

INSURANCE AND REINSURANCE

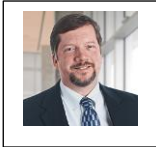
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The mandatory quarantines caused by the COVID-19 pandemic have already resulted in insurance claims for business interruption. This article discusses the challenges to coverage and resulting political and legal pressures on the insurance industry.

COVID-19 Business Interruption Insurance Claims Coverage Issues

ABOUT THE AUTHORS



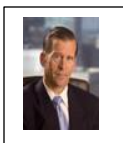
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ABOUT THE COMMITTEE

The Insurance and Reinsurance Committee members, including U.S. and multinational attorneys, are lawyers who deal on a regular basis with issues of insurance availability, insurance coverage and related litigation at all levels of insurance above the primary level. The Committee offers presentations on these subjects at the Annual and Midyear Meetings. Learn more about the Committee at www.iadclaw.org. To contribute a newsletter article, contact:



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I. INTRODUCTION

The COVID-19¹ pandemic will engender a huge number of business interruption insurance claims on a scale to surpass the claims following previous catastrophe claims affecting regions of the United States. While Hurricane Katrina and Superstorm Sandy devastated regions, COVID-19 affects the entire world and within North America, every area of every state and province. Insurance coverage issues inherent in the processing of these forthcoming claims will vary depending on the policy conditions and exclusions in each policy and the circumstances and losses of each insured; however, there are several issues that may occur frequently and these are discussed below. As a side note, federal Cares Act legislation provides forgivable loans to small businesses which turn into grants, thereby decreasing but not erasing an insured's business interruption losses.²

II. PHYSICAL DAMAGE REQUIREMENT

Most business interruption insurance policies include the condition that the insured premises suffer physical damage and many policies since 2006 contain the specific

ISO form CP 01 40 07 06, entitled "Exclusion for Loss Due to Virus or Bacteria." The policy coverage may read that there must be "direct physical loss or damage to property at a premises which are described in the Declarations."

One national law firm often representing insureds argues³ "nothing in these often unedifying terms rules out the possibility of damage caused by the presence of microscopic organisms or requires that loss or damage be visible to the naked eye, or even visible at all." If the premises of the insured's business are flooded or damaged by fire, or building collapse, then the policy condition of an "occurrence" and definitions of "damage" would be satisfied. But what if there is no physical damage to the property of the insured, and the business interruption is caused by some type of governmental shutdown order sparked by the COVID-19 Pandemic?

There is case law holding that some type of physical damage to the insured's premises which causes the business interruption must occur before policy coverage is triggered. In *Mama Joe's, Inc. v. Sparta Ins. Co.* 2018 U.S. Dist. LEXIS 201852, 2018 WL 3412974 (S.D.

¹ According to the Center for Disease Control, a novel coronavirus is a new coronavirus not previously identified. On February 11, 2020, the World Health Organization announced an official name for the disease causing the 2019 novel coronavirus outbreak, first identified in Wuhan China, as coronavirus 2019, abbreviated as COVID-19. [cdc.gov/2019-ncov/faq.html#Coronavirus-Disease-2019-Basics](https://www.cdc.gov/2019-ncov/faq.html#Coronavirus-Disease-2019-Basics)

² The Federal Cares Act signed March 27, 2020 created the Paycheck Protection Program regarding SBA-bank loans for small businesses that continued to pay their employees during the pandemic shutdown. Ultimate forgiveness of these loans if the proceeds are used to pay for payroll costs and other designated expenses for eight (8) weeks following the loan origination is provided for in the act.

³ See Jenner & Block newsletter dated March 12, 2020, by David Kroger and Elin Park.

Fla. June 11, 2018) involving nearby roadwork which caused dust and debris contamination of the insured restaurant, the federal district court held that damage to the property requiring actual damage alteration to the property requiring repairs would be needed to trigger the policy coverage and granted summary judgment for the insurer, thereby denying the restaurant’s claim.

In *Mastrellone v. Lightning Rod Mut. Ins. Co.*, 884 NE 2d 1130 (Ohio App. 2008), the court held that mold could be removed by cleaning and did not affect the structural integrity of the building and therefore did not trigger business interruption coverage. In *Source Food Tech, Inc. v. USF&G*, 465 F.3d 834 (8th Cir. 2006), the Court held that beef imports banned for mad cow disease did not amount to “physical loss or damage.” In *Newman Myers Kreines Gross Harris PC v. Great American Insurance Company*, 17 F Supp. 3d 323 (SDNY 2014) the court held that a power shutoff in advance of Super Storm Sandy approaching did not amount to physical loss or damage. A federal district court in Michigan held in the case of *Image Products v. Chubb Corp*, 703 F. Supp. 2d. 705 (E.D. Michigan 2010), that strong odors, mold and bacteria in the air and ventilation system in the building did not constitute physical damage to the property necessary to trigger insurance coverage and granted summary judgment to the insurer.

III. ARGUMENTS FOR COVERAGE IN THE ABSENCE OF PHYSICAL DAMAGE

Despite these cases dismissing claims of affected policyholders due to lack of physical damage, case law does exist supporting the inventive argument “non-altering” physical damage is present at the insured premises if there is “contamination” at the location, even if the contamination does not physical cause property damage.

A. TEMPORARY CONDITIONS TRIGGERING COVERAGE

For example, in *Gregory Packaging Inc. v. Travelers Prop. Cas. Co. of Am.*, 2014 U.S. Dist. Lexis 165232 (D. N.J., November 25, 2019), a federal district court in New Jersey held that a release of unsafe amount of ammonia in a facility amounted to a “direct physical loss”. That court held property can sustain a physical loss or damage without experiencing structural alteration, and in *Wakefern Food Corp. v. Liberty Mut. Fire Ins. Co.*, 406 N.J. Sup. 524 (N.J. App. Div. 2009), the Court held that property can be “just temporarily unfit” and trigger coverage so the business interruption claim was allowed to proceed.

The *Wakefern Food Corp.* court’s reasoning should be of particular interest to those in the food service industries, as restaurant employees are the most severely affected by business shutdowns from COVID-19, with hair and nail salons, hotels, gymnasiums and entertainment venues such as theaters and sporting events similarly affected.

Mississippi’s casinos have been given a reopening date of May 21, after being closed by governmental decree for roughly two months. Walt Disney Co. and Universal Studios parks in Florida are gradually reopening in May and in Las Vegas, companies have announced staged plans pointing toward plans to reopen in by summer of 2020, demonstrating the conditions disrupting the business operations were at best temporary but the change in operations when reopening occurs do not suggest a return to “business as usual.” Whether and when the ways people interacted before March of 2020 will ever return is a matter of speculation and disagreement.

B. POST COVID-19 ISO ENDORSEMENTS

Even when governmental shutdown orders close the businesses of insured policyholders, traditional business interruption coverage sections on policies usually still require the trigger of a physical damage or loss. However, it has been reported that the Insurance Services Office (“ISO”) has responded to the COVID-19 outbreak by issuing endorsements for the use with commercial property forms that do not condition coverage upon direct physical loss or damage to property. The ISO forms provide limitation business interruption coverage due to actions taken by civil authorities to avoid or limit infection or spread by COVID-19. The two ISO forms have been described as “business interruption, limited coverage for certain

civil authority orders relating to coronavirus” and “business interruption, limited coverage for certain civil authority orders relating to coronavirus (including orders restricting some modes of public transportation)”, respectively. These forms reportedly also include certain exclusions and should be carefully reviewed.

Prior to the ISO form endorsement described above, the commentary on COVID-19 business interruption insurance coverages focused upon the 2006 ISO Form-Virus Exclusion.

ISO Form CP 01 40 07 06 is entitled “Exclusion for Loss Due to Virus or Bacteria” and provides “. . . we 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 stress, illness or disease... the exclusion goes on to state that it applies among other things to business income and it is reportedly found in many first party property insurance policies since 2006.

C. REASONABLE EXPECTATIONS DOCTRINE

But even in the face of such an apparently clear exclusion for business interruption due to a virus pandemic, there have been suggestions that such an exclusion may be avoided either by arguing that the governmental closure order is the cause of the damage and not the contamination by the virus or by arguing the “reasonable expectations” doctrine, adopted in

Mississippi in the case of *Bland v. Bland*, 629 So.2d 582 (Miss. 1993), as follows: “The objectively reasonable expectations of applicants and intended beneficiaries regarding the terms of insurance contracts will be honored even though painstaking study of the policy provisions would have negated those expectations.” *Id.* at 589 (citing Keeton, *Insurance Law Rights at Variance With Policy Provisions*, 83 Harv.L.Rev. 961, 967 (1970)). The *Bland* decision has not been often cited in Mississippi in the years following its publication but it is noted that more recent court opinions have required a finding that the policy be ambiguous as a condition precedent to invoking the “reasonable expectations” doctrine. *WW Holdings, LLC v. ACE Am. Ins. Co.* 574 Fed Appx. 383, 386 n.2 (E.D. La. 2014). Other states have analyzed factual scenarios wherein a discussion was held between an agent and a prospective policyholder over insurance coverage and where both an ambiguity exists in the contract and the agent’s representations created a misconception regarding coverage in the policy, the reasonable expectations doctrine could provide an avenue for recovery. *Talbot 2002 Underwriting Capital, Ltd. V. Old White Charities, Inc.*, 2016 U.S. Dist. LEXIS 52088 (S.D. W.Va April 19, 2016) (citing *Casto v. Northwestern Mut. Life Ins. Co.*, 2009 U.S Dist LEXIS 79385 (S.D. W. Va. Sept. 2, 2009).

D. ARE ALLERGENS POLLUTANTS?

It is also possible that pollution exclusion endorsements in policies might provide a basis for arguments as to coverage. However, in *Westport Ins. Corp. vs. VN Hotel Group, LLC*, 761 F. Supp. 1337 (M.D. Florida 2010)⁴ the court held legionella bacteria are not pollutants and thus found the policy exclusion did not apply and in *Johnson v. Clarendon National Insurance Company*, 2009 Cal App. Unpub. LEXIS 972, 2009 WL 252619, (Cal. 4th DCA February 4, 2009) a court held that a pollution exclusion did not apply to mold and “likely would not apply to viral infections” because the court reasoned that the language of the pollution exclusion was unclear and would be interpreted in favor of coverage. In *First Specialty Insurance Corp. v. GRS Management, Inc.*, 2009 W.L. 254613 (S. D. Fla. 2009) the federal district court held that the virus was a pollutant.

The specific ISO Form “exclusion for loss due to virus or bacteria” provides that “we 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...” the ISO circular dated July 6, 2006 used as part of its filings with State Regulatory Authorities refers to rotavirus, SARS, influenza (such as avian flu), legionella, and anthrax.

⁴ Affirmed on appeal, *Westport Ins. Corp. v. VN Hotel Group, LLC*, 513 Fed. Appx. 927 (11th Cir. 2013).

The ISO Form CP 00 30 10 12 entitled “Business Income (and Extra Expense) Coverage Form provides that the insurer will pay for the actual loss of business income sustained due to the necessary suspension of your operations during the period of restoration. The suspension must be caused by direct physical loss of or damage to property at premises which are described in the declarations and for which a business income limit of insurance is shown in the declarations. The loss or damage must be caused by or result from a covered cause of loss. With respect to loss of or damage to personal property in the open or personal property in a vehicle, the described premises include the area within 100 feet of such premises”.

ISO Form PROP 12 19 09 17 entitled Ordinance or Law Coverage includes the provision that “coverage under this endorsement applies only if a.) the building sustains only direct physical damage that is covered under this policy and is a result of such damage you are required to comply with the ordinance or law...”

IV. CURRENT LITIGATION

Subsequent to the closure of restaurants in the United States due to the COVID-19 pandemic, in lawsuits filed in New Orleans, *Cajun Conti, LLC v. Certain Underwriters at Lloyds*, Civil District Court, Orleans Parish, and Napa County, California, *French Laundry Restaurants d/b/a French Laundry, et al v. Hartford Fire Insurance Co.*, the policy holders have asserted the respective

governmental closure orders and the contamination of the premises by the virus provide a basis for coverage, regardless of any limitations or exclusions in the policy language. Likewise, lawsuits filed by the Chickasaw and Choctaw Nations in Oklahoma against their insurers for business interruption coverage and seeking declaratory judgment of the tribe’s casinos and other business which were shut down and impacted in light of the Covid 19 panic are covered claims notwithstanding under the business interruption provisions regarding orders of civil authorities.

From mid-April to present, most new lawsuits filed have been putative class actions with requests to consolidate federal cases for MDL in Chicago, Miami and Philadelphia.

V. CURRENT LEGISLATION

Finally, legislative actions in various states affecting insurance coverage received lavish media attention but have subsequently failed to gain traction to become enacted into law. The New Jersey legislature introduced a bill (A.B. 3844) to force insurers to pay COVID-19 business interruption claims despite the ISO Form Virus Exclusion used in the policies issued to the insureds in that state with businesses of less than 100 employees. The proposed legislation contains language to the effect that “notwithstanding the provision of any other law, rule, or regulation to the contrary insuring against loss or damage to property which includes the loss or use of occupancy

of business interruption enforced in this state...shall be construed” to include coverage for COVID-19 business interruption losses. Similar legislation has been introduced during the month of March in other states including Ohio, Massachusetts, New York, and Louisiana, and in April, Pennsylvania, South Carolina and Michigan but despite the fanfare with which such bills were announced, none of the bills have made much headway in their respective state legislatures. The first such bill, introduced in New Jersey and discussed above, was withdrawn in the month of March without a vote. In mid-May, the Louisiana bill died in committee.

At the federal level, H.R. 6494, proposed by California Representative Michael Thompson mandates business interruption coverage for viral pandemics or other forced business closures and/or mandatory evacuations under current existing insurance policies. Any such bills that make it into law will be subject to challenges to their constitutionality as ex post facto laws or otherwise in violation of Article One, Section 10 of the United States Constitution, prohibiting state laws impairing the obligation of contracts.

VI. CONCLUSION

All eyes are focused on how courts will respond to arguments that business interruption coverage should provide relief to policyholders whose businesses were forced to close due to the COVID-19 pandemic. The policy language requirement

of physical damage as a pre-requisite to coverage is being challenged in numerous ways by affected business owners and governmental entities. Application of the reasonable expectations doctrine to create coverage where none exists in the policy requires at a minimum the finding of an ambiguity in the policy as a matter of law and in some states, additional proof of misrepresentations by the agent in discussing specifics of coverage. While efforts to enact legislation forcing insurance coverage under existing policies containing exclusions may be fizzling, class action lawsuits pending in numerous states will exert pressure on insurance companies. The outcome of these efforts, initiatives and lawsuits is uncertain at this time but as the precedents set forth above illustrate, outcomes may vary, at least in the short term.

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