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COVID-19 Business Interruption Coverage: A Policyholder's Perspective

As in other high-stakes coverage litigation, some insurers can be expected to advance innumerable arguments concerning limits, exclusions or other terms, pushing off the day of reckoning as long as possible, says Hunton Andrews Kurth's Scott DeVries and Lorelie Masters.

By **Scott DeVries and Lorelie Masters**

Nearly 20 million Americans have lost their jobs because of the COVID-19 pandemic. Many have lost their health care.

In a last-ditch attempt to survive, and to protect their employees' jobs and health benefits, policyholders have looked to their "all risk" property policies. But insurers have routinely rejected these claims—often with no investigation.

Lawsuits have been filed—a lot of them—the number approaching 1,000. Plaintiffs lawyers have styled many of these as class actions. They also have sought to consolidate all federal cases into a single MDL; the Judicial Panel on Multidistrict Litigation has rejected this request (with one small exception).

Insurers routinely move to dismiss, and when successful they breathlessly trumpet the decisions and mass-distribute updated scorecards of "wins" and "losses." However, many of the decisions are pleading-dependent or misread the law. Further, the scorecard concept demonstrates a fundamental misappreciation of legal principles and misreads policy wording.

The core fallacy in many decisions is that the phrase "direct physical loss or damage" is binary. Either policyholders' construction is "correct" or insurers' construction is "correct." This approach has led judges to believe there is only one meaning and they must choose. This is a false choice—the issue is whether policyholder's construction is reasonable. Unfortunately, this foundational determination tends to get lost in the binary "who is right" discussion.

Direct Physical Loss of/Damage to

- **Loss or damage.** First up in these cases has been the standard form "direct physical loss of or damage to" property wording (with slight variations). Policyholders argue that COVID-19 in air on or near insured property causes the requisite loss or damage and in any event, physical damage is not needed. Insurers reply that policyholders have not sufficiently alleged permanent damage to the infrastructure, and COVID-19 did not directly cause the business interruption expense.

Most decisions fail to engage in a true analysis of the critical policy terms. They focus on the term "damage," holding policyholders have not adequately pleaded damage. Since chemicals, smoke or odor in air on property are typically held to constitute "damage" to property, it follows that if properly pleaded, this element should be deemed satisfied.

Fewer of the decisions focus on the term "loss." Since every word in a contract must be given a unique meaning, the use of the disjunctive "or" means there is coverage where there is "loss" or "damage" and "loss" must mean something different than "damage." Courts routinely construe "loss" to describe the policyholder being deprived of the use of property, using standards such as "loss of functionality for intended purpose," "inaccessibility" or "property being stolen or lost in transit." Examples include inability to use an insured location because of a threat of a future rockfall or accumulation of gasoline nearby. This concept was adopted in *Total Intermodal Services v. Travelers Property Casualty* (C.D. Cal.), a case cited in several COVID-19 cases. While the courts correctly reference it, they erroneously read it to require loss be permanent. While permanence may affect the total measure of the deprivation, it wouldn't affect the loss sustained during the period of inaccessibility.

To emphasize, where reasonable, the policyholder's construction is to be applied.

- **Direct.**

Insurers argue that the pandemic must "directly" cause the injury. But, they say, here, the governmental orders break the causal link. However "direct" does not have the narrow limiting effect insurers allege. It is a flexible and expansive concept akin to proximate cause. As one case put it, "the law in this regard is so settled that the citation of authorities in support of the proposition would be unnecessary." Whether it be the COVID-19 virus, the pandemic and/or the order, the requisite "directness" is present. At a minimum, there is more than one reasonable interpretation, and, like other issues of proximate cause, it ultimately would be an issue for the trier of fact.

- **Physical.**

Insurers say "physical" modifies both "loss" and "damage," requiring damage to physical infrastructure. This effectively makes the terms synonymous and violates the requirement that every term have a unique meaning. "Physical" still has a meaning in the "loss" context—the virus has a physical mass, it has spread everywhere (explaining the widespread governmental orders), and the property whose use has been lost unquestionably is physical. (This presence of physicality explains why courts are wrong to rely on *Ward*, a data case, where a California appellate court accepted the minority view that data is not physical.)

Other Factors That Support Policyholders' Interpretation

- **The 2006 ISO pandemic exclusion.**

In 2006, the Insurance Services Office prepared, for general insurance industry use, a standard virus exclusion. The fact that the insurance industry form drafting arm believed there was a need to craft this exclusion corroborates the view that the policy grants coverage for this sort of loss. Why create an exclusion if something is already outside the scope of coverage as insurers now say?

Cases From Other Jurisdictions Can Establish Reasonableness

While a court is not bound by decisions in other jurisdictions, the fact that other judges have construed a term a certain way supports the reasonableness of that view. Insurers often embrace this principle when defending their own conduct in bad-faith cases.

This principle belies the score carding. The number of cases insurers win is irrelevant. What matters are the cases siding with policyholders, cases such as *Studio 417 v. Cincinnati Insurance* (W.D. Missouri) and *Urogynecology Specialist of Florida v. Sentinel Insurance*, that are conclusive on the reasonableness of policyholders' position.

So far, one California trial court has spoken (the case is now on appeal), as have multiple federal district courts (although these ultimately will look to the California appellate courts). Appellate resolution of the "loss or damage" issue may drive settlement of many cases. But, as in other high-stakes coverage litigation, some insurers can be expected to advance innumerable arguments concerning limits, exclusions or other terms, pushing off the day of reckoning as long as possible.

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