Legal Aspects of Big Sports Event Management

Part I: Risk Management—Insurance Coverage for Business Interruption and Event Cancellation

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The legal aspects of big event sports management are diverse. Lawyers mapping them out at the outset of planning such an event face issues related to insurance and risk management, sponsorship, television and other media, alcohol, logistics, spectator and participant issues, background checks and privacy issues, and more. Moreover, all of those issues are overlaid by business, budget, and policy considerations.

Starting with the risk management and insurance coverage discussion here, each article in this four-part series will detail one of the major legal areas of sports event management, and spotlight others that are more discreet. The separate, spotlight article in this issue (see page 26) describes the history and litigation surrounding sports' "Ladies' Night" promotions.

RISK MANAGEMENT: INSURANCE COVERAGE

Among the fundamental considerations in sports event planning are risk management and insurance coverage. Insurance often comes first; it is the gatekeeper to the event in the sense that proof of it may be required before the inception of any subsequent agreements.

The high premiums insurers charge for business interruption and event cancellation coverage reflect the risks involved, including the recently ubiquitous risk of terrorism. Nonetheless, many sports events operate under such coverage, with insurance premiums viewed as a cost of doing business. To maximize the return on premiums spent on this type of coverage, event management should know and understand all of the relevant benefits, contingencies, and exceptions.

TIME ELEMENT

Business Interruption

"Business Interruption" coverage reimburses the insured for the amount of gross earnings minus normal expenses that the insured would have earned but for the interruption of the insured's business (that is, its profits). It applies similarly to perpetual business as it does to a sports event that lasts for a day, a week, or a longer, fixed period of time.

Business interruption coverage provisions typically apply even when an insured is forced to relocate in order to keep its business going or to minimize its overall loss. Insurers may be obligated to indemnify their insureds under such circumstances when businesses earn less than they otherwise would have.[1]

Coverage without physical damage. Although coverage for business interruption is usually granted within a property policy, insureds who have suffered no physical damage still may suffer business losses. For example, given the fact that a hurricane's impact may be felt across the country, insureds who have suffered no physical damage from a hurricane still may suffer business losses. While many insurance policies will not respond to such losses, some policies may respond, and may be a source of substantial economic recovery.

A number of courts have addressed the question of whether business interruption insurance applies to business losses that do not involve actual "physical" damage or destruction. The insureds in two of the leading cases claimed lost revenues because they were forced to close their movie theaters during a dusk-to-dawn curfew imposed by the government after the 1967 Detroit riots.[2] The courts focused on the insuring language of the business interruption policy to determine whether actual "physical" damage or destruction of property was a prerequisite to coverage for those lost revenues. They held that there was coverage because the insuring agreements in the business interruption policies contained not only the words "damage" and "destruction," but also included the word "loss," or otherwise encompassed an interpretation that did not require "physical" damage or destruction to property. One of those courts also focused on the fact that typical business interruption policies are "all risk" policies, reasoning that "[i]f the insurer wanted to be sure that the payment of business-interruption benefits had to be accompanied by physical damage it was its burden to say so unequivocally."[3] While the decisions are not uniform, other courts have reached similar conclusions.[4]

Coverage with damage, but not to insured property. Even if there has been physical injury to tangible property, insurers still may deny coverage if the physical injury was not covered, or if the property did not belong to the insured. For example, the insured in a Sixth Circuit case suffered damage to its property when a machine broke down. The physical injury to the machine was excluded from coverage by a "Mechanical Breakdown" exclusion. However, the court held that the business interruption and extra expense are covered because there had been physical injury, and the "all risk" policy did not exclude all loss from mechanical breakdown.[5]

In another case, the insured suffered $44 million in losses consisting of increased costs of transportation and raw materials, occasioned by flood, even though it did not own the property that had been damaged.[6] The policy language included a coverage grant for "Extra Expense" sustained by the insured as a result of direct physical damage caused by the perils insured against.[7] The insurer denied coverage because the damaged property was owned by suppliers. The insured argued that the policy language required only that (1) there be direct physical damage to "property" and (2) the damage be caused by covered perils. The court found that both of those conditions were met, and held that the language of the insuring agreement did not require that the damaged property be insured under the policy. Therefore, the insured was entitled to coverage for the extra expenses it had incurred.

However, there might not be coverage for business interruption caused by damage to property that is not part of the insured premises. After the January

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17, 1994, Northridge earthquake, a theme park sought coverage under its business interruption policy. In the ensuing litigation, the court held in an unpublished decision that damage to property that was remote and not owned by the insured did not trigger coverage.[8] The court specifically rejected the argument that the damaged roads made it more difficult for people to travel to the park.

Coverage for "restoration" or "extended period of indemnity." When an insured ceases business activities and subsequently resumes operations to the extent possible, business interruption coverage ordinarily extends to cover the resumption period until business returns to normal. This coverage often is found in separate provisions for "restoration" or an "extended period of indemnity." However, coverage may be found even without a policy provision expressly providing for a recovery period.

For example, in a Texas case, the insured owned a restaurant that was severely damaged in a storm.[9] Once the restaurant reopened, it did not return to the same volume of business for another nine months. The insured sought to recover not only for the time it was closed, but also for the time it took to return to its prior business volume. The court broadly interpreted the policy to protect the reasonable expectations of the insured. Because the insurance policy did not explicitly exclude the period of recovery after resumption of operation, the court held that the insured was entitled to recover for the loss it suffered during its closure and also during the months that followed until it recovered its lost business volume.[10]

Coverage also should be afforded for the period from when the insured resumes business until its business returns to normal (subject, of course, to any applicable time or dollar limits in the policy). In a Third Circuit case, fire damage rendered the insured's ultrasound headquarters unusable.[11] The insured's business interruption policy provided coverage for "necessary or potential suspension" of operations. It also required the insured to reduce its loss if possible by "resuming operations." Under the policy, the insurer was obligated to indemnify the insured until it returned to "normal business operations." Rather than suffer the extensive losses that a lengthy complete closure of its business would have entailed, and in compliance with the mitigation requirements of the policy, the insured reopened as quickly as possible at another location. Therefore, it incurred extra expenses and earned less than it otherwise would have. Nonetheless, the district court concluded that once the insured had reopened for business, recovery for the further period of operation with reduced earnings was precluded. The court roundly rejected this conclusion.[12] It reasoned that the plain language of the policy requiring the carrier to indemnify the insured until it returned to "normal business operations" necessarily implied that the carrier was obligated to indemnify the insured while business continued, albeit at a less-than-normal level.[13] Barring recovery of the insured's loss of earnings and extra expenses, when the insured had done no more than attempt to minimize its losses, would have the undesirable effect of giving the insured no motivation to mitigate.

DAMAGE TO PROPERTY THAT WAS REMOTE AND NOT OWNED BY THE INSURED DID NOT TRIGGER COVERAGE.

Contingent Business Interruption

"Contingent Business Interruption" coverage typically covers two types of business interruption. First, it protects against economic losses caused by a "direct" supplier's inability to get its goods to the insured caused by damage to or destruction of its property by an insured peril. Second, it protects against economic losses caused by damage to or destruction of a customer's property of the type insured that prevents the acceptance of the insured's products. This could apply, for example, to situations in which television customers might not be able to receive pay-per-view broadcasts that they otherwise would have ordered.

Civil Authority

"Civil Authority" coverage often applies whenever the insured loses business income because access to its premises is prohibited by an order of civil authority because of damage to or destruction of property belonging to others caused by a covered cause of loss. However, this coverage usually is limited to a specified period of time, which often is as short as two weeks or 30 days.

It may be relatively straightforward to show coverage for many losses associated, for example, with terrorist attacks. This is particularly true when there is a government order restricting access to an area or imposing a curfew. There also may be coverage for orders resulting from terrorist attacks such as any FAA order grounding flights. For example, a Ninth Circuit court stated that "Congress has . . . charged the Administrator of the FAA with carrying out the duties and powers of the Secretary [of Transportation] related to aviation safety. Thus, the Administrator acts on behalf of the Secretary when he issues rules and orders related to aviation safety."[14] Pursuant to the FAA's orders following the attacks on September 11, 2001, air travel was effectively prohibited from approximately 9:40 a.m., September 11 through September 13.

While the FAA's action arguably also affected all of the scheduled sports and entertainment events, insurers may argue that losses are not caused by such orders, but rather result from the "voluntary" cancellation of such events, likely precipitated by a perception that such cancellation or postponement was appropriate (such as in light of the September 11 attacks).[15]

Although there is no authority directly on point, it also could be argued that the authorities who decided to cancel or postpone sporting events also are "civil authorities." Specifically, resort to the

plain meaning of the term, to which courts defer, or to any ambiguity, could allow for argument as to the qualification of the commissioner of Major League Baseball and state colleges and universities as "civil authorities." Such an argument may be based, in part, on cases involving the "state action" and the "color of state law" doctrines, which allow the actions of private entities to be attributed to the government.

An example is provided by the September 11 attacks. Commissioner Selig decided to postpone major league play from Tuesday, September 11, to Sunday, September 16.[16] This decision resulted in the addition of one extra week in the regular baseball season, which moved several well-publicized events, including the final career games of Tony Gwynn and Cal Ripken Jr., Barry Bonds' anticipated surpassing of the home run per-season record, and the World Series. A total of 91 games were postponed to maintain the regular 162-game major league baseball season.[17]

The argument that the commissioner constitutes a qualifying civil authority rests on (a) the special relationship between baseball and the federal government, which has effectively granted immunity to American baseball from the federal antitrust laws, and (b) successfully arguing that when the commissioner acts to shut down the national game of baseball in a state of emergency, he does so under the color of federal law. Whether an agent acts on behalf of civil authority in carrying out an order arguably presents the same inquiry as to whether that agent had "color of authority . . . sufficient to constitute it a civil authority within the meaning of the policy."[18] In the absence of countervailing authority, consideration of whether an act is one under color of state or federal law arguably supports the qualification of the commissioner as a civil authority under the present circumstances.

It is well established that the business of national baseball is immune from federal antitrust laws. "The Supreme Court has held three times that 'the business of baseball' is exempt from the federal antitrust laws."[19] One Supreme Court justice has even expressly stated that "the business is giving exhibitions of base ball [sic], which are purely state affairs."[20] Although the Supreme Court has since expressly held that the actions of baseball's associations cannot be attributed to the state solely on the basis of its antitrust exemption for purposes of the "state action" doctrine,[21] one federal court determined that baseball can act under color of state law where a city significantly encourages the actions of major league baseball.[22] "[S]uch encouragement, particularly the alleged financial indemnification of legal liability . . . [are] the sort of 'significant encouragement' necessary to deem the actions of Baseball to be those of the City of San Francisco."[23] The circumstances involved in responding to terrorist attacks and other events leading to a unilateral cancellation or postponement of events might not qualify. However, if there is some government participation and communication, such as with the commissioner regarding postponement, then the commissioner's decision may be an act of civil authority. This involvement could consist of encouragement by the federal government to resume play at the commissioner's discretion and discussions between the commissioner's office and the FBI regarding security, such as happened after the September 11 attacks.[24] Such communication, in conjunction with Mr. Selig's primary concern over public security,[25] support the construction of the commissioner's decision to prohibit play as an act of civil authority.

The special relationship between government and baseball, and the commissioner's status as a civil authority, also is supported by the federal courts' acknowledgment of the broad and unique powers of the commissioner, which are an "exception," an "anomaly," and an "aberration."[26] As one court concluded about baseball:

> The Commissioner has been given broad power in unambiguous language to investigate any act, transaction or practice not in the best interests of baseball, to determine what preventive, remedial or punitive action is appropriate in the premises, and to take that action. . . . In regard to nonparties to the agreement, he may take such other steps as he deems necessary and proper in the interests of the morale of the players and the honor of the game. Further, indicative of the nature of the Commissioner's authority is the provision whereby the parties agree to be bound by his decisions and discipline imposed and to waive recourse to the courts. . . . In no other sport or business is there quite the same system, created for quite the same reasons and with quite the same underlying policies. Standards such as the best interests of baseball, the interests of the morale of the players and the honor of the game, or "sportsmanship which accepts the umpire's decision without complaint," are not necessarily familiar with courts and obviously require some expertise in their application. While it is true that professional baseball selected as its first Commissioner a federal judge, it intended only him and not the judiciary as a whole to be its umpire and governor.[27]

Finally, another court acknowledged that the "Commissioner of baseball has 'All the attributes of a benevolent but absolute despot and all the disciplinary powers of the proverbial pater familias.'"[28]

The argument relates primarily to professional baseball, given that there exists no parallel history of case law regarding other professional sports, including football and basketball. However, similar arguments regarding the postponement of other sports by their respective commissioners are possible, on the basis of their communications with officials of the federal government. For instance, NFL Commissioner Paul Tagliabue reportedly was in communication with the White House and other leaders regarding the decision to postpone football games scheduled for Sunday, September 16, and Monday, September 17, 2001.[29]

The various state colleges and universities, represented by the individual regional conferences, also constitute potential civil authorities whose actions affected, collectively, the Division I-A football games scheduled for the weekend of September 11, 2001. All of the NCAA Division I-A football games scheduled for Friday, September 14, and Saturday, September 15, were postponed or canceled. Of the Division I-A games that were affected, approximately 79 were rescheduled by agreement of the various conferences and approximately 13 games were canceled without being rescheduled.[30] However, the decision apparently was not made by the NCAA itself—it announced on September 11 that it would leave the decisions regarding the scheduled games to the individual conferences.[31]

As with the commissioner of Major League Baseball, the color of state law doctrine supports the case for the civil authority status of the state colleges and universities, whose collective decision (via the separate conferences) to postpone or cancel games came largely as a result of the NFL's decision to postpone all of its 15 weekend games.[32] It also appears that state universities, operating pursuant to their respective state constitutions, may be state agencies whose agents act under color of state law when they perform their official duties.[33] While this argument may not apply to nonstate colleges and universities, the conferences themselves arguably constitute civil authorities, given that state schools are members and that decisions to postpone or cancel games often are made by agreement within each conference.[34]

Extra Expense

"Extra Expense" coverage indemnifies the insured for any increased cost of business operations above the norm because of a peril insured against. One example would be the purchase of a generator to continue to operate because of an interruption of power caused by a hurricane.

Profit and Commission

"Profit and Commission" coverage applies when an insured's inventory has been destroyed or damaged and, therefore, the insured has been deprived of the opportunity to sell that inventory to the public.

Ingress or Egress

Coverage may be available if access to or from an insured's premises has been stopped or made more difficult because of events such as hurricanes. Many insurance policies cover losses when "ingress" to or "egress" from insured premises is "prevented" because of a covered peril.

In a Second Circuit case, the court indicated that when "prevent" is used with respect to actions (as in to prevent actions), rather than with respect to existence (as in to prevent the existence of), "prevent" may mean "hinder."[35] In insurance policies, the word "prevent" clearly refers to people's actions of ingress to or egress from the premises. Thus, it should be read to mean "hinder." And ingress or egress clearly is hindered for many insureds because of hurricanes and other events. This should trigger coverage.

In another case, a hurricane flooded several roads leading to the insured's premises. One of the roads was closed for several days. However, the insured was able to transport its employees to and from the facility with large trucks. When production at the facility fell, the insured sought coverage under the ingress/egress clause that ensured "loss sustained during the period of time when, as a direct result of a peril not excluded, ingress to or egress from real and personal property not excluded hereunder, is thereby prevented."[36] Although ingress to and egress from the insured's facility were still possible, the flooding of the roads hindered travel to and from the facility. Because usual routes to and from the facility were obstructed and transportation to and from the facility was more difficult, the court held that there was coverage.[37]

EVENT CANCELLATION COVERAGE

Many insureds have not only first-party property insurance with business interruption coverage, but also separate event cancellation coverage. This type of insurance is designed to compensate an insured for a loss arising out of the cancellation, interruption, or postponement of specified events. Policies typically specify that coverage is triggered if the cancellation, interruption, or postponement is caused by "any material reason" that is beyond the insured's control. Most policies also specify that these reasons can include reduced attendance, as long as that reduced attendance is caused by an insured peril.

Many cancellation policies exclude losses resulting from reduced attendance when that reduced attendance is caused by competing events. Most cancellation policies include an exclusion for various forms of weather. Some simply specify "adverse weather," while some specify rain, sleet, or snow for outdoor events. Most cancellation policies include exclusions for war, whether or not declared, and other war-like acts. And coverage usually is not available for cancellations caused by player strikes or owner lockouts. Thus, for example, there was no coverage available in the insurance marketplace for the cancellation of the 2004–05 National Hockey League season.

Many cancellation policies no longer provide terrorism coverage as part of their standard coverage. This is largely because of the cancellation of events such as the Ryder Cup Golf Tournament after the September 11, 2001, terrorist attacks. However, the International Olympic Committee purchased event cancellation insurance for the 2004 summer Olympics and for the 2006 winter games, whether they were cancelled due to natural hazards, war, or terrorism. The International Olympic Committee plans to purchase similar policies for the 2008 summer games and the 2010 winter games.[38] Other significant sporting events such as the Tour de France also have had cancellation coverage.

Thus far litigation over cancellation insurance policies has been limited—probably because of its general lack of availability. The cases to date generally have involved issues not specific to cancellation coverage.[39] However, event cancellation policies did pay for a range of events, including canceled and postponed rock concerts after the September 11 attacks.

CONCLUSION

There are various forms of insurance that may provide substantial financial protection for the cancellation or postponement of events. Specific policy language should be selected for business interruption and event cancellation policies that match the insured's needs. ■

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1. See, e.g., Am. Med. Imaging Corp. v. St. Paul Fire & Marine Ins. Co., 949 F.2d 690, 692–93 (3d Cir. 1991).

2. Sloan v. Phoenix of Hartford Ins. Co., 207 N.W.2d 434 (Mich. Ct. App. 1973); Allen Park Theatre Co. v. Michigan Millers Mutual Ins. Co., 210 N.W.2d 402 (Mich. Ct. App. 1973).

3. Allen Park Theatre, 210 N.W.2d. at 403.

4. See, e.g., Nat'l Children's Expositions Corp. v. Anchor Ins. Co., 279 F.2d 428, 430 (2d Cir. 1960) (business interruption coverage in the absence of actual physical damage).

5. Burdett Oxygen Co. of Cleveland, Inc. v. Employers Surplus Lines Ins. Co., 419 F.2d 247 (6th Cir. 1969).

6. Archer-Daniels-Midland Co. v. Phoenix Assurance Co., 936 F. Supp. 534 (S.D. Ill. 1996).

7. Id. at 537.

8. See Universal Studios, Inc. v. Aetna Cas. & Sur. Co., No. B139301, 2001 Cal. LEXIS 8915 (Dec. 19, 2001).

9. Lexington Ins. Co. v. Island Recreational Dev. Corp., 706 S.W.2d 754 (Tex. App. 1986).

10. Id. at 755–56.

11. Am. Med. Imaging Corp. v. St. Paul Fire & Marine Ins. Co., 949 F.2d 690 (3d Cir. 1991).

12. Id. at 692–93.

13. Id. at 693.

14. S. Cal. Aerial Advertisers' Ass'n v. Fed. Aviation Admin., 881 F.2d 672, 675 (9th Cir. 1989).

15. For instance, the commissioner of the Pac-10 Conference, Tom Hansen, was quoted saying (prior to the confirmed cancellation of the games on September 15) that "[i]f the national day of mourning had been set for Saturday [September 15, 2001], then many more of these games would not have been played." See Chris Dufresne, Conferences Go Own Ways, L.A. TIMES, at http://www.latimes.com/sports/laspcollegemain13sept13.story (last visited Nov. 26, 2001) [hereinafter Dufresne, Conferences]. Similarly, one of the NFL's main reasons that it refrained from playing appears to have been to avoid criticism of the kind received by a former commissioner, Pete Rozelle, for resuming play after President Kennedy's assassination in 1963. See Chris Dufresne, Play Is Stopped, L.A. TIMES, at http://www.latimes.com/sports/la-sp-cancel12sep12.story (last visited Nov. 26, 2001); see also Baseball, Other Leagues Cancel Games, CNN.COM, at http://www.cnn.com/2001/US09/12/attacks.sports.ap (last visited Nov. 26, 2001). Some expressed concern for the inability to travel to destinations of scheduled games also. The Assistant Pac-10 Commissioner, Jim Muldoon, stated, "I can't see putting people on planes this weekend." See id. Similarly, the commissioner of Major League Baseball, Bud Selig, in addressing whether play would resume the weekend of September 11, stated that there were a "myriad of factors and complications," including travel and logistics. See Ross Newhan, All Together Now, L.A. TIMES, at http://www.latimes.com/sports/la-sp-baseball14sep14.story (last visited Nov. 26, 2001).

16. See Newhan, supra note 15.

17. See id.

18. Kan v. Manchester Fire Assurance Co., 15 Haw. 704, 706 (1904).

19. Charles O. Finley & Co. v. Kuhn (Finley), 569 F.2d 527, 541 (7th Cir. 1978).

20. Fed. Baseball Club v. Nat'l League, 259 U.S. 200, 208 (1922) (J. Holmes).

21. See Jackson v. Metro. Edison Co., 419 U.S. 345 (1974).

22. Piazza v. Major League Baseball, 831 F. Supp. 420, 428 n.11 (E.D. Pa. 1993).

23. Id.

24. See Newhan, supra note 15.

25. See id.

26. Charles O. Finley & Co. v. Kuhn (Finley), 569 F.2d 527, 537 (7th Cir. 1978) (quoting the Supreme Court's characterization of baseball's relationship to the federal antitrust laws as an "exception," an "anomaly," and an "aberration" in Flood v. Kuhn, 407 U.S. 258, 282 (1972)).

27. Finley, 569 F.2d at 534–35, 537 (citations omitted).

28. Atlanta Nat'l League Baseball Club, Inc. v. Kuhn, 432 F. Supp. 1213, 1220 (N.D. Ga. 1977) (quoting Milwaukee Am. Ass'n v. Landis, 49 F.2d 298 (N.D. Ill. 1931)).

29. See David Wharton, Baseball, NFL Wait to Play Ball, L.A. TIMES, at http://www.latimes.com/sports/la-sp-events13sep13.story (last visited Nov. 26, 2001).

30. See Rescheduled Division 1-A Games, NBC SPORTS, at http://www.msnbc.com/news/628105.asp (last visited Nov. 26, 2001).

31. See Dufresne, Conferences, supra note 15.

32. See Chris Dufresne, Conferences Run Reverse, L.A. TIMES, at http://www.latimes.com/sports/la-sp-colfb14sep14.story (last visited Nov. 26, 2001).

33. See Nat'l Collegiate Athletic Ass'n v. Tarkanian, 488 U.S. 179, 183 (1988); Graham v. Nat'l Collegiate Athletic Ass'n, 804 F.2d 953, 958 (6th Cir. 1986).

34. See Dufresne, supra note 32.

35. Nat'l Children's Expositions Corp. v. Anchor Ins. Co., 279 F.2d 428, 431 (2d Cir. 1960).

36. Fountain Powerboat Indus., Inc. v. Reliance Ins. Co., 119 F. Supp. 2d 552, 556 (E.D.N.C. 2000).

37. Id. at 557.

38. See Carolyn Adred, Winter Games Covered Against Cancellation, BUS. INS., Feb. 6, 2006, at 17.

39. See, e.g., Long Island Sports Dome v. Chubb Custom Ins. Co., 5 Misc. 3d 1028(A), 799 N.Y.2d 161, 2004 WL 2903619 (Oct. 22, 2004) (carrier's motion for summary judgment regarding insured's failure to appear for examination under oath and to timely file proof of loss denied because of factual disputes).