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LAW ALERT

THE PANDEMIC—INSURED OR NOT? KEY ISSUES

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The pandemic has brought increased scrutiny to the business interruption and civil authority coverages in the property policies of many businesses, public entities and nonprofits. The central issues relating to whether the policies provide coverage for losses sustained as a result of pandemic shutdowns are unresolved—and hotly contested. As detailed below, insureds and insurers inside and outside California are litigating whether any coverage exists for the dramatic income losses caused by governmental shelter-in-place orders. Do not assume that there is no coverage—many of the coverage issues are unresolved. The following is a discussion of just a few of the many key issues involved in obtaining insurance for pandemic-related losses.

A starting principle in any insurance analysis is to read all parts of the policy, including all endorsements, extremely carefully. Insurance policies are contracts, to which the fundamental principles of contract interpretation apply. The plain meaning of contract provisions controls; generally speaking, ambiguities are resolved in a way that protects the reasonable expectations of insureds. Although insurance contracts are often written on standard forms issued by the Insurance Services Office, Inc. (ISO), there are dramatic differences among the business interruption and civil authority coverages for different insureds, even when written by the same insurer. And, coverage that appears to exist in the main policy form may be severely curtailed by an endorsement appearing deep in the policy.

It is also critical to obtain and review the policy that was in effect when pandemic losses began—for many insureds, in March 2020.

There can be drastic differences in the business interruptions, virus and civil authority coverages from year to year—so be sure you're looking at the right policy year. Finally, when making a claim, be sure to document every aspect of a claimed loss very thoroughly, and submit all documentation to the insurer promptly. Policies routinely state that the insurer should be notified as soon as possible after the insured knows of the loss. Many policies also contain a contractual statute of limitations; the policy should be reviewed carefully to determine the deadline for making a claim.

BUSINESS INTERRUPTIONS COVERAGE: A typical business interruptions clause states that the insurer will pay for loss of business income sustained during a necessary suspension of operations. Most policies state that the suspension must be the result of "direct physical loss of *or* physical damage to" property at the insured premises—and must be caused by a covered cause of loss. For many property policies, called "all-risk" policies, "covered causes of loss" are all causes, unless specifically excluded. So, the policy should be carefully reviewed to see if pandemics, epidemics or viruses are excluded. Even if not, to be covered, they must result in "direct physical loss of *or* physical damage to property." The phrase is usually not defined—and therein lies the controversy.

Many courts have *not* required that the loss involve structural damage to be covered by insurance. Insureds argue that the virus constitutes direct physical loss or physical damage to property, analogizing to situations where, for example, ammonia or methamphetamine fumes were held to

constitute direct physical loss to property covered by insurance. Although one cannot see it, the virus is certainly "physical." Under California law one may look to the dictionary definition of an undefined policy term. Webster's defines "loss" as, among other things, "the state of being deprived or of being without something that one has had"—a definition that seems to apply to loss of access to a workplace.

Conversely, insurers argue that a workplace's contamination by a virus simply does not meet any reasonable definition of "*direct* physical loss of or physical damage to" property—especially when, as in most cases, there is no evidence of actual contamination.

As detailed below, the issue of whether known or suspected virus contamination is enough to trigger business interruptions coverage is before several California courts right now.

CIVIL AUTHORITY COVERAGE: Property policies also often contain coverage for loss of income when access to the insured premises is specifically prohibited by order of a civil authority as a direct result of a covered cause of loss. Governmental shelter-in-place orders arguably qualify. Again, if the policy is an "all-risk" policy, then all causes of loss are covered, unless specifically excluded. So, the existence of a pandemic, epidemic or virus exclusion in the policy is key—but, as explained below, not necessarily the end of the story.

Many, but not all, policies require that the action of the civil authority be linked to direct physical loss of or physical damage to property. The policy should be reviewed carefully to determine whether the civil authority coverage also includes the requirement of direct physical loss or damage.

EXTRA EXPENSE COVERAGE: A companion to business interruptions coverage is coverage for "extra expense," typically defined to mean expenses incurred to avoid or minimize losses and continue operations while the insured's regular place of operations is shut down. This usually includes relocation expenses and the cost to equip and operate the business at a temporary location. Many policies contain this valuable benefit.

VIRUS AND PANDEMIC EXCLUSIONS: Many, but not all, policies exclude coverage for virus, epidemics or pandemics. In pending litigation, however, creative insureds' counsel are arguing that, based on California's complex principles of "concurrent causation," if the efficient proximate cause of the loss is the governmental shutdown order and not the virus, then there is still coverage, because the *primary* cause of the loss is not excluded. Under California law, the fact that an excluded cause contributes to the loss is not always determinative; rather, if the "efficient and proximate" cause of the loss is covered, then the policy may have to respond to the claim, even if some other cause is excluded.

LIMITED VIRUS COVERAGE: Rather than excluding virus claims, there is a common endorsement on the market which provides limited coverage for fungi, bacteria or viruses. Many property policies contain this limited coverage. It is typically capped, however, at a low dollar amount; \$25,000 or \$50,000 of limited virus coverage is not uncommon. Here as well, insureds are arguing that if the efficient, proximate cause of the loss is not the virus but rather the governmental shelter-in-place orders, the low limit should not apply.

CASES TO WATCH: In *Friends of DeVito v. Wolf* (__ A.3d __, 2020 WL 1847100 (Pa. 2020)), the Pennsylvania Supreme Court held that Governor Wolf had statutory authority to issue Pennsylvania's governmental order because coronavirus is "by all definitions, a natural disaster" required to authorize the Governor's emergency powers, similar to other casualty events like earthquakes, fires, or tornados. The Court also held that, given the nature of the virus and manner of transmission, the disaster area was "any location... where two or more people can congregate," and that confirmation of the presence of a virus was not necessary given its exponential spread. While the Court was not specifically addressing policyholders' claims, the Court's decision that coronavirus was a natural disaster with an expansive disaster area bolsters policyholders' arguments that coronavirus constitutes physical damage.

In *French Laundry Partners v. Hartford* (Napa County Superior Court), Thomas Keller, the owner of the Michelin-starred French Laundry restaurant, is

seeking declaratory relief against Hartford Insurance Company, arguing that Hartford covers civil authority closures due to physical loss or damage from the coronavirus. The restaurant has an all-risk policy, with Business Income, Civil Authority and Extra Expense coverage, and a coverage extension for direct physical loss or damage caused by virus. The plaintiff alleges that coronavirus is a cause of actual physical loss and damage because it stays on surfaces and makes them dangerous. The plaintiff relies upon Napa County's shelter-in-place order, which refers to physical damage to property as a reason for the shelter in place.

In *Marc Fisher v. Hartford* (Los Angeles County Superior Court No. 20PSCV00256), the plaintiff, which designs and manufactures footwear, has an all-risk policy with loss of Business Income, Civil Authority and Extra Expense coverage. The plaintiff also has a Marine Policy with special coverage for landing, warehousing, transshipping, and other expenses, with no virus exclusion. The plaintiff claims that the Civil Authority and Dependent Property coverage does not require direct physical loss, but even if it did, it would be satisfied by loss of access and use of the property.

In *Scratch Restaurants v. Farmers* (Los Angeles County Superior Court No. 20STCP01233), the plaintiff owns and operates three restaurants and has a policy with Civil Authority coverage. The plaintiff is seeking a declaratory judgment to determine whether the order triggers Civil Authority coverage if the plaintiff proves there has been physical loss and damage.

In *Travelers Casualty Insurance Company v. Geragos* (U.S. District Court, Central District of CA No. 2:20-

CV-03619), Travelers Insurance Company is asking the court to decide that it has no obligation to provide coverage to Geragos & Geragos, a law firm, which made claims for loss of business income due to governmental orders and court closures. Without reference to exclusions, Travelers argues that the virus does not constitute "direct physical loss or damage" and the presence of coronavirus on surfaces causes no physical damage. Moreover, the policies issued to Geragos contain an Exclusion of Loss due to Virus or Bacteria, excluding "loss or damage caused by or resulting from any virus... capable of inducing physical distress..." and make clear that this exclusion applies to "forms or endorsements that cover business income, extra expense, rental value or action of civil authority." Travelers argues the government orders were not due to physical loss or damage, and suspension of business was not caused by direct physical loss.

Courts are also grappling with issues arising under workers compensation law; specifically, whether an employee who contracts COVID-19 is eligible for workers compensation benefits when there is no direct evidence that the exposure occurred during the course and scope of employment. Governmental executive orders, which can appear to create a presumption that a worker who contracts the virus did so on the job, will have a direct bearing on the coverage question.

In sum, coverage for pandemic-related losses is a complex and developing area of the law. The courts are about to decide whether the insurance industry must respond to multi-billions of dollars of losses caused by COVID-19.

For more information on these issues, please contact Dolores Bastian Dalton, Katie Dahlinghaus, or any other attorney at Goldfarb & Lipman.

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