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COVID-19 AND INSURANCE COVERAGE

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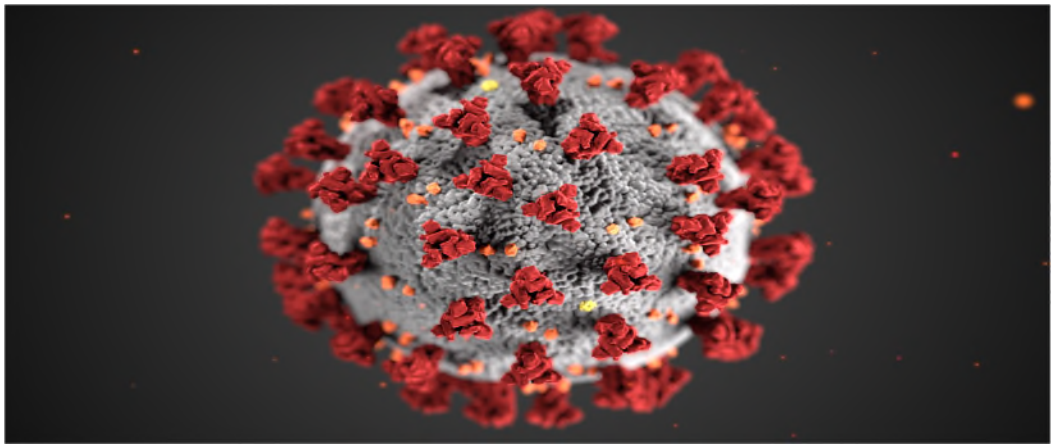

The Covid-19 Pandemic exacerbates the pressure along fault lines in every aspect of our lives. This includes legal fault lines. This article addresses some of those pressure points in insurance coverage.

Some Important Insurance Coverage Issues for COVID-19 Business Loss Claims by Lee Applebaum

COVID-19 is a potential $1,000,000,000,000+ catastrophe for businesses. Insurance coverage demands for COVID-19 business interruption losses are exploding. Many insurers are denying coverage, and insureds' lawsuits for coverage and bad faith have begun. Questions of what business interruption losses should be covered by insurance even reached the COVID-19 daily briefing this past Friday.

Various states, including, e.g., Pennsylvania (Pennsylvania House Bill 2372) and New Jersey (Assembly, No. 3844), are seeing proposed legislation that would require insurers to pay for billions or trillions of dollars in business interruption losses, even if the insurance policies otherwise would not provide such coverage. These proposals usually have a plan tying insurer payments to a fund that would at least partially reimburse insurers for such payments so they are not bankrupted. On the federal level, the idea is circulating for a "Pandemic Risk Insurance Act" that "would create a reinsurance program similar to the Terrorism Risk Insurance act for pandemics, by capping the total insurance losses that insurance companies would face."

While these efforts may ultimately overwrite disputes that would otherwise wind up in every state and federal court, we are only discussing the law as it currently stands on a few COVID-19 coverage issues.

The "Loss Due to Virus or Bacteria" Exclusion

A central starting point is whether policies have a "Loss Due To Virus Or Bacteria" exclusion. This ISO drafted exclusion was originally promulgated in 2006, and is typically numbered CP 01 40 07 06. A copy of the exclusion can be found here.

Paragraph B of the exclusion states, "[w]e will not pay for loss or damage caused by or resulting from any virus, bacterium or other microorganism that induces or is capable of inducing physical distress, illness or disease." Paragraph A provides, "[t]he exclusion set forth in Paragraph B applies to all coverage under all forms and endorsements that comprise this Coverage Part or Policy, including but not limited to forms or endorsements that cover property damage to buildings or personal property and forms or endorsements that cover business income, extra expense or action of civil authority." The exclusion's language makes clear, however, it does not displace other exclusions addressing claims not subject to the virus and bacteria exclusion. Foley v. Wisconsin Mutual Insurance Co., 915 N.W.2d 455 (Wis. App. 2018).

ISO issued a July 6, 2006 circular entitled, "New Endorsements Filed To Address Exclusion Of Loss Due To Virus Or Bacteria," explaining the exclusion. The drafters write, "[t]he exclusion … applies to property damage, time element and all other coverages…." The circular's introduction gives three specific examples of excluded viruses, "rotavirus, SARS, [and] influenza (such as avian flu)." The drafters further observe that "[t]he universe of disease-causing organisms is always in evolution." As we all now know, the original SARS virus and COVID-19 are part of the same virus family.

The introduction adds, "[d]isease-causing agents may render a product impure (change its quality or substance), or enable the spread of disease by their presence on interior building surfaces or the surfaces of personal property. When disease-causing viral or bacterial contamination occurs, potential claims involve the cost of replacement of property … cost of decontamination … and business interruption (time element) losses."

Under the heading "Current Concerns," the circular states, "[a]lthough building and personal property could arguably become contaminated (often temporarily) by such viruses and bacteria, the nature of the property itself would have a bearing on whether there is actual property damage. An allegation of property damage

may be a point of disagreement in a particular case." Exclusions addressing "specific exposures relating to contaminating or harmful substances … enable elaboration of the specific exposure and thereby can reduce the likelihood of claim disputes and litigation."

The authors clearly were thinking of pandemics in drafting this exclusion. They state, "[w]hile property policies have not been a source of recovery for losses involving contamination by disease-causing agents, the specter of pandemic or hitherto unorthodox transmission of infectious material raises the concern that insurers employing such policies may face claims in which there are efforts to expand coverage and to create sources of recovery for such losses, contrary to policy intent." To address these concerns, ISO is "presenting [the Loss Due to Virus or Bacteria] exclusion relating to contamination by disease-causing viruses or bacteria or other disease-causing microorganisms."

In one recently filed COVID-19 case from the District of Columbia, Washington's mayor had issued an order forbidding table seating at restaurants. The restaurant-plaintiff suffered business losses. The insurer denied coverage, and the owner filed a declaratory judgment complaint seeking coverage. A copy of the Complaint in *Proper Ventures, LLC v. Seneca Insurance Co.*, can be found here.

Among other grounds for denial, the insurer relied on the "Exclusion of Loss Due to Virus or Bacteria." The complaint alleges, however, this exclusion does not apply. While this seems implausible per the above discussion, the plaintiff asserts that the "loss of Business Income is not otherwise excluded under the Policy. … [because the] loss of Business Income was not 'caused by or resulting from' a virus as its loss occurred as a result of the Mayor's Order." The plaintiff essentially argues for coverage solely based on a civil authority closure, by contending that the government action in closing the premises cuts off the virus as a causal factor. Once civil authority causation supersedes virus causation, so the argument goes, the exclusion falls by the wayside.

As set forth above, the exclusion's Paragraph A specifically provides that "[t]he exclusion set forth in Paragraph B applies to all coverage under … forms or endorsements that cover business income, extra expense ***or action of civil authority***." The insured will have to overcome this express policy language in the first instance to be able to proceed on its argument.

If insureds making this superseding cause argument can get past the language in Paragraph A on "action of civil authority," courts addressing the intervening cause issue would look to the governing law on interpreting the exclusion's "caused by or resulting from" language. E.g., in various jurisdictions, some courts may measure this by a proximate cause standard, others by a "but for" standard, and others by a substantial cause standard (somewhere between "but for" and proximate cause). Under any causation standard, however, insureds making this argument are still depending on courts eliminating the "why" in the chain of events leading civil authorities to issue closure orders.

General Comments on the Property Damage, Business Interruption, and Civil Authority Closures

The 2006 ISO circular foresaw that in the absence of the virus and bacteria exclusion (i) "the nature of the property itself would have a bearing on whether there is actual property damage: and (ii) "[a]n allegation of property damage may be a point of disagreement in a particular case."

The property damage issue includes two basic prongs: business interruption coverage and coverage for the acts of civil authorities. In the former, there must be "direct physical loss or damage"; and in the later, there must be damage to other property within a specified distance from the insured's property, or in the "immediate area" of the insured's property.

There is some case law, in other fact scenarios, addressing the concept of whether unseen or gaseous substances contaminating property can constitute direct physical damage or loss. For example, a 2014 New Jersey federal case, Gregory Packaging, Inc. v. Travelers Property Casualty Co., addressed ammonia contamination, and a 2016 Oregon federal case, Oregon Shakespeare Co. v. Great American Ins. Co. (later vacated by the parties' agreement), addressed smoke from forest fires closing down plaintiff's business operations. In a 2015 case involving an odor of cat urine permeating a condominium, New Hampshire's Supreme Court gathered cases on both sides of the issue in evaluating what degree of physical alteration is needed to find a direct physical loss. Mellin v. Northern Security Ins. Co. That court held an alteration affecting the sense of smell was a physical alteration. This contrasted with a 2010 Michigan federal court

decision finding strong odors and the presence of mold insufficient to constitute direct physical loss. Universal Image Prods. v. Chubb Corp.

The reality is that the decision concerning direct physical damage or loss, and property damage, may well ride on the judge's own intellectual framework for addressing the physical nature of real, but invisible, phenomena. We can expect courts to address issues as to whether the presence of the virus on a surface is sufficiently intermingled with the surface material as to alter that property, or whether it is separate from the surface. For example, if the virus is on all the tables in a restaurant, and successfully can be cleared off with a disinfectant in an hour, was there direct physical damage or loss? If so, did it only exist for an hour?

What if the virus has reached more difficult to clean parts of the same restaurant, the owner-insured cannot be certain all potentially exposed areas have been sanitized, and the restaurant stays closed because of the risk? Moreover, how does the insured prove the virus is actually present on any surface in the restaurant at all, or how long that presence persisted? Imagine that proof issue in a much larger scenario, like a warehouse, where one employee out of hundreds develops COVID-19, and the entire warehouse might have to be closed and sanitized. It is unlikely that there is going to be testing to determine where the virus actually might be located before sanitizing takes place. There may not even be testing to determine whether the virus is even present at all on any surfaces inside the facility, but only fast action to eliminate potential risk.

The experts required to answer questions of what is physical, or whether matter has been altered on a microscopic level, may well be biochemists or physicists in addition to virology experts, though some of these concepts appear to verge on metaphysics.

Another issue is the duration of any direct physical damage or loss, or any property damage. Even in cases of demonstrable physical loss or damage through viral presence on the premises, those damages can likely be remediated through sanitizing the insured's property. While the sanitized premises may be cleaned and the damage cured, the remediation might mean very little if the same pattern of contamination will regularly repeat itself every time people are allowed back on the premises, as employees or customers.

More significantly, greater economic business losses may well be based upon contamination events that have not happened. Such losses arise only because the insured, public, and government are trying to prevent that

contamination from ever occurring in the first instance, i.e., much of the real economic business loss is the consequence of prophylactic action to avoid risk, rather than the virus' actual presence on an insured's premises.

What if there is no Arguable Property Damage, and a Business is Closed because of Fear or as a Prophylactic Measure?

Thus, the broader economic question may involve those circumstances where the virus is not actually on or in the insured's property, or on or in any property within the distance necessary to invoke civil authority coverage. Rather, the insured's business is closed, either voluntarily or by government order, out of fear the premises ***might become*** contaminated, or that the business premises might simply act as a meeting ground for spreading infection among employees and customers independent of whether any part of the premises is contaminated. The prevention rationale may reach even further outside a concern for direct physical loss or damage, e.g., reasoning that if businesses are closed people will not be taking public transportation to visit the business, or milling about on the streets to walk to a business.

In one New York federal case dealing with the "direct physical loss or damage" language, the court found that "[t]he words 'direct' and 'physical,' which modify the phrase 'loss or damage,' ordinarily connote actual, demonstrable harm of some form to the premises itself, rather than ***forced closure of the premises for reasons exogenous to the premises themselves, or the adverse business consequences that flow from such closure***." Newman Myers Kreines Gross, P.C. v. Great Northern Ins. Co., 17 F. Supp. 3d 323, 331 (S.D.N.Y. 2014). (Emphasis added)

Another New York federal case addressed coverage in a dispute involving purely economic damages resulting from the events of 9/11. Philadelphia Parking Authority v. Federal Insurance Co., 385 F. Supp. 2d 280 (S.D.N.Y. 2005) (interpreting Pennsylvania law). In that case, the plaintiff parking garage operator lost business at the Philadelphia airport due to diminished air travel after the 9/11 tragedy. It sought coverage from its insurer for these economic losses. The court found that the business impacts flowing from 9/11 could not serve as the source of a covered loss. These economic business losses lacked the predicate of direct physical loss or damage to the insured's property. Rather, the insured's loss of business itself was the only

damage to the insured. Similarly, an Iowa federal court ruled that a putative loss of use in business operations occasioned solely by the "threat" of a flood was not physical loss or damage. Phoenix Insurance Co. v. Infogroup, Inc. 147 F. Supp. 3d 815 (S.D. Ia. 2015).

Was Insurance Available to Cover Business Losses before the Current Outbreak?

Another issue will likely be whether insurance coverage was available for viral pandemics before the COVID-19 outbreak. For example, an insured may argue that its reasonable expectations require reading business interruption or civil authority coverage to include pandemics, as there is no other means to obtain insurance coverage for these potential epidemics, making the policy's coverage somehow illusory. Among other things, insurers may respond that insureds could have purchased coverage for pandemics before the COVID-19 crisis; therefore, the policy language should not be read beyond its ordinary meaning to provide coverage where coverage does not reasonably exist under the policy's plain language.

In an April 3, 2020 declaratory judgment filing in Texas, the plaintiff theater and restaurant owner seeks coverage under a "Pandemic Event Endorsement." A copy of the complaint in *SCGM, Inc. v. Lloyds of London, U.S. District Court Southern District of Texas, No. 4:20-cv-01199*, can be found here. The complaint alleges "[f]ollowing the 2014 Ebola crisis, many insurance carriers made specific exclusions for Ebola and other communicable diseases and viruses. Lloyds sought to take advantage of the exclusions in coverage by rolling out a Pandemic Event Endorsement that claimed to 'fill in the gaps that [other insurers] creatively exclude or do not address' that may relate to future pandemics."

The endorsement, attached as an exhibit to the complaint, defines "pandemic event" to include either "(a) the actual presence of an Infected Person within a Covered Location; or, (b) the announcement by a Public Health Authority that a specific Covered Location is being closed as a result of an Epidemic declared by the CDC or WHO." The endorsement limits "covered disease" to 25 specifically listed "pathogens, their mutations or variations" and a 26th category for other diseases designated by Lloyds. The complaint alleges Lloyds took the initial position that COVID-19 "is not covered under the Pandemic Event Endorsement as it is not a named disease on that endorsement." Plaintiff counters that "Severe Acute Respiratory Syndrome

associated Coronavirus (SARS-CoV) disease" is specifically named, that SARS-CoV-2 is the virus causing COVID-19, and that SARS-CoV-2 is a variant of SARS-CoV-1, i.e., a named pathogen.

[We note here that the World Health Organization has stated the International Committee on the Taxonomy of Viruses "announced 'severe acute respiratory syndrome coronavirus 2 (SARS-CoV-2)' as the name of the new virus on 11 February 2020. This name was chosen because the virus is genetically related to the coronavirus responsible for the SARS outbreak of 2003. While related, the two viruses are different." Thus, this litigation may also involve whether the relationship constitutes a mutation or variation sufficient to come within the list.]

Even assuming some level of coverage on any of the above discussed grounds, there will likely be additional issues arising in COVID-19 cases that will require analyzing a wider range of a policy's terms, conditions, sublimits, etc. In evaluating whether to fight the above-described battles, both insureds and insurers should look at the practical consequences of each and every particular policy language battle. The meaning of success should be measured against how things could stand at the end of the war, and not just any one battle.

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