, road closures hindered traffic in some areas. To the extent wineries were unable to carry on shipping operations or hold tastings and other special events, experts say, they may be entitled to business interruption coverage.

"In addition to wine sales, some of these wineries make a fair amount of money from tastings and holding weddings and other events at their venue," Rutan & Tucker LLP partner Lisa Neal said. "The policy terms will dictate what will be covered, but wineries should take a close look at whether they have business interruption coverage, which will cover profits that would have been earned for a defined period of time."

At the outset, it is crucial for a winery to identify and document every aspect of its business that has been affected, whether or not a dollar value is immediately ascertainable.

"For instance, if your tasting room is closed for period of time, document the details of the closure now, even if the potential financial impact is not yet known," said Karen Cusato, founder and managing director of forensic accounting firm Cusato Consulting LLC. "Document all potential losses today, and then as soon as possible begin to estimate any related financial impact by gathering and analyzing key business records."

A great place to start, Cusato said, is reviewing historical financial statements. If a business is new or has had a recent change such as a new facility or increased production, it may also need to look at business forecasts to determine what future profits would have been if the loss had not occurred, according to Cusato.

Pillsbury Winthrop Shaw Pittman LLP partner Robert Wallan pointed out that a winery's grape crop, quality and price will vary from year to year.

"That is an area that will require a lot of calculations. Insureds won't be able to come up with numbers overnight; it's not as simple as saying 'my profits were X million last year,'" Wallan said. "They will have to look at the different components of revenue and cost."

### **Can Reputational Damage Be Proven?**

A subset of business interruption loss covered by some policies is lasting damage to a company's reputation and the accompanying financial impact. The mere perception that northern California wine country is unsafe or the local wine is tainted can have devastating implications for area wineries, according to experts.

"Many winery businesses in the Sonoma and Napa areas are reliant on tourism, which will most certainly decline at least over the next several months due to the current conditions in the area and

possibly for years to come due to reputational issues associated with a tainted crop," Anderson Kill's Artese said. "There likely will be fights as to whether and to what extent those 'wider effects' of the event on the surrounding area should be taken into account in calculating policyholders' business interruption losses."

To prove reputational damage, wineries will have to marshal evidence that a decline in sales or visits was attributable to consumers' negative perceptions, as opposed to market conditions or other factors, experts say.

"Wineries can track the reputational impact by paying attention to customer comments and researching related articles in industry publications and on the web," Cusato said. "They can also analyze customer statistics such as comparing visits up through the time of the loss with visits afterward."

In order to encourage customers to return, wineries may have to incur some extra expenses related to public relations, including sending out letters, providing discounts and advertising, and insurance coverage for those expenses may be available depending on the wording of a policy, according to experts.

"I have seen that a lot with fires — companies trying to assure the public that they are still open for business," Cusato said.

### **Are Breaks in the Supply Chain Covered?**

Many winemakers don't operate on a self-contained basis, where they grow and process solely their own grapes and directly sell their wine without a distributor, noted Blank Rome's Kornfeld. So wineries may encounter "contingent" business interruption issues if a grape supplier or shipper is temporarily or permanently shut down.

"For contingent business interruption, a company should look at any written agreements with their impacted suppliers and/or customers, along with any documentation received from their suppliers or customers regarding the impact of the fires on their businesses and how this may impact doing business with them going forward," Cusato said.

A company's contingent business interruption coverage is often dependent on whether the affected supplier or customer had its own insurance in place for a given loss, experts say.

"Many claims will likely come down to whether or not the purchaser itself had coverage in place that would have covered fire and smoke damage to grapes," Artese said. "The answer to that question may vary based on whether the grapes were still on the vine or harvested and stored in a building on the vineyard's property at the time of loss."

According to experts, wineries should also look into whether they can fill the void left by the inability to carry on business as usual with a supplier or customer.

"A critical question regarding suppliers will be, can you source the product from elsewhere, and if so, how will this impact production and costs?" she said. "For impacted customers, can an alternative buyer be found, or are the related sales lost forever or simply delayed?"

--Editing by Brian Baresch and Emily Kokoll.