The appeal of COVID-19 business interruption appeals

Reuters

July 9, 2021 – More than one year has passed since the start of the COVID-19 global pandemic. According to the Centers for Disease Control, COVID-19 has infected more than 33 million people in the United States and more than 600,000 have died.

Also in that time, hundreds of thousands of stateside businesses have careened into economic despair, and in many cases have had no choice but to file for bankruptcy protection. Policyholders have called and continue to call on their business interruption insurance policies to respond to pandemic-related losses. Trillions are at stake.

More than 1,900 lawsuits have been filed, according to data compiled by the University of Pennsylvania Carey Law School. Key battleground areas include whether there is direct physical loss or damage to property and whether virus exclusions are enforceable and eliminate coverage. Of the roughly 1,900 filed, less than a quarter have been decided. Of those decided, 188 or nearly 40% are currently up on appeal.

Appeals remain pending in 13 state courts: California, District of Columbia, Florida, Illinois, Indiana, Massachusetts, Michigan, New Jersey, New York, Ohio, Oklahoma, Pennsylvania and Wisconsin. No state appellate court has yet rendered a decision. Only one federal appellate court, the 8th U.S. Circuit Court of Appeals in Oral Surgeons v. Cincinnati Insurance, has issued a ruling.

The Eighth Circuit affirmed the Iowa district court's decision to dismiss the insured's complaint, reasoning that dismissal was warranted where the policy required direct "accidental physical loss or accidental physical damage" and the complaint did not allege any physical alteration of property. The complaint, rather, only pled "generally that Oral Surgeons suspended non-emergency procedures due to the COVID-19 pandemic and the related government-imposed restrictions."

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Given the particular policy language, allegations of that complaint, and lack of a “physical alteration” requirement under the law of most states, the decision is not expected to have a significant impact (if any) on pending appeals.

Although new COVID-19 business interruption filings and trial court rulings will continue capturing headlines well into the balance of this year and beyond, decisions from appellate courts are expected to be a welcome reprieve for policyholders seeking clarity in this sea of uncertainty. Why? Because as courts of last resort, the appellate courts will ultimately shape the law on coverage for COVID-19 business interruption losses.

Here are five appeals to keep an eye on:

The early state appeal

As the second earliest filed state appeal, Inns by the Sea v. California Mutual Insurance is positioned to impact many affected businesses. On Sept. 8, 2020, the policyholder, a hotel owner and operator, appealed the lower court’s grant of the insurer’s demurrer without leave to amend.

Although oral argument has yet to be scheduled, the appeal is fully briefed. Amicus curiae briefs have been filed, including one by the authors’ firm on behalf of United Policyholders in support of Inns by the Sea.

The crux of the dispute is whether direct physical loss or damage to property is sufficiently alleged. The California Court of Appeal has been tasked with answering the following two questions:

•Does the insuring agreement affording coverage for “direct physical loss of or damage to” property require a showing of “physical alteration” to real property?

•Are allegations that property has become unsafe for its intended use due to the physical presence of COVID-19 sufficient to allege “direct physical loss of or damage to” property for purposes of a demurrer?

A favorable decision for the policyholder will result should the appellate court answer the first question negatively and the second question affirmatively.

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The merits appeal

In one of the first appeals of a favorable merits determination for policyholders, stakeholders continue to track the Choctaw Nation v. Lexington appeal closely. Granting summary judgment in favor of the policyholders, the Choctaw Nation, the Oklahoma District Court ruled that the Nation's business closures due to the pandemic constitute a covered "direct physical loss" under the policies.

The court concluded "direct physical loss" includes property rendered unusable for its intended purpose and that physical alteration of property is not required.

The virus exclusions in the policies, the court further held, do not "contemplate pandemics, or suspected, imminent, threatened, or fear of viruses — common language utilized by carriers to exclude such losses clearly and distinctively." Accordingly, the exclusions did not "clearly and distinctly" apply to the Nation's loss. Finally, the court concluded that a loss of use exclusion did not eliminate coverage.

The insurers appealed to the Supreme Court of the State of Oklahoma on March 16 and 17, 2021. Choctaw Nation responded to the insurers' petitions in error on April 6, 2021.

The virus exclusion appeals

The enforceability and applicability of virus exclusions are a central focus in several other early state appeals, including those pending in Michigan and Ohio.

In the very first COVID business interruption decision, a Michigan Circuit Court in Gavrilides Management Company v. Michigan Insurance Company dismissed the policyholder-restaurants' complaint without leave to amend. The court's ruling centered on whether the pleading alleged direct physical loss of or damage to property, although the court also stated in passing that the policy's virus exclusion would apply.

The policyholders initiated an appeal on Aug. 4, 2020. Briefing was complete as of Feb. 16, 2021. Amicus curiae briefs were filed, including one by the authors' firm on behalf of United Policyholders in support of the policyholders.

Also being closely monitored is an Ohio appeal in Nail Nook v. Hiscox Insurance. On March 5, 2021, the

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policyholder, a nail salon, initiated an appeal after the trial court granted the carrier's motion for judgment on the pleadings. Ruling that a virus exclusion clearly and unambiguously barred coverage, the court concluded the policyholder "can prove no set of facts that would entitle it to coverage under the policy for loss or damage caused by the coronavirus, as alleged."

The policyholder filed its initial brief in Ohio's Eighth District Court of Appeals on April 14, 2021. The insurer submitted its response brief on May 4, 2021.

One of the first heard

With oral argument scheduled for Aug. 11, 2021, the second COVID business interruption appellate decision will almost certainly be issued by the 9th U.S. Circuit Court of Appeals in Mudpie v. Travelers. The policyholder, a retailer, initiated its appeal on Sept. 24, 2020, after the Northern District of California dismissed its complaint.

The outcome of Mudpie v. Travelers is highly anticipated by policyholders and insurers alike.

The authors' firm filed briefs on behalf of amicus curiae in two cases discussed in this article.

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