New York Supreme Court
APPELLATE DIVISION—SECOND DEPARTMENT

SPORTIME CLUBS, LLC,

Plaintiff-Appellant,

—against—

AMERICAN HOME ASSURANCE COMPANY,

Defendants-Respondent.

UNITED POLICYHOLDERS' BRIEF AS AMICUS CURIAE IN SUPPORT OF APPELLANT

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INTEREST OF AMICUS CURIAE

United Policyholders ("UP") is a highly respected non-profit 501(c)(3) organization. Since its founding in 1991, UP has been a dedicated advocate and information resource for individual and commercial insurance consumers. UP assists consumers purchasing a policy or pursuing a claim. UP hosts a library of publications and videos related to personal and commercial insurance products, coverage, and the claims process at www.uphelp.org.

Grants, donations, and volunteers support UP's work, which is divided into three program areas: Roadmap to Recovery (disaster recovery and claim help), Roadmap to Preparedness (insurance and financial literacy and disaster preparedness), and Advocacy and Action (advancing pro-consumer laws and public policy). Public officials, state insurance regulators, academics and journalists routinely seek UP's input on insurance and legal matters. UP's Executive Director has been appointed to twelve consecutive terms as an official consumer representative to the National Association of Insurance Commissioners. In that role, UP works with regulators on matters related to policy sales, claims, and consumer rights. UP also serves on the Federal Advisory Committee on Insurance, which briefs the Federal Insurance Office and the Treasury Department.

On business interruption related to COVID-19, UP gave three separate NAIC presentations in 2020.[1] UP called attention to the uniform pattern of coverage denials (even where policy language differed and policies contained no virus or pandemic exclusion) by insurance companies nationwide, coupled with unsupported assertions that paying claims would bankrupt the insurance industry. UP also presented evidence that insurance companies were not candid with regulators about the significance of virus and pandemic-related limitations and exclusions they added to their policies.[2] Although insurance companies had paid business interruption claims stemming from the SARS CoV-1 outbreak, some told regulators they had never paid virus-related losses to justify not reducing rates when they added virus exclusions after the outbreak.

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[1] NAIC Special Session on COVID-19 Lessons Learned, https://content.naic.org/sites/default/files/national_meeting/speakerbios_covid-19_lessons_learned_summer_nm_2020_0.pdf; Testimony of Amy Bach on Business Interruption Policies and Claims, Summer National Meeting Property and Casualty Insurance (C) Committee August 12th, 2020, https://3inbm04c0p4j2h1w132uyb5e-wpengine.netdna-ssl.com/wp-content/uploads/2020/10/8-12-20_bach_c_committee_final_3.pdf; Testimony of Amy Bach on COVID-19 Related Business Interruption Claims, Coverage Issues, Disputes and Litigation, Summer National Meeting, Consumer Liaison Committee, August 14th, 2020, https://content.naic.org/sites/default/files/national_meeting/Version%202%20-%20Slideshow%20-%20Consumer%20Liaison%20Cmte%20-%2008.14.20.pdf.

[2] Richard P. Lewis *et al*., Here We Go Again: Virus Exclusion for COVID-19 and Insurers, NU PROP. CASUALTY 360 (Apr. 7, 2020), https://www.propertycasualty360.com/2020/04/07/here-we-go-again-virus exclusion-for-covid-19-and-insurers/?slreturn=20200927114442.

UP chooses cases cautiously and appears as *amicus curiae* nationwide. UP's briefs provide a counterweight to the claims of the insurance industry and facilitate evenhanded development of the law. UP has filed *amicus* briefs in federal and state courts across 42 states and in over 450 cases. Its briefs have been cited in the opinions of multiple state supreme courts as well as the U.S. Supreme Court.[3] UP has weighed in on important insurance issues in matters before New York courts.[4]

In this brief, UP seeks to fulfill the classic role of *amicus curiae*, supplementing the efforts of counsel and drawing the Court's attention to law that might otherwise escape consideration. Its commitment to advocating for policyholders during the pandemic has been vital. As commentators have stressed, an *amicus* is often in a superior position to "focus the court's attention on the broad

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[3] *See Humana Inc. v. Forsyth*, 525 U.S. 299, 314 (1999); *Sproull v. State Farm Fire & Cas. Co.*, 126446 (Ill. Sep. 23, 2021); *Julian v. Hartford Underwriters Ins. Co.*, 110 P.3d 903, 911 (Cal. 2005); *Cont'l Ins. Co. v. Honeywell Int'l, Inc.*, 188 A.3d 297, 322 (N.J. 2018); *Allstate Prop. & Cas. Ins. Co.v. Wolfe*, 105 A.3d 1181, 1185-6 (Pa. 2014).

[4] *See Keyspan Gas E. Corp. v. Munich Reinsurance Am., Inc.*, 73 N.Y.S.3d 113 (N.Y. 2018); *Universal American Corp. v. Nat'l Union Fire Ins. Co.*, 25 N.Y. 3d 675 (2015); *U.S. Fid.& Guar. Co. v. Am. Re-Insurance Co.*, 21 N.Y.3d 923 (2013); *Bi-Economy Mkt., Inc. v. Harleysville Ins. Co. of NY.*, 10 N.Y.3d 187 (2008); *U.S. Underwriters Ins. Co. v. City Club Hotel*, LLC, 3 N.Y.3d 592 (2004); *Belt Painting Corp. v. TIG Ins. Co.*, 100 N.Y.2d 377 (2003); *Consol. Edison Co. v. Allstate Ins. Co.*, 98 N.Y.2d 208 (2002*); Travelers Cas. and Sur. Co. v. Certain Underwriters at Lloyd's of London*, 96 N.Y.2d 583 (2001); *A-One Oil, Inc. v. Mass. Bay Ins. Co.*, 92 N.Y.2d 814 (1998); *Am. Home Assurance Co. v. Int'l Ins. Co.*, 90 N.Y.2d 433 (1997); *Town of Harrison v. Nat'l Union Fire Ins. Co. of Pittsburgh, Pa.*, 89 N.Y.2d 308 (1996).

implications of various possible rulings." R. Stern, E. Greggman & S. Shapiro, *Supreme Court Practice*, 570-71 (1986) (*quoting* Ennis, *Effective Amicus Briefs*, 33 Cath. U.L. Rev. 603, 608 (1984)).

PRELIMINARY STATEMENT

The Trial Court erred in dismissing the complaint filed by Plaintiff-Appellant Sportime Clubs, LLC ("Sportime") against Defendant-Respondent American Home Assurance Company ("AIG") pursuant to CPLR 3211(a)(1). The ruling disregards the controlling precedent of this Department, the plain language of the insurance policy AIG sold to Sportime (the "Policy"), Sportime's reasonable expectations of coverage, and the procedural law of New York. The ruling should be reversed for several reasons.

First, as argued by Appellant, the determination that there is no "physical loss or damage" without structural alteration[5] flies in the face of binding Second Department precedent. This Court has held that "damage" to property includes impairment of "function and value" and does *not* require "a distinct demonstrable alteration of the physical structure." *See Pepsico, Inc. v. Winterthur International American Insurance Company*, 24 A.D.3d 743 (2d Dep't 2005) ("*Pepsico II*"). The Trial Court erred by relying instead on a First Department ruling that it

[5] Opinion at p. 7, R. 10.

interpreted as holding the contrary. The precedent of this Department, not the First Department, controls.

Second, even if the Trial Court were free to disregard this Department's precedent (which it was not), and even if it interpreted the First Department case correctly (which it did not), the most it could have found was that the Policy is ambiguous. That fact, too, establishes coverage. Under settled New York law, ambiguous insurance policy provisions are interpreted "against the drafter" (*contra proferentem)*. The Trial Court's wholesale adoption of AIG's interpretation compromised the protections afforded to New York policyholders against insurance companies that build ambiguities into their policies. When AIG sold the Policy, it was well aware that courts for decades interpreted the policy language to cover functional impairment in the absence of structural alteration. If AIG did not intend that interpretation, it needed to spell that out. AIG did not do so. Thus, the Trial Court violated New York substantive law by reading that requirement into the Policy anyway, just as it violated New York procedural law when it disregarded the ambiguity and dismissed the case under CPLR 3211(a)(1).

Third, not letting cases like this one proceed beyond pleadings will seriously impair the insurance marketplace. Going forward, insurance coverage for numerous perils—fumes, odors, smoke and ash, toxic dust, and other damaging or deadly microscopic contaminants—will be called into question. This will not only

hurt policyholders who are unlucky enough to suffer atypical types of losses, it also will undermine the societal benefits of risk-spreading that are the bedrock of a well-functioning insurance marketplace.

Finally, reversal does not threaten the stability of AIG or other insurers. The insurance industry historically has *profited* from crises like Superstorm Sandy, Hurricane Katrina and other large-scale events. It is profiting from the pandemic already. For years, insurance companies have enjoyed the benefit of the premiums that Sportime and other policyholders paid for their policies. Now, they are using the pandemic to extract steep premium *increases* from customers—even while refusing to pay pandemic-related claims. Insurance companies are crying "wolf" when they claim that they could go bankrupt if there is coverage for COVID-related losses under certain policies. This Court should not be cowed by such inaccurate claims, which certainly have no place in determining the benefits owed under the insurance contract that AIG sold to Sportime.

UP respectfully urges this Court to achieve the interests of justice by reversing the ruling.

ARGUMENT

I. THE TRIAL COURT WAS WRONG TO HOLD THAT "PHYSICAL LOSS OR DAMAGE" REQUIRES STRUCTURAL ALTERATION.

Businesses pay premiums for policies that cover business interruption so that their properties can operate as designed and generate revenues. When property is

functionally impaired—whether from a fire or flood, or from noxious odors or the presence of a deadly virus—the loss or damage is the same. That is why this Court correctly held in *Pepsico II* that "physical damage" included non-dangerous molecular changes to soda, caused by faulty raw ingredients that resulted in an off-taste, and that thus substantially impaired "the product's function and value."[6] It rejected the claim that the policyholder needed to prove "'a distinct demonstrable alteration of the physical structure of the [policyholder's] products by an external source,' in other words, that the product has gone from good to bad."[7]

Impairment to functionality is well-established in New York as constituting "physical loss or damage" under property policies. For example, in *Trupo v. Preferred Mutual Insurance Company*, the Fourth Department found that "physical loss" included the contamination of a home by chemicals after an explosion.[8] In *Schlamm Stone & Dolan, LLP v. Seneca Insurance Co.*, the trial court found that "the presence of noxious particles, both in the air and on surfaces in plaintiff's premises, would constitute property damage under the policy's terms." [9] In *Hritz v. Saco,*[10] the trial court found that "physical loss" included the inability to use a

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[6] *See* 24 A.D.3d at 744.

[7] *Id.*

[8] 59 A.D.3d 1044, 1045 (4th Dep't 2009).

[9] 2005 WL 600021 at **3, 6 (N.Y. County Mar. 16, 2005).

[10] 18 A.D.3d 377, 378 (1st Dep't 2005) (holding that "mold" exclusion applied to

home due to "mold and mycotoxins" that triggered "severe allergic reactions." Other NY courts have held the same.[11]

Here, Sportime's pleading squarely alleged that a deadly virus impaired the functionality of its property and rendered it incapable of generating revenues.[12] Sportime is entitled to coverage for its losses, just as in the cases above.

A. Standard Policy Language and Decades of Decisions Confirm that Property Rendered Unfit for Its Intended Use Has Suffered "Physical Loss or Damage."

Where property is rendered unfit for its intended use—as by smoke from forest fires, toxic dust from nearby building collapses, or microscopic viruses that could kill inhabitants—policyholders are entitled to coverage even if property has

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eliminate this otherwise-covered physical loss).

[11] *See e.g., Siegel v. Chubb Corp.*, 33 A.D.3d 565, 566 (1st Dep't 2006) (mold was "efficient proximate cause" of loss, and thus mold exclusion applied to otherwise-covered physical loss). While many courts, including the Trial Court, cite *Roundabout Theatre Company v. Continental Casualty Company* as holding the contrary, that decision did not involve substantial allegations of damage to the insured property itself, so it does not support that interpretation. 302 A.D.2d 1, 6 (1st Dep't 2002) (framing the issue as whether the policy "provide[s] coverage for *off-site* property damage" (emphasis added).

[12] Among other things, Sportime alleged that "[c]ountless individuals, asymptomatic, pre-symptomatic, and otherwise, experienced the Insured Locations prior to the closure orders," (R. 28 (¶ 48); that "Sportime is indeed aware of customers and employees who tested positive for COVID-19," (R. 28 (¶ 49); and, with various references to emerging scientific understandings, that "the presence of SARS-CoV-2 in a building's airspace and on or around property constitutes 'direct physical loss or damage to property." R. 48–49 (¶ 117).

not been structurally altered.[13] This fact has been true for decades. During the 1950s,[14] the 1960s,[15] the 1970s,[16] the 1980s,[17] and the 1990s[18]—courts consistently have found such losses covered as "physical loss or damage."

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[13] *See, e.g., Gregory Packaging, Inc. v. Travelers Prop. Cas. Co.*, No. 2:12-cv-04418, 2014 WL 6675934, at *5-6 (D.N.J. Nov. 25, 2014) (concluding that "property can sustain physical loss or damage without experiencing structural alteration," that "the heightened ammonia levels rendered the facility unfit for occupancy until the ammonia could be dissipated," and therefore that the ammonia discharge caused direct physical loss or damage); *Oregon Shakespeare Festival Ass'n v. Great Am. Ins. Co.*, No. 1:15-cv-01932-CL, 2016 WL 3267247, at *5-6 (D. Or. June 7, 2016), *vacated by joint stipulation*, 2017 WL 1034203 (Mar. 6, 2017) (smoke from wildfires).

[14] *American Alliance Ins. Co. v. Keleket X-Ray Corp.*, 248 F.2d 920, 925 (6th Cir. 1957) (finding that the policyholder, which manufactured instruments used in measuring radioactivity, had suffered property damage from a release of radon dust and gas which made the building unsafe, and made it impossible to calibrate the instruments prior to sale because of background radiation).

[15] *Hughes v. Potomac Ins. Co.*, 18 Cal. Rptr. 650, 655 (Cal. App. 1962) (finding that the policyholder's home – which became perched on the edge of a cliff after a landslide deprived it of lateral support and stability – was damaged because it became unsafe to live in and was thus, useless); *W. Fire Ins. Co. v. First Presbyterian Church*, 437 P.2d 52, 54 (Colo. 1968) (en banc) (finding a "direct physical loss" where a church complied with the fire department's order to close because gasoline vapors made "use of the building dangerous").

[16] *Cyclops Corp. v. Home Ins. Co.*, 352 F. Supp. 931, 937 (W.D. Pa. 1973) (finding the policyholder entitled to coverage for loss of business income where vibration of motor, without apparent damage, caused the business to be shut down).

[17] *Hampton Foods, Inc. v. Aetna Cas. & Sur. Co.*, 787 F.2d 349, 352 (8th Cir. 1986) (finding the policyholder could claim business income coverage where risk of collapse necessitated abandonment of grocery store).

[18] In chronological order: *Hetrick v. Valley Mut. Ins Co.*, 15 Pa. D. & C. 4th 271, 1992 WL 524309, at *3 (Pa. Comm. Pl. May 28, 1992) (finding there would be coverage for loss of use of a house if an outside oil spill made the house uninhabitable); *Largent v. State Farm Fire & Cas. Co.*, 842 P.2d 445, 446 (Or.

App. 1992) (noting that insurance company conceded methamphetamine fumes could cause "accidental direct physical loss"); *Farmers Ins. Co. v. Trutanich*, 858 P.2d 1332, 1335 (Or. App. 1993) (finding costs of methamphetamine odor covered as direct physical loss or damage); *Azalea, Ltd. v. American States Ins. Co.*, 656 So. 2d 600, 602 (Fla. Dist. Ct. App. 1995) (finding damage to sewage treatment plant from chemicals that destroyed a bacteria colony necessary for the plant to operate amounted to "direct damage to the structure"); *Arbeiter v. Cambridge Mut. Fire Ins. Co.*, No. 9400837, 1996 WL 1250616, at *2 (Mass. Super. Mar. 15, 1996) (finding oil fumes present in house after discovery of oil leak constituted physical damage); *Sentinel Mgmt. Co. v. N.H. Ins. Co.*, 563 N.W.2d 296, 300 (Minn. Ct. App. 1997) (finding the presence of asbestos could constitute physical loss or damage); *Murray v. State Farm Fire & Cas. Co.*, 509 S.E.2d 1, 17 (W. Va. 1998) (finding a home rendered unlivable by falling rocks had suffered a "direct physical loss to the property"); *Shade Foods, Inc. v. Innovative Prods. Sales & Mktg., Inc.*, 78 Cal. App. 4th 847, 865 (2000) (holding that the intermingling of a quarter pound of wood shavings in 80,000 pounds of almonds caused physical loss or damage to the almonds even though the almonds were structurally unchanged); *Matzner v. Seaco Ins. Co.*, 9 Mass. L. Rptr. 41, 1998 WL 566658, at *4 (Mass. Super. Aug. 12, 1998) (concluding that "direct physical loss or damage" was ambiguous and could mean either "only tangible damage to the structure of insured property" or "more than tangible damage to the structure of insured property," and that "carbon monoxide contamination constitutes 'direct physical loss of or damage to' property"); *Columbiaknit, Inc. v. Affiliated FM Ins. Co.*, No. 98-434-HU, 1999 WL 619100, at *7-8 (D. Or. Aug. 4, 1999) (finding that policyholder could bear its burden to demonstrate that clothes containing mold or mildew suffered "direct physical loss or damage" if it established "at trial a class of garments which has increased microbial counts and that will, as a result, develop either an odor or mold or mildew"); *Board of Educ. v. International Ins. Co.*, 720 N.E.2d 622, 625-26 (Ill. App. 1999) (citing liability insurance coverage cases finding that incorporation of asbestos into buildings caused "property damage," defined under liability policies to be "physical injury to or destruction of tangible property").

These rulings continued into the 2000s,[19] when insurance companies paid claims for losses caused by a novel coronavirus, SARS-CoV-1.[20] Even after that outbreak, they continued to use "physical loss or damage" in their policies, and courts continued to find coverage for their business interruption losses in the absence of structural alteration.[21] The substantial precedent on this issue was

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[19] In chronological order: *Sentinel Mgmt. Co. v. Aetna Cas. & Sur. Co.*, 615 N.W.2d 819, 825-26 (Minn. 2000) (holding that "[a] principal function of any living space [is] to provide a safe environment for the occupants" and "[i]f rental property is contaminated by asbestos fibers and presents a health hazard to the tenants, its function is seriously impaired"); *Prudential Prop. & Cas. Ins. Co. v. Lillard-Roberts*, No. 01-1362, 2002 WL 31495830, at *8-*9 (D. Or. June 18, 2002) (concluding that mold damage to house could constitute "distinct and demonstrable" damage and that inability to inhabit a building may constitute "direct, physical loss"); *Cooper v. Travelers Indem. Co. of Ill.*, No. 01-cv-2400, 2002 WL 32775680, at *1 (N.D. Cal. Nov. 4, 2002) (holding that the presence of coliform bacteria and E.coli could constitute physical loss or damage); *Graff v. Allstate Ins. Co.*, 54 P.3d 1266, 1269 (Wash. Ct. App. 2002) (holding that the presence of methamphetamine vapors could constitute physical loss or damage).

[20] The coverage included a $16 million payout to one hotel chain, Mandarin Oriental International. Gavin Souter, Hotel Chain to get Payout for SARS-Related Losses, Nov. 02, 2003, https://www.businessinsurance.com/article/20031102/story/100013638/hotel-chain-to-get-payout-for-sars-related-losses.

[21] In chronological order: *Motorists Mut. Ins. Co. v. Hardinger*, 131 F. App'x 823, 824–27 (3d Cir. 2005) (holding that the presence of E. coli could constitute physical loss or damage); *De Laurentis v. United Servs. Auto. Ass'n*, 162 S.W.3d 714, 722-23 (Tex. App. Mar. 31, 2005) (finding mold damage constituted "physical loss to property"); *Schlamm*, 2005 WL at *4 (finding "the presence of noxious particles, both in the air and on surfaces of the plaintiff's premises, would constitute property damage under the terms of the policy"); *Cook v. Allstate Ins. Co.*, No. 48D02-0611-PL-01156, 2007 Ind. Super. LEXIS 32, at * slip op. at 9-10 (Ind. Super. Ct. Madison County Nov. 30, 2007) (finding infestation of house with brown recluse spiders constituted "sudden and accidental direct physical loss" to the house, and "[c]ase law demonstrates that a physical condition that

followed by courts nationwide for the next decade, leading up to the COVID-19 pandemic, including, of course, this Court's decision in *Pepsico II*.[22]

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renders property unsuitable for its intended use constitutes a 'direct physical loss' even where some utility remains and, in the case of a building, structural integrity remains"); *Brand Mgt., Inc. v. Maryland Cas. Co.*, No. 05-cv-02293, 2007 WL 1772063, at *2 (D. Colo. June 18, 2007) (noting that where a sushi manufacturer which closed for 15 days to disinfect its premises after discovery of listeria contamination, the insurance company voluntarily paid the business income claim); *Stack Metallurgical Servs., Inc. v. Travelers Indem. Co.*, No. 05-1315, 2007 WL 464715, at *8 (D. Or. Feb. 7, 2007) (finding "physical loss or damage" to a policyholder's heat treater for medical implants when a lead hammer was mistakenly left in the treater; noting that "[t]here is no question that the physical transformation of the furnace which rendered it useless for processing medical devices, the use for which it was specially certified, reduced both the value of the furnace and [the policyholder's] ability to derive business income from the furnace. This reduction of value was caused by an incident that is fairly characterized as 'direct physical damage'").

[22] In chronological order: *Wakefern Food Corp. v. Liberty Mut. Fire Ins. Co.*, 968 A.2d 724, 734 (N.J. Super. App. Div. 2009) ("In the context of this case, the electrical grid was 'physically damaged' because, due to a physical incident or series of incidents, the grid and its component generators and transmission lines were physically incapable of performing their essential function of providing electricity."); *Manpower Inc. v. Insurance Co. of the State of Pa.*, No. 08C0085, 2009 WL 3738099, at *1 (E.D. Wis. Nov. 3, 2009) (finding "direct physical loss … or damage to" a building adjacent to a building which collapsed despite the fact that the collapse did not cause any noticeable damage to the policyholder's occupied space); *Travco Ins. Co. v. Ward*, No. 2:10cv14, 2010 WL 2222255, at *8-9 (E.D. Va. June 3, 2010) (finding a house built with drywall manufactured in China, that emitted toxic gases, causing the policyholder to move out, had suffered direct physical loss, although it was "physically intact, functional and ha[d] no visible damage;" noting that the majority of cases nationwide find that "physical damage to the property is not necessary, at least where the building in question has been rendered unusable by physical forces"); *In re Chinese Mfr'd Drywall Prods. Liab. Litig.*, 759 F. Supp. 2d 822, 831 (E.D. La. 2010) (finding there "exists a covered physical loss" where "potentially injurious material" is "activated, for example by releases gases or fibers," and "that the presence of Chinese-

The insurance industry is well aware of these decisions. In fact, a trade organization that drafts policy language for the industry admitted that its responsibilities include monitoring such decisions and updating its forms and endorsements in response thereto.[23] Yet it never added a requirement of "structural alteration." Instead, it left the language unchanged, knowing that phrase has been interpreted by policyholders and courts alike not to require structural alteration. This history makes clear that AIG, like the rest of the insurance industry, never intended the requirement of structural alteration on which it now relies—and that it is unconscionable to read the Policy as if that language had been added.

B. Insurance Companies Admit and Argue that Events Rendering Property Unfit for Its Intended Use Cause "Physical Loss or Damage."

Prior to the pandemic, insurance companies freely admitted that coverage is triggered when property was rendered unfit for its intended use. Two prominent examples are discussed below.

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manufactured drywall in a home constitutes a physical loss" because it "renders the [policyholders'] homes useless and/or uninhabitable"); *Association of Apartment Owners of Imperial Plaza v. Fireman's Fund Ins. Co.*, 939 F. Supp. 2d 1059, 1068 (D. Haw. Apr. 9, 2013) (applying Hawai'i law) (finding intrusion of arsenic into roof caused "direct physical loss or damage" to the roof); *Gregory Packaging*, 2014 WL 6675934, at *5–6 (*see* n.7 *supra*); *Mellin v. Northern Sec. Ins. Co.*, 115 A.3d 799, 803-05 (N.H. 2015) (holding that pervasive odor of cat urine was "physical loss" to condominium); *Oregon Shakespeare Festival*, 2016 WL 3267247, at *5-6 (*see* n.7 *supra*).

[23] ISO Circular dated July 6, 2006 ("ISO Circular"), at 7 of 13 (Addendum 1).

1. Concessions in Regulatory Filings.

Evidence that structural alteration is not required to trigger coverage under property policies is found in statements that insurance companies have made when seeking approval of policy forms. In 2005, for example, the Greater New York Insurance Companies ("Greater NY") asked the New York State Insurance Department for permission to include a virus exclusion in its property policies. It proposed that the exclusion be optional, as many policyholders would want to continue having coverage for viruses.[24] Greater NY explained that such coverage would exist unless the exclusion was included, stating "our main object of this filing is to remove the carte blanch application of this Exclusion and not deny coverage to the majority portion of our book" for losses stemming from virus.[25] The admission that standard-form property policies using the "physical loss or damage" formulation cover "this type of loss ('pandemic')"[26] is exactly what AIG denied in this action and the Trial Court erroneously accepted as true.

Greater NY even admitted that its policyholders reasonably expect such coverage from their property policies:

> [W]e do not anticipate that any of our insureds will voluntarily request this [virus] exclusion; some (habitational risks) because it would never enter their minds as a problem for which they would voluntarily

[24] *See* Greater NY's Explanatory Memorandum, Addendum 2, p. 1. [25] *Id.*

[26] *Id.*

> reduce coverage; <u>others (restaurants) because they feel that such an event is well within the realm of possible fortuitous occurrences and should be covered should such an event arise</u>.[27]

The instant case demonstrates that Greater NY was correct, as Sportime's complaint makes clear that it expected coverage for the losses suffered when the pandemic shut down its operations.

2. <u>Concessions in Court Filings.</u>

Three months before the pandemic began, Factory Mutual Insurance Company ("Factory Mutual")—perhaps the most sophisticated property insurance company in the United States—filed a motion in the U.S. District Court for the District of New Mexico, arguing that "physical loss or damage" to property exists when the presence of a physical substance renders property unfit for its intended use, even when it does not cause structural alterations.[28]

At issue in *Factory Mutual Insurance Co. v. Federal Insurance Co.* was a mold infestation in a "clean room" at a drug manufacturing plant.[29] Mold and its spores, like SARS-CoV-2 virions, exist on the surface of property and in the air. Factory Mutual argued that the mold infestation constituted "physical loss or

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[27] *Id.* (emphasis added).

[28] Factory Mutual's Mot. *in Limine* No. 5 re Physical Loss or Damage, filed Nov. 19, 2019 in *Factory Mut. Ins. Co. v. Fed. Ins. Co.*, No. 1:17-cv-00760-GJF-LF (D.N.M.) (Addendum 3).

[29] *Id.* at 3.

damage" under a property policy sold by Federal Insurance Company ("Federal Insurance") because the mold "destroyed the aseptic environment and rendered [the clean room] unfit for its intended use."[30] It also asserted that case law "broadly interprets the term 'physical loss or damage' in such policies,"[31] relying upon many of the cases discussed above:

> Numerous courts have concluded that loss of functionality or reliability under similar circumstances constitutes physical loss or damage. *See, e.g., Western Fire Insurance Co. v. First Presbyterian Church*, 437 P.2d 52 (Colo. 1968) (church building sustained physical loss or damage when it was rendered uninhabitable and dangerous due to gasoline under the building); *Gregory Packaging, Inc. v. Travelers Property and Casualty Company of America*, Civ. No. 2:12-cv-04418 2014 U.S. Dist. LEXIS 165232, 2014 WL 6675934 (D. N.J. 2014) (unsafe levels of ammonia in the air inflicted "direct physical loss of or damage to" the juice packing facility "because the ammonia physically rendered the facility unusable for a period of time."); *Port Authority of N.Y. and N.J. v. Affiliated FM Ins. Co.*, 311 F.3d 226, 236 (3d Cir. 2002) (asbestos fibers); *Essex v. BloomSouth Flooring Corp.*, 562 F.3d 399, 406 (1st Cir. 2009) (unpleasant odor in home); *TRAVCO Ins. Co. v. Ward*, 715 F.Supp.2d 699, 709 (E.D. Va. 2010), *aff'd*, 504 F. App'x. 251 (4th Cir. 2013) ("toxic gases" released by defective drywall).[32]

According to Factory Mutual, the loss continued until the policyholder's customers viewed the property's use to be safe:

> The period of time as well as costs required to bring [the policyholder's] facility to the level of cleanliness following the mold infestation required by [the policyholder's] customers is also physical loss or damage covered by the Federal policy. The facility was damaged by

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[30] *Id.*

[31] *Id.*

[32] *Id.* at 3–4 (emphasis added).

> stringent requirements of [the policyholder's] customers regarding production to the same extent it was damaged from the mold infestation itself as the facility was unusable as the result of a covered loss. . . . Without the customers' approval of the restored aseptic conditions following the mold infestation, [the] facility remained unusable.[33]

Factory Mutual further argued that at the very least, its interpretation was reasonable, so even if Federal could propose an alternative, that merely would establish that "physical loss or damage" is ambiguous.[34] Since black-letter law requires ambiguities to be construed against the policy drafter, coverage would exist either way.

Ironically, no policyholder could have said it better. By making the exact argument that Sportime makes here, Factory Mutual put the lie to AIG's denial of coverage. The Trial Court's wholesale adoption of AIG's arguments about the meaning of "physical loss or damage" should be reversed.

II. THE TRIAL COURT VIOLATED CPLR 3211(a)(1) BY DISMISSING THE COMPLAINT WHEN THE POLICY LANGUAGE DID NOT UTTERLY REFUTE THE POSSIBILITY OF COVERAGE.

In dismissing the complaint, the Trial Court acknowledged, but failed to follow, the settled standard under CPLR 3211(a)(1):

> A motion to dismiss on the ground that an action is barred by documentary evidence (CPLR 3211 [a] [1]) may be appropriately granted only where the documents in question utterly refute plaintiff's factual allegations and conclusively establish a defense as a matter of law (*Goshen v. Mut. Life Ins. Co. of New York*, 98 NY2d 314, 326

[33] *Id.* at 4–5 (emphasis added).

[34] *See id.* at 3 n.1.

> [2002]). The court is expected to liberally construe the pleadings and accept the facts as alleged in the complaint as true, according plaintiffs the benefit of every favorable inference to ultimately determine only whether the alleged facts conform within any cognizable legal theory. (CPLR 3026; *See Leon v. Martinez*, 84 NY2d 83, 87-88 [1994]).

Opinion at p. 3, R. 6.

Dismissal is improper under CPLR 3211(a)(1) unless the policy provision at issue uses "clear and unmistakable language capable of no other reasonable interpretation." *Wright v. Evanston Ins. Co.*, 14 A.D.3d 505, 788 N.Y.S.2d 416 (2d Dep't 2005) (internal quotes omitted) (*citing Continental Cas. Co. v. Rapid-Am. Corp.*, 80 N.Y.2d 640, 652 (1993); *Belt Painting Corp. v. TIG Ins. Co.*, 100 N.Y.2d 377, 383 (2003)). Here, because the Policy is ambiguous, that standard could not be met. The dismissal also disregarded, and certainly failed to interpret in favor of Sportime as required, the extensive allegations in the complaint about the physical loss or damage caused by SARS-CoV-2. *See, e.g.*, R. 27-30, 37, 48-51; Appellant's Brief at 46–48.

Legal scholars and insurance law experts have sharply criticized courts for dismissing COVID-19 coverage cases before the facts have been developed. *See* Prof. Erik S. Knutsen and Prof. Jeffrey W. Stempel, *Infected Judgment: Problematic Rush to Conventional Wisdom and Insurance Coverage Denial in a Pandemic*, 27 CONN. INS. LAW J. 185, 192 (2020) (Addendum 4) ("Judges granting dismissal motions without any opportunity for discovery, and denying any

possibility of coverage at the metaphorical starting gate, have undermined the traditional American commitment to jury trials as well as widely accepted legal principles of insurance policy construction such as interpreting ambiguous terms against the drafter and considering policyholder reasonable expectations."). Most of these dismissals improperly rest upon factual presumptions that judges are not qualified to make. *See id.* at 193–94 ("Notwithstanding some shining exceptions, the first wave of decisions in these cases has been largely disappointing and reflects poorly on the legal and hyper-textual analysis of the bench.").

Many courts—especially state courts—are joining this chorus by denying motions to dismiss. For example, a state court in Illinois recently observed that too many courts are rushing to judgment on COVID-19 coverage disputes, blindly following inapposite decisions from other courts instead of focusing on the allegations before them:

> Economists refer to this as an appeal to "herding behavior"—a process by which group-think replaces individual decision-making. . . . Judges are not sheep, and I do not decide a case by counting noses. Further, the "herd" can be wrong. *See, e.g.*, A. Daughety et al., "Stampede to Judgment: Persuasive Influence and Herding Behavior by Courts," 1 American Law and Economics Review 158 (Fall 1999).

See JDS Construction Group, LLC, and 9 Dekalb Fee Owner LLC v. Continental Casualty Co., Case No. 2020 CH 5678, at 4 (Ill. Cir. Ct. Oct. 25, 2021). Similarly, a state court in Connecticut observed: "The rush to judgment on the question of physical damage in some courts—without reasoning and without evidence—has

been ill advised. For now, in this court, and for this policy, it would be wrong to rush." *New Castle Hotels LLC v. Zurich Am. Ins. Co.*, No. X07-HHD-CV-21-6142969-S, 2021 WL 4478669, at *3 (Conn. Super. Ct. Sept. 7, 2021) (Addendum 5).[35] That court took aim at the courts that adopt insurance company views without carefully considering the arguments and evidence:

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[35] *See also, e.g., MacMiles LLC v. Erie Ins. Exch.*, No. GD-20-007753, 2021 WL 3079941, at *5n. 12 (Pa. Com. Pl. May 25, 2021) (Addendum 6) ("merely accepting the non-binding decisions of other courts 'by the purely mechanical process of searching the nations courts for conflicting decisions' amounts to an abdication of this Court's judicial role"); *Ungarean v. CNA et al. No.: GD-20-006544, 2021 WL 1164836, at *6, n. 12, (Pa. Com. Pl. March 22, 2021)* (Addendum 7) (same); *Brown's Gym, Inc. v. The Cincinnati Ins. Co.*, No. 20 CV 3113, 2021 WL 3036545, at *19 (Pa. Com. Pl. July 13, 2021) ("State trial courts throughout the nation have agreed with the foregoing rationale articulated in the federal case law in denying insurers' attempts to dismiss business interruption insurance claims filed by insureds who assert that COVID-19 was present on their covered property"); *Goodwill Indus. of Orange Cnty., Cal. v. Philadelphia Indem. Ins. Co., No. 30-2020-01169032-CU-IC-CXC, 2021 WL 476268, at *3 (Cal. Super. Ct. Jan. 28, 2021* (Addendum 8) (stating that the Fecompany "are not binding on this court and were decided under a different standard" [compared to a motion to dismiss] and that unlike the insurance company's cases, the plaintiff did allege that the coronavirus and COVID-19 caused physical loss or damage to the property at issue, which allegations must be accepted as true); *Snoqualmie Entertainment Authority v. Affiliated FM Ins. Co., No. 21-2-03194-0 SEA, 2021 WL 4098938, at *6 (Wash. Super. Sep. 3, 2021)* ("This Court is not persuaded by [another judge's] reliance on the opinions of other federal district court opinions across the country that applied the laws of other states, nor its holding that the undefined phrase 'all-risks of physical loss or damage' cannot be reasonably interpreted by the average lay person to include the insured's inability to physically use, control, or manipulate its property as a result of the COVID-19 closure orders and Tribal resolutions"), *Boardwalk Ventures CA LLC v. Century-Nat'l Ins. Co., No. 20STCV27359, 2021 WL 1215892, at *3 (Cal. Super. Ct. Mar 18, 2021)* (rejecting the "litany of unpublished federal district court cases" cited by the insurance company "in support of the proposition

> Zurich claims that there is nothing "physical" about the losses or damage flowing from the COVID-19 virus. Zurich notes that some courts in other jurisdictions have addressed this issue – remarkably at the pleading stage – remarkably with little apparent deliberation. Yes, Zurich can cite decisions where courts agree with it. Some of them merely note that claimants haven't even alleged physical damage using the words "physical". Others go further. The virus damages lungs not property, they say.
>
> But can this merely be asserted to become true? Maybe this kind of result is the product of an expansive view of "plausibility" under the pleading standard adopted by the United States Supreme Court in *Bell Atlantic Corp. v. Twombly*. But Connecticut's standard prefers a ruling from the evidence rather than the gut.

New Castle Hotels, slip. op. (Addendum 5) at 5 (emphasis supplied).

Moreover, most cases cited by insurance companies improperly rest on an unsupported and erroneous entry in an insurance treatise. *See* Richard P. Lewis, Lorelie S. Masters, Scott D. Greenspan and Chris Kosak, *Couch's "Physical Alteration" Fallacy: Its Origins and Consequences* 56:3 TORT, TRIAL & INS. PRAC. L.J. 621 (Fall 2021) (Addendum 9). Commendably, this Court was not led astray by insurance company arguments based on that entry. *See Pepsico II*, 24 A.D.3d at

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that courts applying California law have 'uniformly dismissed lawsuits like the instant action'" – recognizing that these cases are not binding and the dismissal was not proper); *Risinger Holdings, LLC v. Sentinel Ins. Co., Ltd*., No. 1:20-CV-00176, 2021 WL 4520968, at *12 (E.D. Tex. Sept. 30, 2021) (holding that the policy's use of "physical loss" is ambiguous and concluding that the policyholder "may have suffered direct physical loss due to Governor Abbott's lockdown order by being deprived of the use or full use of the physical space of its covered property, or alternately, because of the severe material losses it endured when it was forcibly excluded from its businesses").

744 (rejecting the insurance company's contention "that to prove physical damages plaintiffs must prove that there has been a distinct demonstrable alteration of the physical structure of plaintiffs' products by an external force"). Indeed, nearly a decade after *Pepsico II* was handed down, an editor responsible for the erroneous entry published an article acknowledging the mistake. The article directly contradicted the treatise's conclusion that structural alteration was required, stating instead that "[t]he modern interpretive trend is liberalizing the meaning of direct physical loss to focus upon loss of use as opposed to direct physical loss involving physical alteration." Stephen Plitt, "Direct Physical Loss in All-Risk Policies: The Modern Trend Does Not Require Specific Physical Damage, Alteration" CLAIMS JOURNAL (Apr. 15, 2013), available at https://amp.claimsjournal.com/magazines/idea-exchange/2013/04/15/226666.htm (emphasis added).

The right to present evidence is a bedrock of our democracy that was denied to Sportime here based on factual assumptions that not only were false, but that the Trial Court was not entitled to make. Such dismissals threaten the rights of policyholders generally and should be reversed.

III. THE COURT SHOULD NOT BE DISTRACTED BY "CRIES OF WOLF" FROM AIG AND THE INSURANCE INDUSTRY.

At times of crisis, insurance companies are quick to argue that they could be forced into bankruptcy if they are forced to cover resulting claims. *See* J. Robert

Hunter, THE INSURANCE INDUSTRY'S INCREDIBLE DISAPPEARING WEATHER CATASTROPHE RISK: HOW INSURERS HAVE SHIFTED RISK AND COSTS ASSOCIATED WITH WEATHER CATASTROPHES TO CONSUMERS AND TAXPAYERS (Consumer Federation of America, Feb. 17, 2012), Addendum 10, at p. 1 ("industry data demonstrates that insurers have significantly and methodically decreased their financial responsibility for [catastrophic] events in recent years and shifted much of this risk to consumers and taxpayers. . . . most of these savings have been achieved by hollowing out the coverage in homeowners insurance policies and raising rates").

For thirty years, insurance companies attempted to color the discussion of environmental coverage by asserting that they would be rendered bankrupt if they are required to cover claims that arise from the strict liability environmental statute, CERCLA. In testimony before Congress, insurance representatives claimed that the cost of such clean-ups will be five times their total "surplus" and could be ruinous. *See Insurer Liability for Cleanup Costs of Hazardous Waste Sites*, No. 101-175 (101st Cong., 2d Sess., Sept. 27, 1990) (Committee on Banking, Finance, and Urban Affairs), pp. 18-29 and 75-76. Although the industry was held accountable for many such clean-ups, the predicted collapse never arrived.

In response to the COVID-19 pandemic, insurance companies are "crying wolf" yet again. Insurance industry trade associations repeatedly have asserted in

amicus briefs in COVID-19 cases that determinations in favor of coverage would bankrupt the industry.[36] While these outcome-determinative claims have no place in contract disputes, they are overtly false.

To the contrary, the pandemic has proved very *profitable* for insurance companies—one of the few industries able to make such a claim. To the knowledge of UP, no insurance company has entered insolvency due to the pandemic. Instead, insurance companies have enjoyed enormous windfalls. For example, in July 2020, Progressive Insurance Company "boasted about an 83% year over year increase in net income" which works out to about $800 million per quarter.[37] Chubb Limited reported net income of $1.19 billion in its third quarter, in 2020—up 9.4%, or $100 million, from the year before.[38] CNA Insurance similarly reported a $106 million increase in net income in the same period.[39]

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[36] *See, e.g.*, Eli Flesch, "Trade Group Tells 1st Cir. Eateries Not Owed Virus Coverage" Law360.com (Sept. 15, 2021), https://www.law360.com/insurance-authority/property/articles/1422231/trade-group-tells-1st-circ-eateries-not-owed-virus-coverage.

[37] Richard Holober, *Progressive Insurance Hoards Covid-19 Windfall Profits*, Consumer Federation of California (Aug. 13, 2020), https://uphelp.org/wp-content/uploads/2021/02/cfc_progressive.pdf

[38] Claire Wilkinson, *Chubb reports gains in Q3 profit, net premium written*, Business Insurance (Oct. 28, 2020), https://www.businessinsurance.com/article/20201028/NEWS06/912337411/Chubb-reports-gains-in-Q3-profit,-net-premium-written.

[39] Angela Childers, *CNA Reports Higher Net Income Despite Cat Losses*, Business Insurance (Nov. 2, 2020), https://www.businessinsurance.com/article/20201102/NEWS06/912337508/CNA-reports-higher-net-income-despite-cat-

W.R. Berkley Corporation reported a massive 161% increase in its fourth quarter, in 2020.[40]

Indeed, despite not paying any COVID-19 related business interruption claims, insurance companies significantly *increased* their rates in 2020 across all lines of business. One large broker reported that 89% of its clients saw a rate increase for their property insurance—the "highest number recorded since the early 2000s."[41] From April through June 2020, property insurance rates spiked by 22%.[42] Insurance companies ratcheted up prices again between July and September, with a total increase of 24% for commercial property coverage.[43] From October to December 2020, premiums increased another 20%.[44] In late 2020,

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losses.

[40] J. Greenwald, *Berkley Reports 161% Jump in Profits*, Business Insurance (Jan. 26, 2021), available at https://www.businessinsurance.com/ article/00010101/ NEWS06/912339367/Berkley-reports-161-jump-in-profits.

[41] Matthew Lerner, *Most Policyholders See Rate Hikes Across Multiple Lines*, Business Insurance (Oct. 26, 2020), https://www.businessinsurance. com/article/ 20201026/NEWS06/912337341/Most-policyholders-see-rates-hikes-across-multiple-lines-Arthur-J-Gallagher-Re.

[42] Matthew Lerner, *U.S. Commercial Property Pricing up 22% in Q2*, Business Insurance (Aug. 10, 2020), https://www.businessinsurance.com/ article/ 00010101/NEWS06/912336034/US-commercial-property-pricing-up-22-in-Q2.

[43] Claire Wilkinson, *Insurance Prices Increased Sharply in Third Quarter*, Business Insurance (Nov. 5, 2020), https://www.businessinsurance.com/article/ 00010101/NEWS06/912337590/Insurance-prices-increased-sharply-in-third-quarter-Marsh.

[44] Matthew Lerner, *Global Prices Rise 22% in Q4: Marsh*, Business Insurance (Feb. 4, 2021), https://www.businessinsurance.com/ article/20210204/

2020, property insurance companies told consumers to expect increases of 15% to 25% in 2021.[45] The pandemic has been very profitable for insurance companies, indeed, and yet they refuse to pay business interruption claims for businesses teetering on the edge of collapse.

CONCLUSION

The dismissal here was premature and unjust. Sportime is entitled to its day in court on the ambiguities that AIG built into its policies. That would be the result if this Court were to grant Sportime's appeal. UP respectfully submits that such relief should be granted.

Respectfully submitted,

ANDERSON KILL PC

Dated: October 29, 2021

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NEWS06/912339588/Global-prices-rise-22-in-Q4-Marsh-Global-Insurance-Market-Index-.

[45] Judy Greenwald, *Continued Rate Increases Expected: Willis*, BUSINESS INSURANCE (Nov. 19, 2020), https://www.businessinsurance.com/article/20201119/NEWS06/912337904/Continued-rate-increases-expected-Willis-Towers-Watson.

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PRINTING SPECIFICATION STATEMENT

APPELLATE DIVISION - SECOND JUDICIAL DEPARTMENT

I hereby certify pursuant to 22 NYCRR § 1250.8(j) that the foregoing brief was prepared on a computer using Microsoft Word.

A proportionally spaced typeface was used, as follows:

Font: Times New Roman

Size: 14

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The total number of words in this brief, inclusive of point headings and footnotes and exclusive of pages containing the table of contents, table of citations, proof of service, certificate of compliance, or any authorized addendum containing statutes, rules, regulations, etc., is 6,967.

TABLE OF CONTENTS

ADDENDUM

ADDENDUM 1

ISO Circular

FORMS - FILED JULY 6, 2006

FROM: LARRY PODOSHEN, SENIOR ANALYST

COMMERCIAL PROPERTY LI-CF-2006-175

NEW ENDORSEMENTS FILED TO ADDRESS EXCLUSION OF LOSS DUE TO VIRUS OR BACTERIA

This circular announces the submission of forms filings to address exclusion of loss due to disease-causing agents such as viruses and bacteria.

BACKGROUND

Commercial Property policies currently contain a pollution exclusion that encompasses contamination (in fact, uses the term *contaminant* in addition to other terminology). Although the pollution exclusion addresses contamination broadly, viral and bacterial contamination are specific types that appear to warrant particular attention at this point in time.

ISO ACTION

We have submitted forms filing CF-2006-OVBEF in all ISO jurisdictions and recommended the filing to the independent bureaus in other jurisdictions. This filing introduces new endorsement CP 01 40 07 06 - Exclusion Of Loss Due To Virus Or Bacteria, which states that there is **no coverage 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**.

Note: In Alaska, District of Columbia, Louisiana*, New York and Puerto Rico, we have submitted a different version of this filing, containing new endorsement CP 01 75 07 06 in place of CP 01 40. The difference relates to lack of implementation of the mold exclusion that was implemented in other jurisdictions under a previous multistate filing.

Both versions of CF-2006-OVBEF are attached to this circular.

* In Louisiana, the filing was submitted as a recommendation to the Property Insurance Association of Louisiana (PIAL), the independent bureau with jurisdiction for submission of property filings.

PROPOSED EFFECTIVE DATE

Filing CF-2006-OVBEF was submitted with a proposed effective date of January 1, 2007, in accordance with the applicable effective date rule of application in each state, with the exception of various states for which the insurer establishes its own effective date.

Upon approval, we will announce the actual effective date and state-specific rule of effective date application for each state.

RATING SOFTWARE IMPACT

New attributes being introduced with this revision:

- A new form is being introduced.

CAUTION

This filing has not yet been approved. If you print your own forms, do not go beyond the proof stage until we announce approval in a subsequent circular.

RELATED RULES REVISION

We are announcing in a separate circular the filing of a corresponding rules revision. Please refer to the **Reference(s)** block for identification of that circular.

REFERENCE(S)

LI-CF-2006-176 (7/6/06) - New Additional Rule Filed To Address Exclusion Of Loss Due To Virus Or Bacteria

ATTACHMENT(S)

- Multistate Forms Filing CF-2006-OVBEF
- State-specific version of Forms Filing CF-2006-OVBEF (Alaska, District of Columbia, Louisiana, New York, Puerto Rico)

We are sending these attachments only to recipients who asked to be put on the mailing list for attachments. If you need the attachments for this circular, contact your company's circular coordinator.

PERSON(S) TO CONTACT

If you have any questions concerning:

- the content of this circular, please contact:

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Now, as in the past, all of our products and services are advisory, and are made available for optional use by participating insurers as a matter of individual choice. Your company must decide for itself which, if any, ISO products or services are needed or useful to its operation and how those selected for use should be applied. We urge that you be guided by the advice of your attorneys on the legal requirements.

Amendatory Endorsement - Exclusion Of Loss Due To Virus Or Bacteria

About This Filing

This filing addresses exclusion of loss due to disease-causing agents such as viruses and bacteria.

New Form

We are introducing:

- Endorsement **CP 01 40 07 06** - Exclusion Of Loss Due To Virus Or Bacteria

Related Filing(s)

Rules Filing CF-2006- OVBER

Introduction

The current pollution exclusion in property policies encompasses contamination (in fact, uses the term *contaminant* in addition to other terminology). Although the pollution exclusion addresses contamination broadly, viral and bacterial contamination are specific types that appear to warrant particular attention at this point in time.

An example of bacterial contamination of a product is the growth of listeria bacteria in milk. In this example, bacteria develop and multiply due in part to inherent qualities in the property itself. Some other examples of viral and bacterial contaminants are rotavirus, SARS, influenza (such as avian flu), legionella and anthrax. The universe of disease-causing organisms is always in evolution.

Disease-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 (for example, the milk), cost of decontamination (for example, interior building surfaces), and business interruption (time element) losses.

Current Concerns

Although 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. In addition, pollution exclusions are at times narrowly applied by certain courts. In recent years, ISO has filed exclusions to address specific exposures relating to contaminating or harmful substances. Examples are the mold exclusion in property and liability policies and the liability exclusion addressing silica dust. Such exclusions enable elaboration of the specific exposure and thereby can reduce the likelihood of claim disputes and litigation.

While 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.

In light of these concerns, we are presenting an exclusion relating to contamination by disease-causing viruses or bacteria or other disease-causing microorganisms.

Features Of New Amendatory Endorsement

The amendatory endorsement presented in this filing states that there is **no coverage 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 exclusion (which is set forth in Paragraph B of the endorsement) applies to property damage, time element and all other coverages; introductory Paragraph A prominently makes that point. Paragraphs C and D serve to avoid overlap with other exclusions, and Paragraph E emphasizes that other policy exclusions may still apply.

Copyright Explanation

Important Note

Insurance Services Office, Inc. (ISO) makes available advisory services to property/casualty insurers. ISO has no adherence requirements. ISO policy forms and explanatory materials are intended solely for the information and use of ISO's participating insurers and their representatives, and insurance regulators. Neither ISO's general explanations of policy intent nor opinions expressed by ISO's staff necessarily reflect every insurer's view or control any insurer's determination of coverage for a specific claim. ISO does not intercede in coverage disputes arising from insurance policies. If there is any conflict between a form and any other part of the attached material, the provisions of the form apply.

THIS ENDORSEMENT CHANGES THE POLICY. PLEASE READ IT CAREFULLY.

EXCLUSION OF LOSS DUE TO VIRUS OR BACTERIA

This endorsement modifies insurance provided under the following:

COMMERCIAL PROPERTY COVERAGE PART
STANDARD PROPERTY POLICY

A. The 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.

B. 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.

However, this exclusion does not apply to loss or damage caused by or resulting from "fungus", wet rot or dry rot. Such loss or damage is addressed in a separate exclusion in this Coverage Part or Policy.

C. With respect to any loss or damage subject to the exclusion in Paragraph **B.**, such exclusion supersedes any exclusion relating to "pollutants".

D. The following provisions in this Coverage Part or Policy are hereby amended to remove reference to bacteria:

1. Exclusion of "Fungus", Wet Rot, Dry Rot And Bacteria; and

2. Additional Coverage - Limited Coverage for "Fungus", Wet Rot, Dry Rot And Bacteria, including any endorsement increasing the scope or amount of coverage.

E. The terms of the exclusion in Paragraph **B.**, or the inapplicability of this exclusion to a particular loss, do not serve to create coverage for any loss that would otherwise be excluded under this Coverage Part or Policy.

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Amendatory Endorsement - Exclusion Of Loss Due To Virus Or Bacteria

About This Filing

This filing addresses exclusion of loss due to disease-causing agents such as viruses and bacteria.

New Form

We are introducing:

- Endorsement **CP 01 75 07 06** - Exclusion Of Loss Due To Virus Or Bacteria

Related Filing(s)

Rules Filing CF-2006-OVBER

Introduction

The current pollution exclusion in property policies encompasses contamination (in fact, uses the term *contaminant* in addition to other terminology). Although the pollution exclusion addresses contamination broadly, viral and bacterial contamination are specific types that appear to warrant particular attention at this point in time.

An example of bacterial contamination of a product is the growth of listeria bacteria in milk. In this example, bacteria develop and multiply due in part to inherent qualities in the property itself. Some other examples of viral and bacterial contaminants are rotavirus, SARS, influenza (such as avian flu), legionella and anthrax. The universe of disease-causing organisms is always in evolution.

Disease-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 (for example, the milk), cost of decontamination (for example, interior building surfaces), and business interruption (time element) losses.

Current Concerns

Although 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. In addition, pollution exclusions are at times narrowly applied by certain courts. In recent years, ISO has filed exclusions to address specific exposures relating to contaminating or harmful substances. Examples are the mold exclusion in property and liability policies and the liability exclusion addressing silica dust. Such exclusions enable elaboration of the specific exposure and thereby can reduce the likelihood of claim disputes and litigation.

While 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.

In light of these concerns, we are presenting an exclusion relating to contamination by disease-causing viruses or bacteria or other disease-causing microorganisms.

Features Of New Amendatory Endorsement

The amendatory endorsement presented in this filing states that there is **no coverage 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 exclusion (which is set forth in Paragraph B of the endorsement) applies to property damage, time element and all other coverages; introductory Paragraph A prominently makes that point. Paragraph C serves to avoid overlap with another exclusion, and Paragraph D emphasizes that other policy exclusions may still apply.

Copyright Explanation

Important Note

Insurance Services Office, Inc. (ISO) makes available advisory services to property/casualty insurers. ISO has no adherence requirements. ISO policy forms and explanatory materials are intended solely for the information and use of ISO's participating insurers and their representatives, and insurance regulators. Neither ISO's general explanations of policy intent nor opinions expressed by ISO's staff necessarily reflect every insurer's view or control any insurer's determination of coverage for a specific claim. ISO does not intercede in coverage disputes arising from insurance policies. If there is any conflict between a form and any other part of the attached material, the provisions of the form apply.

THIS ENDORSEMENT CHANGES THE POLICY. PLEASE READ IT CAREFULLY.

EXCLUSION OF LOSS DUE TO VIRUS OR BACTERIA

This endorsement modifies insurance provided under the following:

COMMERCIAL PROPERTY COVERAGE PART
STANDARD PROPERTY POLICY

A. The 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.

B. 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.

However, this exclusion does not apply to loss or damage caused by or resulting from fungus. Such loss or damage is addressed in a separate exclusion in this Coverage Part or Policy.

C. With respect to any loss or damage subject to the exclusion in Paragraph **B.**, such exclusion supersedes any exclusion relating to "pollutants".

D. The terms of the exclusion in Paragraph **B.**, or the inapplicability of this exclusion to a particular loss, do not serve to create coverage for any loss that would otherwise be excluded under this Coverage Part or Policy.

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ADDENDUM 2

EXPLANATORY MEMORANDUM – RESPONSE TO OBJECTION 1 DATED 4-30-2010

The chief object of this filing is to submit a Company Exception to ISO State Exception Rule A.6.

Currently, this ISO rule imposes a Mandatory application of a Virus and Bacteria Exclusion CP 01 78 to the coverage afforded by the ISO Commercial Property Coverage Form. The ISO initial filing of this endorsement indicated that the exclusion was appropriate due to "pandemic" exposure to loss which was not anticipated in the standard coverage forms or in development of the loss costs for Commercial Property. Therefore, we assume that this Exclusion is deleting coverage across the entire NY Commercial Fire and Allied book written by the ISO member companies that utilize the ISO product, unless modified by such a Company exception.

Because the application of this Exclusion is to Commercial Property, we anticipate losses to fall largely in Business Personal Property (“stock”) and Business Interruption/Time Element coverage segments. We also anticipate that it will not affect large segments of GNY’s current book, but rather solely to some isolated risks.

The GNY Insurance Companies wishes to make this endorsement CP 01 78 Optional on individual risks rather than Mandatory on a panacea basis. Because the GNY Insurance Companies is largely a niche market of habitational business, we feel that our exposure to this type of loss ("pandemic") is minimal, since such contagious disease is largely is transmitted to third parties via ingestion or some other direct contact to an insured’s products. While it is possible that some type of disease (airborne Legionnaires Disease, for example) could spread through a HVAC system in any selected Apartment or Condo Building, it is highly unlikely that it would spread throughout a vast proportion of the apartments and condominiums across NYC that we insure.

While GNY does write some business in the restaurant classifications and we acknowledge that some exposure is inherent in such classifications due to the "Typhoid Mary" or contagious disease hazard (as some saw in the Hepatitis B exposure via a green onion vector some years ago), we feel such exposure is minimal since we do not write large concentrations of these risks in the same locales who could potentially use the same vendors of supplies. We do not write “chain” restaurants utilizing the same suppliers.

For all of the above reasons, we believe application of this Exclusion is appropriate on occasion, only to certain individual risks which sell or distribute products to the public. Additionally, GNY’s underwriting management feels that such an endorsement would be considered imposed on a restaurant account only if the risk presented with claim history indicative of recent incident and loss control with little remediation.

Therefore, to answer your specific questions, we do not anticipate that any of our insured’s will voluntarily request this exclusion; some (habitational risks) because it would never enter their minds as a problem for which they would voluntarily reduce coverage; others (restaurants) because they feel that such an event is well within the realm of possible fortuitous occurrences and should be covered should such an event arise.

We anticipate that the Company will impose this exclusion on such individual risks that present with recent loss history of this type of claim and loss control that would give us concerns of an on-going nature (cavalier attitude of management regarding implementation of hand washing procedures by food handling staff); i.e., we would impose attachment of this Exclusion in accordance with prudent supportable underwriting analysis of risk (since the variables involved could be of substantial scope). We do not anticipate imposing this exclusion on any specific classification (though restaurants are probably the most likely to experience such events) or across large segments of our book of business, since we do not feel the exposure to loss is very high in any segment of our existing Commercial Property book (though we acknowledge the possibility for Apartments, Condominiums and Office/Retail Buildings to experience such an event).

Because of the broad scope of the potential events which may occur, we feel that it is largely impossible to create a rule which takes in every aspect of exposure to communicable disease. Is it possible to simply indicate something in your proposed revision of our rule to state “This Exclusion will be applied on a case-by-case basis to risks which present with recent loss history which in the underwriters judgment indicates a potential higher than average exposure to loss”?

As indicated, our main object of this filing is to remove the carte blanch application of this Exclusion and not deny coverage to the majority portion of our book.

EXHIBIT C

Exhibit RT-1 – Side by Side Comparison

[Currently Filed and approved ISO Original Rule]

ADDITIONAL RULE(S)

A6. EXCLUSION OF LOSS DUE TO VIRUS OR BACTERIA

Attach New York - Exclusion Of Loss Due To Virus Or Bacteria Endorsement CP 01 78 to all policies.

[Our Proposed New Rule]

ADDITIONAL RULE(S)

The following Additional Rule in the ISO State Exceptions is amended:

A6. EXCLUSION OF LOSS DUE TO VIRUS OR BACTERIA

RULE A6. EXCLUSION OF LOSS DUE TO VIRUS OR BACTERIA is replaced by the following:

ISO form CP 01 78 is an optional form.

Premium Determination When Exclusion is Applied:

Upon the introduction of this endorsement in 2006, the ISO position regarding the above Exclusion endorsement is that this exposure represents a "pandemic exposure to loss" and therefore is not assumed in the promulgation of Commercial Fire and Allied Lines data collection which is the basis for the development of loss costs. ISO indicates that they never anticipated extending such an exposure under the existing coverage form(s) of the period (at that time, filings would have assumed the CP 04 02 edition of the Commercial Property Coverage Forms.

Under the unmodified ISO rule attributed to this endorsement, this endorsement is applied to all policies on a mandatory basis. We have modified this rule to make it an Optional endorsement, based on Risk Characteristics indicated in the sections which follow.

Because coverage for such a pandemic exposure was not anticipated for coverage, there is therefore no increment included in ISO Commercial Fire and Allied Lines loss costs currently that represents a charge for this exposure. There is therefore no credit afforded in the application of the exclusion to any policy if added to any specific risk in accordance with the following exposure to loss:

Risk Characteristics For Application of Exclusion (CP 01 78):

1. Historical report of an event which may or may not have resulted in loss involving sickness (including death) arising out of an insured's clients' (and/or any other person to whom the insured's clients' have contact) exposure to disease or infection while on the

insured's premises or due to contact with the insured's operations, employees; or products.

2. Such claim or loss must arise from the action or order of a civil authority to close the insured's operation in order to limit public exposure to such contagion, sickness and death; or

3. Such historical event or incident can arise from the action of the insured to close the insured's operation in order to limit public exposure to such contagion, sickness and death due to the insured's prudent expectation that such an event is likely to occur.

4. Account will be considered acceptable upon submission of clearance by civil authority governing type of business insured operates or through certification by duly authorized Public Health or contagious disease expert.

5. Issues described under paragraphs 1 through 3 above may be waived if proximate cause of the incident/event is traced to vendor or supplier of the insured with which the insured has severed its relationship and/or if the insured was proven not to have contributed to the incident.

6. Issues described under paragraphs 1 through 3 above may not be waived if the insured is a restaurant and the proximate cause of the incident/event is traced to improper food handling practices, storage or sanitation infractions or improperly cooked ground beef.

RISK CHARACTERISTICS DETERMINING WHEN EXCLUSION IS NOT APPLIED:

Application of the Exclusion is determined solely on the above-noted criteria ("**Risk Characteristics For Application of Exclusion")**. Coverage provided by omission of the exclusion is therefore otherwise written freely and without restriction.

Premium Determination When Exclusion is NOT Attached:

Apply the Factor in the Table below against the combined Building, Business Personal Property or Business Income including/without Extra Expense adjusted premium for the location after application of all other modification factors.

Grade	Exposure	Charge
High	Restaurants/Hotels/Grocery or Food Product Manufacturers with Products Liability exposure; No prior loss history.	Factor: .025
Medium	Buildings (lessors') with Restaurant, Grocery or Retail exposures; No Questionable Loss Control pertaining to cleaning of ventilation systems; No prior loss history.	Factor: .015
Low	All other Classifications; No prior loss history.	Flat: $25

ADDENDUM 3

UNITED STATES DISTRICT COURT

FOR THE DISTRICT OF NEW MEXICO

FACTORY MUTUAL INSURANCE COMPANY (as Assignee of ALBANY MOLECULAR RESEARCH, INC. and OSO BIOPHARMACEUTICALS MANUFACTURING, LLC)	)	
Plaintiff,	)	**CASE NO.: 1:17-cv-00760-GJF-LF**
vs.	)	
FEDERAL INSURANCE COMPANY and DOES 1-10,	)	
Defendants.	)	

PLAINTIFF FACTORY MUTUAL INSURANCE COMPANY'S MOTION *IN LIMINE* NO. 5 RE PHYSICAL LOSS OR DAMAGE

I. INTRODUCTION

Plaintiff Factory Mutual Insurance Company ("FM Global") hereby moves this court for an order excluding any and all evidence, references to evidence, testimony and argument that the mold infestation, as well as the costs incurred to remediate and return the facility to its pre-loss condition, is not physical loss under the Federal Insurance Company policy. Plaintiff further moves the court to instruct defendant and defendant's counsel to advise all witnesses accordingly.

Evidence and argument that mold is not physical damage have no tendency to prove or disprove disputed facts relevant to the determination of this action and are contrary to the law in this regard. Accordingly, such assertions cannot lead to proper evidentiary inferences, i.e., a deduction of *fact* logically and reasonable drawn from another established *fact*. It will consume unnecessary

time and create an extreme danger of confusing and misleading the jury about what is physical loss or damage for purposes of establishing coverage under the Federal policy.

II. ARGUMENT

A. Legal Standard.

The Court has the inherent authority to control trial proceedings, including ruling on motions *in limine.* See, e.g., *Luce v. United States,* 469 U.S. 38, 40, n.2 and 4 (1984). In addition, a motion *in limine*:

> affords an opportunity to the court to rule on the admissibility of evidence in advance, and prevents encumbering the record with immaterial or prejudicial matter, as well as providing a means of ensuring that privileged material as to which discovery has been allowed by the court will not be used at trial if it is found to be inadmissible.

75 Am.Jur.2d, *Trial* § 94 (1991) (footnotes omitted).

Federal Rule of Evidence Rule 401 states that evidence is relevant if: (a) it has any tendency to make a fact more or less probable than it would be without the evidence; and (b) the fact is of consequence in determining the action. *Sprint/United Mgmt. Co. v. Medelsohn*, 552 U.S. 379, 388 (2008). Rule 402 specifically prohibits irrelevant evidence. The Advisory Committee has stated that "relevance is not an inherent characteristic of any item of evidence but exists only as a relation between an item of evidence and a matter properly provable in the case." *Fed. R. Evid*. 401. In addition, the Court may exclude otherwise relevant evidence "if its probative value is substantially outweighed by the danger of unfair prejudice." *Fed. R. Evid*. 403. Further, evidence may be excluded when there is a significant danger that the jury might base its decision on emotion, or when non-party events would distract reasonable jurors from the real issues in the case. *Tennison v. Circus Circus Enterprises, Inc*., 244 F.3d 684, 690 (9th Cir. 2001). With this in mind, "motion[s] in limine allow[] the parties to resolve evidentiary disputes before trial and avoid[] potentially prejudicial evidence being presented in front of the jury, thereby relieving the trial judge from the formidable

task of neutralizing the taint of prejudicial evidence." *Brodit v. Cambra*, 350 F.3d 985, 1004-05 (9th Cir. 2003).

B. The Mold Infestation Is Physical Loss or Damage Under the Federal Policy.

FM Global anticipates that Federal will argue and attempt to introduce evidence that the mold infestation is not "physical loss or damage" under its policy and thus, not covered. In addition, Federal has indicated it will assert that the costs to remediate and return the facility to its pre-loss condition are not "physical loss or damage." These arguments are contrary to the facts of this loss and the case law which broadly interprets the term "physical loss or damage" in property insurance policies.[1]

It is undisputed that the mold infestation destroyed the aseptic environment and rendered Room 152 unfit for its intended use – manufacturing injectable pharmaceutical products. Numerous courts have concluded that loss of functionality or reliability under similar circumstances constitutes physical loss or damage. *See, e.g., Western Fire Insurance Co. v. First Presbyterian Church*, 437 P.2d 52 (Colo. 1968) (church building sustained physical loss or damage when it was rendered uninhabitable and dangerous due to gasoline under the building); *Gregory Packaging, Inc. v. Travelers Property and Casualty Company of America*, Civ. No. 2:12-cv-04418 2014 U.S. Dist. LEXIS 165232, 2014 WL 6675934 (D. N.J. 2014) (unsafe levels of ammonia in the air inflicted "direct physical loss of or damage to" the juice packing facility "because the ammonia physically rendered the facility unusable for a period of time."); *Port Authority of N.Y. and N.J. v. Affiliated FM Ins. Co*., 311 F.3d 226, 236 (3d Cir. 2002) (asbestos fibers); *Essex v. BloomSouth Flooring Corp*., 562 F.3d 399, 406 (1st Cir. 2009) (unpleasant odor in home); *TRAVCO Ins. Co. v. Ward*, 715

[1] At best for Federal, 'physical loss or damage,' which is undefined, is susceptible of more than one reasonable interpretation and is therefore ambiguous and must be construed against Federal. See Memorandum and Order, docket 118, p. 9, citing *United Nuclear Corp. v. Allstate Ins. Co*., 285 P.3d 644, 647 & 649 (N.M. 2012); *Battishill v. Farmers All. Ins. Co*., 127 P.3d 1111, 1115 (N.M. 2006).

F.Supp.2d 699, 709 (E.D.Va. 2010), aff'd, 504 F. App'x. 251 (4th Cir. 2013) ("toxic gases" released by defective drywall).

Loss of functionality and/or reliability is especially significant where, as here, the property covered involves a product to be consumed by humans. Courts have concluded that the product is damaged where its "function and value have been seriously impaired, such that the product cannot be sold." *Pepsico, Inc. v. Winterthur International America Insurance Co*., 806 N.Y.S.2d 709, 744 (App. Div. 2005), citing *General Mills, Inc. v. Gold Medal Insurance Co*., 622 N.W.2d 147 (Minn. Ct.App. 2001); *Pillsbury Co. v. Underwriters at Lloyd's, London*, 705 F Supp 1396 (D. Minn. 1989); *National Union Fire Ins. Co. of Pittsburgh, Pa. v. Terra Indus*., 216 F Supp 2d 899 (N.D. Iowa 2002), aff'd 346 F3d 1160 (8th Cir. 2003), cert denied 541 US 939 (2004); *Shade Foods, Inc. v. Innovative Prods. Sales & Mktg., Inc*., 93 Cal Rptr. 2d 364 (Cal.App. 2000); *Zurich Am. Ins. Co. v. Cutrale Citrus Juices USA, Inc*., 2002 WL 1433728, 2002 US Dist LEXIS 26829 (M.D. Fla. 2002). These courts' rationale regarding food products applies equally, if not more so, to the injectable pharmaceuticals OSO manufactured which were exposed to mold and no longer met industry safety standard. *See*, *General Mills v. Gold Medal Insurance*, 622 N.W.2d at 152 (food product which no longer met FDA safety standard sustained property damage.); *Motorists Mutual Ins. Co. v. Hardinger*, 131 F.Appx. 823 (3d Cir. 2005) (E coli in water well was physical loss or damage to insured's home.)[2]

The period of time as well as costs required to bring OSO's facility to the level of cleanliness following the mold infestation required by OSO's customers is also physical loss or damage covered by the Federal policy. The facility was damaged by stringent requirements of OSO's customers regarding production to the same extent it was damaged from the mold infestation itself as the facility was unusable as the result of a covered loss. See, e.g., *Western Fire v. First Presbyterian*,

[2] The Court appears to agree that the mold infestation at the OSO facility was "physical loss or damage" as that term is used in property insurance policies such as the one issued by Federal. See Memorandum and Order, docket 118, p. 9.

437 P.2d at 55 (insured was awarded costs to remediate infiltration and contamination when gasoline rendered church unusable); *Farmers Insurance Co. v. Trutanich,* 858 P.2d 1332, 1335 (Ore.App. 1993) (costs of rectifying methamphetamine odor covered as direct physical loss or damage.)

The case of *Marshall Produce Co. v. St. Paul Fire & Marine Ins. Co*., 256 Minn. 404, 98 N.W.2d 280 (1959 Minn.) is instructive. There, the insured manufactured food products for the army pursuant to a contract that required the manufacturing plant be smoke free. When smoke from a fire on a neighbor's property permeated the insured's plant for some period of time, the army refused to accept any of the products, rendering them worthless. The Minnesota Supreme Court rejected the insurer's argument that there was no physical loss or damage. According to the court, the food was damaged because of army regulations that set forth stringent requirements for the manufacturing environment. The court also noted that the impairment of value, not the physical damage, was the measure of damages. *Id.* 98 N.W. 2d at 293.

Here, Federal was familiar with OSO's manufacturing process and the contracts which required OSO to maintain an aseptic manufacturing standards at its facilities. Federal was also aware that a mold infestation could cause significant damage not only to the products exposed to the mold, but also because of the time and cost to clean the mold to the standards required by the manufacturing contracts. Without the customers' approval of the restored aseptic conditions following the mold infestation, OSO's facility remained unusable. Indeed, had OSO manufactured products without the customers' approval of the facility, the customers could have properly refused to accept the products and they would have been as worthless as the food products at issue in *Marshall Produce v. St. Paul*. See also, *General Mills, Inc. v. Gold Medal Insurance Co*., 622 N.W.2d 147 (Minn. Ct.App. 2001) (The function and value of food products was impaired where the

FDA prevented the insured from selling them.); *Pepsico, Inc. v. Winterthur International America Insurance Co*., 806 N.Y.S.2d 709, 744 (App. Div. 2005) (Insured sustained property damage where its beverages had become "unmerchantable," i.e., the product's function and value were seriously impaired, such that the product could not be sold.)

Accordingly, evidence or argument that the mold infestation or the time and costs to remediate the infestation are not physical loss or damage does not create a reasonable inference as to the probability or lack of probability of a fact. *Fed. R. Evid*. 401; *A.I. Credit Corp v. Legion Insurance Co*., 265 F.3d 630, 638 (7th Cir. 2001). There being no legal basis to require FM Global to prove demonstrable structural damage or alteration to property or products, evidence or argument in this regard does not involve or establish a controverted fact and should be barred from trial. Allowing Federal to argue or elicit testimony that the loss did not create structural damage or alteration to property or products, so is not covered is inconsistent the law, prejudicial to FM Global and will only confuse the jury. See *Fed. R. Evid*. 403.

III. CONCLUSION

Based on the foregoing, FM Global respectfully requests that the Court grant this motion *in limine* to preclude questions, testimony or argument that the mold infestation and costs to remediate the infestation are not physical loss or damage under the Federal policy.

Respectfully submitted,

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CERTIFICATE OF SERVICE

This is to certify that on November 19, 2019, a true and correct copy of the foregoing was delivered to all counsel of record in accordance with the Federal Rules of Civil Procedure and the Local Rules of this Court.

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ADDENDUM 4

INFECTED JUDGMENT: PROBLEMATIC RUSH TO CONVENTIONAL WISDOM AND INSURANCE COVERAGE DENIAL IN A PANDEMIC

ERIK S. KNUTSEN AND JEFFREY W. STEMPEL [*] ©

Abstract

The COVID-19 pandemic created not only a public health crisis but also an insurance coverage imbroglio, prompting near-immediate business interruption claims by policyholders impacted by government restrictions ordered in response to the pandemic. Insurers and their representatives "presponded" to the looming coverage claims by quickly moving to denigrate arguments for coverage, engaging in a pre-emptive strike that has largely worked to date, inducing too many courts to rush to judgment by declaring—as a matter of law—that policy terms such as "direct physical loss or damage" do not even arguably encompass the business shutdowns resulting from COVID-19. Our closer examination of the term and of other key coverage questions suggests that policyholders have a much stronger case than suggested by the initial—and often superficial and conclusory—conventional wisdom flowing from the first wave of judicial decisions. Only a few courts have analyzed the COVID coverage debate with the type of reflective care, judicial humility, and respect for the trial process one would hope to see. The "early returns" in these coverage wars have been analytically disappointing, creating risk of an unfortunate path dependency or cascade of cases excessively narrowing the meaning of key terms such as "loss" and "damage," and diminishing the quality of future coverage decisions.

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[*] Respectively, Professor of Law, Queens University-Canada and Doris S. & Theodore B. Lee Professor of Law, William S. Boyd School of Law, University of Nevada Las Vegas. Thanks to Bill Boyd, Jay Feinman, Chris French, Dan Hamilton, Yong Han, Helmut Heiss, the late Doris Lee, Ted Lee, Randy Maniloff, David McClure, Ann McGinley, our colleagues in the American College of Coverage Counsel and the Project Group for the Principles of Reinsurance Law (PRICL), and the ALI Restatement of the Law of Liability Insurance process. The opinions expressed in this article are of course our own and should not be attributed to any of those we cite or thank.

TABLE OF CONTENTS

I. INTRODUCTION

A. COVID-19 AND COVERAGE CONTROVERSY

As the world now knows, a variant of the SARS coronavirus emerged in Asia in late 2019[1] creating a severe concentration of infections in Wuhan, China that spread rapidly throughout the world reaching the United States perhaps as early as December 2019.[2] By February 2020, the new virus named COVID-19[3] was a

[1] "SARS" (Severe Acute Respiratory Syndrome) is the name given to a class of particularly dangerous virus that causes respiratory problems but often adversely affect other organs. Julia Ries, *Here's How COVID-19 Compares to Past Outbreaks*, HEALTHLINE (Mar. 12, 2020), https://www.healthline.com/health-news/how-deadly-is-the-coronavirus-compared-to-past-outbreaks. SARS viruses are common in animals and only occasionally cross over to humans—with dangerous results. *Id.* The SARS-1 virus, which spread rapidly between 2002 and 2004, infected many and caused an estimated 774 deaths worldwide (though none in the United States). *Id*. *See generally* Center for Disease Control and Prevention, CDC.GOV, https://www.cdc.gov (providing range of information regarding the SARS virus and COVID-19 in particular).

[2] *See* CDC.GOV, *supra* note 1 (noting that as of January 1, 2021, COVID-19 surpassed twenty million cases and 341,199 deaths in the United States). *Accord*, Johns Hopkins Coronavirus Resource Center, https://www.coronavirus.jhu.edu.

[3] COVID-19 is "a mild to severe respiratory illness that is caused by a coronavirus (*Severe acute respiratory syndrome coronavirus 2 of the genus Betacoronavirus*)" transmitted chiefly by contact with infectious material (such as respiratory droplets) or with objects or surfaces contaminated by the causative virus, and is characterized especially be fever cough, and shortness of breath and may progress to pneumonia and respiratory failure." *See COVID-19*, MERRIAM-WEBSTER DICTIONARY (2020), https://www.merriam-webster.com/dictionary/COVID-19.

The term coronavirus derived from the crown-like spikes of the virus that appear when it is viewed by microscope. Kathy Katella, *Our New COVID-19 Vocabulary—What Does it All Mean?*, YALE MEDICINE (Apr. 7, 2020), https://www.yalemedicine.org/stories/covid-19-

widely acknowledged serious problem[4] that was deemed a "pandemic" by March 11, 2020.[5] Beginning in March 2020, state and local governments began issuing

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glossary/. It is a relative of the SARS-CoV (often referred to as "SARS" or Severe Acute Respiratory Syndrome) that caused substantial injury and death in a 2002-2003 worldwide outbreak. *Id*. Coronaviruses of various types can cause common colds as well as SARS and Middle East respiratory syndrome (MERS). *Id*. The variant emerging in 2019 "is believed to have started in animals and spread to humans. *Id*. Animal-to-person spread was suspected after the initial outbreak in December among people who had a link to a large seafood and live animal market in Wuahn, China." *Id*.

COVID-19 is thus the name for the disease resulting from infection by the virus with the letters COVI standing for coronavirus, the D for disease, and the number 19 in the name resulting because this particular strain of the virus emerged in Wuhan in November 2019 Because the name is derived from initials, it is frequently abbreviated as "COVID-19" in capital letters.

[4] *See* Christopher C. French, *COVID-19 Business Interruption Insurance Losses: The Cases for and Against Coverage*, 27 CONN. INS. L.J. 1 (2020) (acknowledging that COVID-19 infections were presenting serious problem). As is not common knowledge, governments exhibited a range of reactions to the COVID-19 problem. Some (*e.g.*, Canada, New Zealand, Hawaii), ordered substantial comprehensive "lockdowns" as a means of retarding the spread of the disease. *See, e.g*., Lauren Vogel, *COVID-19: A Timeline of Canada's First-wave Response*, CAN. MED. ASS'N J. NEWS (June 12, 2020), https://cmajnews.com/2020/06/12/coronavirus-1095847; Alexis Robert, *Lessons from New Zealand's COVID-19 Outbreak Response*, THE LANCET (November 1, 2020), https://www.thelancet.com/journals/lanpub/article/PIIS2468-2667(20)30237-1/fulltext; Alejandro de la Garza, *Hawaii Is Riding Out the COVID-19 Storm. But Geographic Isolation Isn't the Blessing it May Seem,* TIME (Nov. 25, 2020 10:07 AM), https://time.com/5915084/hawaii-covid-coronavirus/. Others, such as Sweden, adopted a system of modified restrictions that varied among states. Mariam Claeson & Stefan Hanson, *COVID-19 and the Swedish Enigma*, THE LANCET (January 23, 2021), https://www.thelancet.com/journals/lancet/article/PIIS0140-6736(20)32750-1/fulltext.

[5] The World Health Organization declared COVID-19 a pandemic on March 11, 2020. *See WHO Characterizes COVID-19 as a Pandemic*, WHO (Mar. 11, 2020), https://www.who.int/emergencies/diseases/novel-coronavirus-2019/events-as-they-happen (providing a timeline of COVID-19 developments and quoting WHO Director-General that the organization has "made the assessment that COVID-19 can be characterized as a pandemic" and is "the first pandemic caused by a coronavirus. And we have never before seen a pandemic that can be controlled, at the same time."). *See also* Natasha Frost, *Coronavirus, QAnon, Trump: Your Monday Briefing*, N.Y. TIMES (Oct. 11, 2020), https://www.nytimes.com/2020/10/11/briefing/coronavirus-qanon-trump-your-monday-briefing.html ("More than six months since the start of the pandemic, European countries such as France, Spain and Britain are reporting daily infection numbers comparable to—and sometimes far beyond—those of their first peaks.").

closure orders barring access to and operation of many facilities deemed insufficiently essential.[6]

The governmental orders varied, of course. Some demanded a stronger or more comprehensive shutdown than others. But many, if not most, precluded normal operation of "nonessential" business functions, perhaps most prominently indoor dining and entertainment, under pain of punishment for violation.[7] Within days of government recognition (now widely seen as belated) that COVID was highly contagious and dangerous,[8] insurance claims for business interruption were widely anticipated with additional anticipated coverage controversy involving other insurance products. The insurance coverage community was abuzz about the topic throughout Spring 2020, attention that continues only slightly abated today.[9] Lawsuits followed relatively quickly, numbering more than 1,000 by Fall 2020.[10]

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[6] *See* French, *supra* note 4; Terry Spencer & Teresa Crawford, *US Moves Nearer to Shutdown Amid Coronavirus Fears*, AP (Mar. 16, 2020), apnews.com/article/1510caddee80ea2d73363fab76d55967 ("Officials across the country curtailed many elements of American life to fight the coronavirus outbreak. . . Governors and mayors closed restaurants, bars, and schools as the nation sank deeper into chaos.").

[7] *See infra* Part I(B) and Part II.

[8] *See Death Rates from Coronavirus (COVID-19) in the United States as of December 22, 2020, by State*, STATISTA (Dec. 22, 2020), https://www.statista.com/statistics/1109011/coronavisure-covid19-death-rates-by-state (noting that, as of December 22, 2020, more than 319,000 American deaths were attributed to COVID-19 from a total of more than 20 million infections). Visible case studies of COVID-19 dangers were chronicled in often heart-wrenching news reports, *see, e.g.*, *Those We've Lost*, N.Y. TIMES (Nov. 3, 2020), https://www.nytimes.com/interactive/2020/obituaries/people-died-coronavirus-obituaries.html (discussing as a regular feature in the Times since the onset of the pandemic), as well as being demonstrated rather dramatically and contemporaneously when President Donald Trump, three US Senators, White House employees, and Secret Service agents were afflicted during late September and early October 2020. The President was treated by a large team of physicians utilizing an array of antibiotics, steroids, and supplemental oxygen during the President's 3-day hospitalization, with continuing treatment after discharge. *See* Katie Thomas & Denise Grady, *Trump Returns Home After Downplaying Disease, but Doctor Says He Isn't 'Out of the Woods,'* N.Y. TIMES (Oct. 7, 2020, 1:38 AM), https://www.nytimes.com/live/2020/10/05/world/covid-trump; Maggie Haberman & Annie Karni, *Trump's Return Leaves White House in Disarray as Infections Jolt West Wing*, N.Y. TIMES (Oct. 6, 2020), https://www.nytimes.com/2020/10/06/us/politics/white-house-coronavirus.html.

[9] *See infra* Part II.

[10] *See* Tom Baker, *COVID Coverage Litigation Tracker*, cclt.law.upenn.edu/author/tombaker/ (last visited December 31, 2020).

In the early spring days of the pandemic, the insurance industry began a remarkable media campaign to make known its position on the issue of coverage for virus-related losses: there is no coverage. In insurance industry publications, in lawyers' news media, and even in the news media consumed by the general public, the message of "no coverage for pandemic losses" was repeated again and again. This lies in stark contrast to the treatment of coverage for COVID-related losses in other jurisdictions such as Western Europe. But in America, however, the insurance industry repeated the mantra.

Policyholders only had to open a newspaper to see how the industry was advancing their views that claims would be denied, imposing motions to dismiss, at least before presumably favorable tribuinals. And insurers began to win. Those wins were reported and highlighted in the media. This anti-coverage public relations media blitz forms a curious backdrop to what actually occurred in courts across the United States deciding COVID-related claims. In short, as this article discusses below, courts often fell short in their analyses in these coverage cases, ignoring time-tested principles of insurance policy interpretation and even of basic civil litigation rules. The spectre of the anti-coverage media blitz may well have primed the judiciary for the results to come.

By January 2021, roughly seventy-five of these cases had some sort of substantive court decision, most commonly the grant or denial of a motion to dismiss for failure to state a claim, particularly the latter, pro-insurer result.[11] Insurers prevailed in sixty-seven of the seventy-five cases, with courts granting Rule 12(b)(6) (or its state equivalent) dismissal on the basis of a lack of sufficiently triggering damage, a virus exclusion that ousts coverage, or both.[12] The speed of these decisions and the success of insurers should be regarded—at least on the triggering damage question—as surprising and erroneous.[13] Although insurers have a significant array of arguments against coverage, we find them considerably less powerful than suggested by insurers and accepted by many judges to date.[14]

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[11] *Id.* In what might be termed the "first wave" of COVID-19 property insurance and business interruption cases, the majority have been brought by policyholders as plaintiffs rather than by insurers seeking a declaratory judgment of no coverage. For clarity, this article will generally use the term "policyholders" to include both named insureds and all other insureds under a policy unless insured status is important to determination of a coverage issue.

[12] *See* Baker, *supra* note 10.

[13] *See infra* Part IV.

[14] *See infra* Part III. This is not to say that insurers deserve none of these early victories. Where policies contain a sufficiently broad virus exclusion, the facts of many cases will likely make the exclusion applicable and support a finding of no coverage. As Professor Baker has noted:

In our view, each insurance coverage case needs to be decided based upon not only its particular factual context but also according to the specific policy at issue. Some policies contain a virus exclusion (which of course makes a stronger, perhaps even irrefutable, case for no coverage)[15] while many others lack any such limitation on coverage—a factor strongly favoring policyholders.[16] But the "early returns" point toward excessively impulsive and overbroad (in our view) embrace

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> Of the seven cases in which a merits-based motion to dismiss has been denied, four involve insurance policies without any virus exclusion, one involves the Hartford's Endorsement for Limited Fungi, Bacteria, or Virus Coverage (which contains a virus exclusion that could be read to apply only to losses involving defective materials), and two have virus exclusions that apply to sickness or disease.
>
> By contrast, of the eighteen cases in which a court has granted a merits-based motion to dismiss, only two don't have virus exclusions.
>
> This matters, among other reasons because the presence of a virus exclusion inhibits policyholders from pleading their cases in ways that would help them meet the requirement that their business income losses result from "physical loss of or damage to" the premises in question.
>
> Bottom line [as of Oct. 7, 2020]: insurers are winning, overwhelmingly, when their polices have virus exclusions. But they are losing, at least at the motion to dismiss stage, when their policies do not have virus exclusions.

Baker, *supra* note 10. We are, as discussed in Part IV, nonetheless disturbed by many of these early insurer victory cases because of their superficial and weak reasoning taking an excessively narrow view of what constitutes "physical loss or damage," which may have negative implications for future coverage disputes.

[15] *See infra* Part V.

[16] If nothing else, the presence of an exclusion implies, sometimes strongly in light of the language of the insuring agreement, that in the absence of an exclusion, a claim or loss is covered. As discussed in Part IV, the virus exclusion was developed to avoid potential coverage pursuant to standard issue policies. If the insuring agreement or other exclusions in those policies had sufficiently precluded coverage, there logically would have been no need for a specific virus exclusion. We appreciate that insurers may want a "belt and suspenders" approach to policy drafting and that exclusions in some cases may be added simply to solidify widely accepted understandings and to foreclose unrepresentative judicial construction of policies. But courts should also appreciate that just as often (or perhaps more frequently), exclusions are added to policies because the policies provide coverage in the absence of such exclusions.

of an insurer-sponsored conventional wisdom that COVID claims are simply not insured.[17]

In particular, we are unimpressed with insurer arguments that COVID and attendant government closure orders do not—as a matter of law—constitute "direct physical loss or damage" to covered property. To date, the majority of judges hearing COVID cases disagree. Although their views are positive law and ours are not, we remain disappointed in the quality of analysis applied in many of the COVID coverage cases, which has often been reductionist, simplistic, crabbed, and overconfident regarding textual analysis, as well as insufficiently sensitive to the value of trial proceedings for resolving these disputes.[18]

Judges granting dismissal motions without any opportunity for discovery, and denying any possibility of coverage at the metaphorical starting gate, have undermined the traditional American commitment to jury trials as well as widely accepted legal principles of insurance policy construction such as interpreting ambiguous terms against the drafter and considering policyholder reasonable expectations.[19] Where the issue is solely whether sufficient "loss" or "damage" has taken place, standard property insurance policy language is simply not as conclusive as purported by these courts. Although other defenses such as a virus exclusion may carry the day for some insurers, insurers have to date gotten much more mileage out of very weak "no-loss/no-damage" arguments than should be the case if trial judges were consistently doing a thorough job.

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[17] Consistent with discussion in Part II of this article regarding the (in our view) successful public relations efforts of insurers to paint COVID-19 business interruption claims as (to use a favorite phrase of the former President Trump) losers, the legal and insurance trade press has tended to under-report policyholder victories while giving significant attention to insurer victories, emphasizing judicial statements labeling policyholder coverage arguments as meritless. Having followed the legal and trade press thoroughly the pandemic, we were surprised upon reading Professor Baker's COVID Coverage Litigation Tracker to find that policyholders had "prevailed" on as many dismissal motions as they have (which is still a tiny fraction of the total number of motions). Baker, *supra* note 10. We put the term "prevailed" in scare quotes to emphasize that that surviving a motion to dismiss is not the equivalent of obtaining coverage—and certainly does not reflect payments that small business policyholders state they desperately need to survive. By contrast, when an insurer obtains a Rule 12 dismissal, it really has won something. In all eighteen cases where insurers have to date prevailed on dismissal motions, the court has dismissed the entire case with prejudice, leaving the policyholder with the unattractive options of appeal or accepting defeat.

[18] *See infra* Part IV.

[19] *See infra id.*

Potentially aiding and abetting this judicial failure has been substandard briefing and advocacy by policyholder counsel, many of whom are not insurance specialists but tort lawyers prosecuting coverage cases with perhaps relatively little experience or expertise about the nuances of insurance coverage law.[20] In many of the cases with outcomes we criticize, insurers have been served by better advocacy, an important factor in cases where judges also lack insurance expertise. In some other cases, a judge's background formerly representing insurers may also foreshadow pro-insurer rulings.[21] But we also posit that the bench was probably affected by widespread insurer efforts to "poison the well" against COVID-19 coverage claims through an early onslaught of pro-insurer, anti-coverage commentary in the legal press, the insurance trade press, and in mass circulation media.[22]

A more extensive and nuanced analysis of COVID coverage issues suggests to us that policyholders should be winning most of these dismissal motion cases—at least on the loss and damage issues—and proceeding further in the adjudication process. Notwithstanding some shining exceptions,[23] the first wave of decisions in these cases has been largely disappointing and reflects poorly on the legal and hyper-textual analysis of the bench. If this trend continues, the insurance industry will have

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[20] Insurers have taken the rare step of filing memoranda opposing amicus participation in Covid coverage cases, presumably because they wish the court not to have the benefit of analysis by more seasoned coverage counsel. *See, e.g.,* Defendant's Opposition to United Policyholders, National Independent Venue Association, and Washington Hospitality Association's Motion for Leave to Appear as Amici Curiae, Vita Coffee, LLC v. Fireman's Fund Ins. Co., No. 2:20-cv-01079-JCC-DWC (W.D. Wash. 2020) (noted insurer side law firm opposes, *inter alia*, submission of United Policyholders amicus brief authored by Covington & Burling partner David Goodwin, a prominent policyholder coverage attorney).

[21] *See, e.g*., Franklin EWC, Inc. v. Hartford Fin. Servs. Grp., No. 20-cv-04434 JSC, 2020 U.S. Dist. LEXIS 174010 (S.D. Cal. Sept. 22, 2020) (granting of an insurer's dismissal motion by Magistrate Judge Jacqueline Scott Corley, formerly at DLA Piper, a firm known for representing insurers that has been involved in COVID coverage litigation, sufficiently aggressively that it has opposed judicial consideration of a proffered amicus brief by United Policyholders. *See also infra* Part II.

[22] By legal press, we refer to media directed primarily at lawyers, such as *US Law Week*, *Law 360* and the like. By insurance trade press, we refer to periodicals such as *Insurance Journal*, *Business Insurance*, *National Underwriter*, *Best's Review* and electronic newsletters, bulletins, and blogs (*e.g*., Randy Maniloff's *Coverage Opinions* or the Hunton & Williams newsletters). General circulation media is aimed primarily at laypersons and runs the gamut from individual blogs or websites to major newspapers of record.

[23] *See infra* Part IV(A) (discussing well-reasoned cases finding sufficient allegations of physical loss or damage for coverage claim to proceed).

obtained an undeserved victory that is inconsistent with the extent of coverage it promised to policyholders, particularly small businesses.

The remainder of this part of the article examines the risk management and insurability issues presented by pandemic claims and identifies the principal types of first-party property insurance that could be implicated. Part II recaps the remarkable public relations campaign of insurers designed to influence both judicial and lay perception of insurance coverage for COVID-related losses. Part III examines the crucial coverage issues of whether there has been direct physical loss or damage sufficient to create coverage, acknowledging that coverage may be taken away by certain virus exclusions or other aspects of the policy or situation. Part IV briefly raises the virus exclusion contained in many policies and some challenges with it.

We conclude with concerns regarding the success of a tightly packaged, insidiously executed, and albeit factually and legally incorrect adversarial position put forth in insurance media may well have affected the initial outcomes of COVID-related coverage litigation. While we of course hope that to be untrue, when one begins to stack together some of the bizarre and frankly un-judicial goings on in these early COVID coverage cases, one has to wonder whether and to what degree concerted insurer-directed media infected the judicial outcomes. If true, that lays a haunting precedent over future coverage litigation for insurance matters both about pandemic-related losses and beyond.

B. CONSIDERING COVID COVERAGE DISPUTES IN THE BROADER CONTEXT OF THE INSURABILITY OF PANDEMIC-RELATED LOSSES

A pandemic is a "clash event,"[24] like a war or nuclear accident. Losses flowing from this event are large, uniformly repeated amongst many policyholders, and simultaneously cut across multiple insurance product lines. Insurance is built as a risk-based product, designed to buffer chance happenings of loss-related events by pooling collective risk in a pool while knowing that not all policyholders in that risk pool will experience a loss at exactly the same time.

With a pandemic, "chance" may be frustrated in that the precise manner in which risks become losses may not be fully expected (or rather modelled) by insurers. This makes it difficult for the insurer to spread risk amongst the risk pool or even amongst various lines of insurance products. While some industries in a

[24] Michelle E. Boardman, *Known Unknowns: The Illusion of Terrorism Insurance,* 93 GEO. L.J. 783, 784 (2004) (dubbing "clash events" those large-scale losses like earthquakes and nuclear disasters that affect many policyholders at once and cut across multiple insurance lines).

pandemic can be severely affected (like the travel and hospitality industries in the current COVID-19 pandemic), and most at least significantly affected (such as retailers and services), there will be some industries that actually thrive in a pandemic (such as online retailers and delivery services). It may be fair to argue that it is the job of insurers to predict and price their insurance products accordingly, as part of building a solvent insurance framework. A failure to incorrectly build and price insurance in the wake of a clash event can leave only two outcomes: financial decimation for either the policyholder or the insurer. The stakes are high.

In a pandemic situation like that with COVID-19, a downturn in commercial activity is also often related to a resulting downturn in the financial markets. This challenges an insurer's ability to capitalize on investment returns for its retained insurance premium funds. The differential between premiums obtained and losses paid out—the spread—becomes tougher to profitably manage, because the financial markets unexpected reacted as a result of the very factor causing the losses insured.

But losses realized in a pandemic are not, by nature, impossible to insure. The difficulty is with estimating the correct pricing of the insurance products that tracks the realistic risks of payouts while still maintaining a profitable baseline for the insurer.

Anything that is fortuitous can be insured, in principle. The pandemic is an unexpected event. Whether insurers choose to insure pandemic-related losses as a matter of commercial choice is, of course, itself another matter.

Pandemic-relating losses are insurable in theory because the timing of the pandemic itself is a fortuitous event. We do not know when—or if—one will strike. But even in the wake of a full-blown pandemic, there are still fortuitous aspects making insurance a potentially profitable financial product to sell. Because, as noted above, not all industries will be affected at the same time and to the same degree, insurers may still be able to structure and price insurance profitably, even during a full-blown pandemic. This is because the degree and extent of loss experienced amongst individual policyholders is fortuitous. In fact, some policyholders may profit from the pandemic in their specific industries and may have no loss at all.

An insurer's ability to properly price an insurance product that appropriately accounts for pandemic-related losses based on the underwriting risk involves three factors:

a) can the insurer properly rate the risk?
b) is the premium for the risk affordable to policyholders?
c) will the premium (along with investment income) exceed the loss?

As has probably occurred with COVID, insurance products were likely priced with the foresight of only a slight possibility of a pandemic. The insurer model may not have accounted for the various kinds of losses amongst policyholders (i.e. largely business interruption losses from governmental orders either closing businesses or telling customers to shelter at home to quell the spread of the virus).

Insurers cannot claim that the pandemic was completely unforeseen as an event. The world has seen its share of rising health epidemics in the recent decades, from Ebola to SARS to H1N1, swine flu, Zika, MERS, and HIV/AIDS. In fact, the insurance industry had a virus and bacteria exclusion approved by regulators for inclusion in property insurance policies in 2006, in direct response to the SARS virus (though this exclusion is not featured in all property policies).[25] The insurance industry also marketed specific insurance for pandemic-related losses, a product still available at the start of the COVID-19 pandemic in March 2020.[26]

However, most insurers began the COVID-19 pandemic with blanket coverage denials for policyholders' COVID-related claims. And insurers did this not on the basis of the virus exclusion most logically relevant to the issue, but instead on the argument that the policyholder has suffered no physical loss or damage.

The insurance denials prompted some governments to propose legislation to mandate either government reinsurance for pandemic-related losses,[27] or insist that insurers cover such losses, even despite actual policy coverage wording.[28] In

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[25] INSURANCE SERVICE OFFICE, ISO FORM CP 01 40 07 06 - EXCLUSION OF LOSS DUE TO VIRUS OR BACTERIA (July 6, 2006) [hereinafter ISO VIRUS EXCLUSION], https://www.propertyinsurancecoveragelaw.com/files/2020/03/ISO-Circular-LI-CF-2006-175-Virus.pdf (mentioning specifically SARS, avian flu, and influenza, as well as anthrax).

[26] *See, e.g.*, *PathogenRX, An Innovative Solution for Pandemic and Epidemic Risks,* MARSH, https://www.marsh.com/us/campaigns/pathogenrx.html (last visited Jan. 24, 2021) (which had almost no take-up prior to COVID-19); Stuart Collins, *Insurers Wary of Meeting Growing Demand for Specialist Pandemic Cover,* COM. RISK ONLINE (Apr. 9, 2020), https://www.commercialriskonline.com/insurers-wary-meeting-growing-demand-specialist-pandemic-cover/; *see also* Robert Hartwig, Greg Niehaus & Joseph Qiu, *Insurance for Economic Losses Caused by Pandemics,* 45 GENEVA RISK & INS. REV. 134, 138 (2020) (discussing the failed PathogenRX market).

[27] *See, e.g.*, Pandemic Risk Insurance Act of 2020, H.R. 6983, 116th Cong. (2020).

[28] Various state governments in New Jersey, New York, Pennsylvania, Louisiana, Ohio, Massachusetts, and South Carolina all proposed bills mandating that insurers cover COVID-19 pandemic-related losses. *See, e.g.,* The Gen. Assemb. of Pa., H.B. 2372, 2020 Sess. (Pa. 2020) ("Business Interruption Insurance Act"); State of N.Y. Assemb., A. 10226-B, 2020 Assemb. (N.Y. 2020) ("An Act in relation to requiring certain perils be covered under business interruption insurance during the coronavirus disease 2019 (COVID-19) pandemic"); State of N.Y. Senate, S. 8178, 2020 S. (N.Y. 2020) ("An Act in relation to

response, the National Association of Insurance Commissioners (NAIC) warned in correspondence to the U.S. House Committee on Small Business that such legislation requiring insurers to cover COVID-19 related losses would financially decimate the insurance industry.[29] The Insurance Commissioners argued that most insurance products were not designed or priced to provide coverage for pandemic-related losses. They also contended that "virtually every policyholder suffers significant losses at the same time." But pandemic-related losses themselves are not uninsurable in principle. Insurers may just not have properly estimated how the particular losses of this pandemic have played out and may not have priced their products accordingly. Or, perhaps, the insurance products were not designed to cover pandemic-related losses at all.

C. INSURANCE IMPLICATED IN A PANDEMIC

A pandemic such as the COVID crisis can result in insurance claims across a variety of insurance product lines, including:

a) property insurance, especially for contamination losses and business interruption losses, as well as losses arising from civil authority 'stay at home' orders or forced business closure orders;
b) liability insurance, in the event an employee or customer takes legal action against the policyholder for injury suffered as a result of failure to take reasonable health precautions;
c) workers compensation and employment insurance, for the sickness or quarantining or isolation of employees;
d) directors and officers insurance, for any liability visited by corporate decisions as a result of the pandemic; and
e) event cancellation insurance, triggered if a major event is cancelled (such as a sporting event or concert or film production).

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requiring certain perils be covered under business interruption insurance during the coronavirus disease 2019 (COVID-19) pandemic"). These bills are currently winding their way through the legislative processes.

[29] Letter from Nat'l Ass'n of Ins. Comm'rs and the Cntr for Ins. Pol'y & Rsch to The Honorable Nydia M. Veláquez, Chairwoman, U.S. House Committee on Small Business (May 20, 2020), https://naic.org/documents/government_relations_200521.pdf.

1. Business Interruption Coverage

The most active area for insurance coverage issues at this stage of the COVID-19 pandemic has been litigation arising from business losses by commercial entities, as a result of policyholder claims for losses under business interruption and civil authority insurance provisions. This has triggered interpretive debates in the courts over the meaning of business interruption and civil authority coverage contained in commercial property policies. These types of insurance products are additional coverages to the standard all-risk commercial property insurance policy.[30]

The standard commercial property policy provides coverage for losses arising from all risks to the policyholder's commercial property, save and except those risks that are specifically excluded in the policy. As a separate add-on, usually as an endorsement and for additional premiums, the policyholder can augment its property policy with various types of insurance coverage for other potential business-related losses.[31]

One such potential business-related loss is the interruption of a business' potential to generate income. This type of coverage is designed to protect the earning stream of the business in the event the business' capacity to earn income is interrupted as a result of a covered cause of loss. The coverage indemnifies the policyholder for income lost while the building restores its operations.[32]

The coverage clause in the standard property policy typically covers "direct physical loss of or damage to" insured property.[33] The business interruption coverage clause typically dictates that the insurer will pay for the loss of business income "due to the necessary suspension or delay of operations caused by direct physical loss of or damage to property." To determine insurance coverage, the policyholder must prove it suffered some "direct physical loss of or damage to property." The archetypal scenario for triggering business interruption insurance is the fire at a commercial establishment. The fire damages the storefront and the

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[30] *See* French, *supra* note 4, at 17–20; MARK S. DORFMAN & DAVID A. CATHER, INTRODUCTION TO RISK MANAGEMENT AND INSURANCE 346–47 (10th ed. 2013); EMMETT J. VAUGHAN & THERESE M. VAUGHAN, FUNDAMENTALS OF RISK AND INSURANCE 563–65 (11th ed. 2013).

[31] *See* French, *supra* note 4, at 21–30; DORFMAN & CATHER, *supra* note 30, at 346–47; VAUGHAN & VAUGHAN, *supra* note 30, at 563–65.

[32] *See* French, *supra* note 4, at 21–30; DORFMAN & CATHER, *supra* note 30, at 346–47; VAUGHAN & VAUGHAN, *supra* note 30, at 563–65.

[33] *See* JEFFREY W. STEMPEL & ERIK S. KNUTSEN, STEMPEL & KNUTSEN ON INSURANCE COVERAGE §15.01[D] (4th ed. 2015 & Supp. 2020).

business is unable to earn income until such time as the business can repair the fire-damaged storefront.

In a pandemic situation like COVID, however, the place of business is not physically destroyed but contaminated by virus, making use of the business property unsafe. Alternatively, access to the business' property may be curtailed due to governmental orders designed to curb the spread of the disease. For example, many restaurants have been ordered closed to dine-in customers and could only operate via take-out or delivery for a period of time. The question becomes whether the policyholder has suffered a "direct physical loss of or damage to" its commercial property by either contamination by virus or by a governmental order restricting property access or use.

Insurers will likely stress that commercial property policies are designed to cover physical damage to tangible property—like fire damage. One way of looking at the issue is that any loss of business income should be tied to the necessary interruption of a business' income stream as a result of something that harms the property in a way that would interfere with a policyholder using its property as a place to earn income. If the property itself is not damaged, the coverage should not be triggered.[34]

Policyholders, however, likely believe that they purchased business interruption insurance as an add-on to their property coverage in order to insure a capital asset—the income-earning power of their business (hence the name "business interruption insurance"). If that income stream is interrupted due to an interference with their use of their property—whether by virus contamination or by orders of government—their reasonable expectation would be that the business interruption portion of their policy would cover such losses. The property policy is, after all, "all-risk" property insurance, and the business interruption coverage is tied to that "all-risk" concept. Policyholders who purchased business interruption insurance would expect coverage for an inability to use their property to earn business income.[35]

2. Civil Authority Coverage

A common extension to the business interruption coverage in a commercial property policy is civil authority coverage. Under this coverage, a policyholder can insure its lost business income stream if access to its property is impaired or prohibited due to the order of some civil authority (i.e. a government). Some wordings of this coverage specifically require that the civil authority's order is due

[34] *See* French, *supra* note 4, at 51.
[35] *See* French, *supra* note 4, at 68–71.

to the direct physical loss of or damage to property adjacent to the policyholder's insured property as a result of a covered cause. A common coverage clause for civil authority insurance states: " . . . if an order of civil or military authority limits, restricts or prohibits partial or total access . . . provided such order is the direct result of physical damage of the type insured."[36] The classic example is the burned warehouse that sits next to the policyholder's place of business. To keep people in the adjacent properties safe, a civil authority could ban access to a policyholder's property simply because it is close to another property exhibiting unsafe characteristics (like the unstable structure after a fire).

Business interruption insurance claims due to COVID have arisen under the civil authority coverage provisions, resulting from losses due to state or municipal "shelter in place" orders or the closure of non-essential businesses or the modification of the use of businesses, such as eliminating indoor dining at restaurants. The risk of COVID with its airborne and highly contagious quality prompted many civil authorities to issue various orders in an attempt to contain the disease.

Courts examining civil authority coverage tend to look to causation arguments: was the order the result of directly physical loss of or damage to property? If so, is such a covered cause of loss? Policyholders have argued that they suffered loss of use or loss of functionality of their property due to the civil authority orders, and that constitutes a direct physical loss of property. However, insurers have argued that the language of most coverage grants demands that policyholders must also prove that alleged property damage to some property adjacent to the policyholder's place of business actually led to the civil authority making the order.

3. Contingent Business Interruption Coverage

Contingent business interruption coverage is similar to business interruption coverage except that the policyholder's income stream is affected by loss or damage to a related business' property, and not the property of the policyholder. This coverage is commonly implicated in a manufacturer setting, where a supplier suffers a loss and the manufacturer cannot obtain a needed component in a timely fashion and suffers a business interruption.[37]

For example, if a tire manufacturer suffers a fire at the tire plant and is unable to ship its tires to auto makers because of fire damage to the plant, the auto makers will likely have a business interruption loss due to the inability to get tires

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[36] *See* STEMPEL & KNUTSEN, *supra* note 33, at §28.04.

[37] *See* French, *supra* note 4, at 21–30; Dorfman & Cather, *supra* note 30, at 346–47; Vaughan & Vaughan, *supra* note 30, at 563–65.

in a timely manner from their supplier. The auto maker can then make a contingent business interruption claim in that, although it did not suffer the loss itself on its own property, its supplier did, and that loss to the supplier affected the policyholder's own business income stream. The key to coverage for contingent business interruption insurance is that, like business interruption insurance, the supplier must have suffered some "direct physical loss of or damage to" property as a result of a cause covered by the policyholder's all-risk insurance.

4. Ingress/Egress Coverage

Ingress/egress coverage is also sub-coverage that may be included in business interruption coverage. It provides coverage for losses arising if access to a policyholder's property is impeded through some reason other than by a civil authority order (i.e. blocked due to construction debris). To date, this coverage has not yet been implicated in any court decisions deciding COVID pandemic-related coverage issues. This makes sense as it was civil authority orders that largely affected property access for policyholders.

II. INSURER PUBLIC RELATIONS BLITZ: INSURERS PUSH THEIR ANTI-COVERAGE MESSAGE

As previously noted, COVID-19 became recognized as a major public health issue likely to adversely impact commerce in early March 2020. It was fairly clear at the outset, particularly when citizens began to stockpile supplies and stay indoors and when governments issued closure orders, that COVID would have a serious negative impact on many businesses, particularly entertainment, dining, and tourism.[38]

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[38] *See* French, *supra* note 4, at 1–3; *Why Are Markets Collapsing? How Bad Will COVID-19 Really Be?,* KNOWLEDGE@WHARTON (Mar. 16, 2020), https://knowledge.wharton.upenn.edu/article/why-are-the-markets-collapsing-how-bad-will-covid-19-really-be ("markets are acting as if we are going to encounter the worst-case scenario") (italics removed). The actual downturn in these areas of commerce has perhaps been even worse than anticipated due to the difficulty in containing COVID, resulting in a quilted cycle of closures and declining customer patronage that has perhaps lasted even longer than predicted. *See* Zoe Wood, *How the Cineworld Closures Could Turn Leisure Parks into a Disaster Movie*, THE GUARDIAN (Oct. 10, 2020 03:00 EDT), https://www.theguardian.com/business/2020/oct/10/how-the-cineworld-closures-could-turn-leisure-parks-into-a-disaster-movie (describing massive movie theatre closures and layoffs and ripple effect on bars, restaurants, and shops that benefitted from entertainment traffic). *Accord* Julian Kozlowski, Laura Veldkamp, & Venky Venkateswaran,

In response to the COVID-19 pandemic, insurers quickly took control of the insurance coverage message in the media: there will be no coverage for COVID-19 related losses.[39] Typical of the industry line were statements by insurance executives that "[p]andemics are not insurable because they are too widespread, severe, and unpredictable to underwrite" and that "[c]ommercial-property insurance policies that include business-interruption coverage generally are not intended to cover disease- or pandemic-related losses."[40]

Another prominent insurer executive claimed to "see very minimal loss exposure from this" due to the addition of coverage-restricting language in policies

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Scarring Body and Mind: The Long-Term Belief-Scarring Effects of COVID-19 (Nat'l Bureau of Econ. Rsch., Working Paper No. 27439, June 2020), https://www.nber.org/system/files/working_papers/w27439/w27439.pdf (finding that "long-run costs for the U.S. economy" from adverse psychological impact of pandemic will be "many times higher than the estimates of the short-run losses in output. This suggests that, even if a vaccine cures everyone in a year, the COVID-19 crisis will leave its mark on the US economic for many years to come.").

[39] *See, e.g.*, Caroline Glen, *Insurers Are Telling Businesses Their Policies Don't Cover Coronavirus Shutdown. John Morgan Attorneys Say They're Wrong*, ORLANDO SENTINEL (May 4, 2020), https://www.orlandosentinel.com/coronavirus/jobs-economy/os-bz-coronavirus-insurance-denials-morgan-lawsuits-20200504-pbrpq6z7ofbevau67cpgq4nzqi-story.html; Ellen Ioanes, *Does My Business-Interruption Insurance Cover Closing Because of COVID-19?*, BARRON'S (June 17, 2020 5:30 AM), https://www.barrons.com/articles/does-my-business-interruption-insurance-cover-closing-because-of-covid-19-51592386201; Leslie Scism, *Companies Hit by COVID-19 Want Insurance Payouts. Insurers Say No.*, WALL ST. J. (June 30, 2020 10:24 AM), https://www.wsj.com/articles/companies-hit-by-covid-19-want-insurance-payouts-insurers-say-no-11593527047. *See also* INS. INFO. INST., *Insurance Industry Provides Interactive 'Explainer' to Help Navigate Business Interruption Insurance, III* (Oct. 16, 2020), https://www.iii.org/pres-release/insurance-industry-porovides-interactive-explainer-to-help-navigate-business-interruption-insurance-101620. The navigation tends to leave policyholders on the shoals of no coverage as the III Explainer consistently takes a narrow view of the scope of coverage and, in particular, contends that most all COVID-related coverage is not covered. *Accord Business Interruption Insurance: An Interactive Explainer Outlining the Case for a Federal Solution to Pandemic Relief*, FUTURE OF AM. INS. & REINSURANCE, https://fairinsure.org/business-interruption-insurance/?utm_source=Board+of+Directors&utm_campaign=5ca10385b4-EMAIL_CAMPAIGN_2018_08_15_11_45_COPY_01&utm_medium=email&utm_term=0_0934a86008-5ca10385b4-122588685.

[40] *See* Ioanes, *supra* note 39 (quoting David Sampson, president and CEO of the American Property Casualty Insurance Association (APCIA)).

because of "past pandemics and/or partial pandemics."[41] Swinging into attack mode, this industry leader also took the by-now almost obligatory insurer swipe at plaintiff counsel and made it clear that seeking coverage would not be for the faint of heart: "Lawyers and the trial bar will attempt to torture the language on standard industry forms and try to prove something exists that actually doesn't exist . . . ." "The industry will fight this tooth and nail. We will pay what we owe."[42]

Whether this evolved to be the message over a short period of time, or whether it was a concerted industry effort (likely the latter), we believe it made an impact on the subsequent insurance coverage court decisions about COVID-related claims. It provides an interesting example of insurers seizing the messaging opportunity to potentially affect legal decisions. Making use of extra-legal media messaging to impact the legal sphere is a useful tactic for prospective litigants and insurers seem to be good at it.

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[41] *See* Leslie Scism, *U.S. Businesses Gear Up for Legal Disputes with Insurers Over Coronavirus Claims*, WALL ST. J. (Mar. 6, 2020 10:00 AM), https://www.wsj.com/articles/u-s-businesses-gear-up-for-legal-disputes-with-insurers-over-coronavirus-claims-11583465668 (quoting Chubb Ltd. CEO Evan Greenberg, however "Chubb declined to comment further" on the issue when asked by the Journal reporter*). See also* Maria Sassian, *Triple-I CEO Tells U.S. House—Global Pandemics are Uninsurable,* INS. INFO. INST. (May 21, 2020), https://www.iii.org/insuranceindustryblog/triple-i-ceo-tells-u-s-house-global-pandemics-are-uninsurable/ **(**"'An event like a global pandemic is uninsurable [said the executive.] Unlike a typical covered catastrophe, which is limited in terms of geography and time, pandemics have the potential to impact everywhere, all at once . . . . As such, this type of magnitude requires government resources to step in and provide support.").

[42] *See* Scism, supra note 39 (quoting Chubb Ltd. CEO Evan Greenberg).

Media targets included both the legal press,[43] the insurance trade press[44] as well as the business press,[45] and even the mainstream lay press read by the average public[46]

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[43] *See, e.g.*, Larry P. Schiffer, *Does the Novel Coronavirus Cause Direct Physical Loss of or Damage to Property?*, NAT'L L. REV. (July 13, 2020), https://www.natllawreview.com/article (concluding that "[b]ased on the case law and the nature of the novel coronavirus, it appears unlikely that courts will conclude that viral contamination causes 'direct physical loss.'"); *Insurers' COVID-19 Notepad: What You Need to Know Now*, CROWELL MORING (June 9, 2020), https://www.crowell.com/NewsEvents/AlertsNewsletters/all/Insurers-COVID-19-Notepad-What-You-Need-to-Know-Now-Week-of-June-8 (suggesting that coverage unlikely for COVID-related claims); Lauraann Wood, *Insurer Says Policy Isn't Triggered in COVID-19 Coverage Suit*, LAW360 (July 14, 2020 3:56 PM), https://www.law360.com/articles/1291736/insurer-says-policy-isn-t-triggered-in-covid-19-coverage-suit.

> Even if the virus had been present on the covered businesses' properties, it wouldn't constitute direct physical loss or damage because it doesn't cause 'a tangible change to the physical characteristics of property,' [the insurer argued]. COVID-19 isn't incorporated into their properties' physical structure, doesn't require a building's physical alteration for removal 'and does not render the building unfit for use,' it said.
>
> 'Rather, the coronavirus can be removed from surfaces with soap and water and rendered inert with various common household disinfectants, including bleach,' [said the insurer.] '[The insureds'] alleged losses are at most economic losses, not a direct physical loss or damage.'
>
> The businesses also aren't entitled to coverage under the civil authority provision for additional coverage under their policies, which 'has a very specific set of terms and conditions that must be met,' [the insurer represented to the court.]

Wood, *supra*.

[44] *See, e.g.*, Jeff Dunsavage, *COVID-19 Wrap-up: BI Coverage Continues to Make Headlines,* TRIPLE-I BLOG (May 21, 2020**),** https://www.iii.org/insuranceindustryblog/covid-19-wrap-upbi-coverage-continues-to-make-headlines **(**"The *Post* interviewed Triple-I CEO Sean Kevelighan and Triple-I non-resident scholar Michael Menapace, who explained why the suits are unreasonable and threaten the insurance industry's solvency. 'The insurance business works by spreading risk around so the industry isn't hit all at once with claims,' Kevelighan says. 'A pandemic disrupts business far and wide, with no end date in sight.'"); *Focus on Facts, Not Media Misinformation: Berkley*, CARRIER MGMT (June 7, 2020), https://www.carriermanagement.com/news/2020/06/07/207575.htm?print (**"**Arguing that the media has been fed misinformation by

the plaintiffs bar, the chief executive officer of a property/casualty insurer said facts will win out on debates over business interruption coverage disputes related to COVID-19 shutdowns.") (referring to W. Robert Berkley, Jr., president and CEO of WR Berkley); Stephan Kahl, *Munich Re to Stop Selling Pandemic Business Coverage*, INS. J. (Sept. 11, 2020), https://www.insurancejournal.com/news/international/2020/09/11/582141.htm; *Beazley Hikes Estimate for COVID-19 Related Claims Amid Resurgence in Virus*, SHARES MAG. (Sept. 22, 2020 07:30), https://www.sharesmagazine.co.uk/news/market/7092096/Beazley-hikes-estimate-for-Covid-19-related-claims-amid-resurgence-in-virus (estimating range of exposure from $170 to $350 million net of reinsurance).

[45] *See, e.g.*, Leslie Scism, *U.S. Businesses Gear Up for Legal Disputes with Insurers Over Coronavirus Claims*, WALL ST. J. (Mar. 6, 2020 10:00 AM), https://www.wsj.com/articles/u-s-businesses-gear-up-for-legal-disputes-with-insurers-over-coronavirus-claims-11583465668; Ioanes, *supra* note 39; Katherine Chiglinsky, *Virus Fight Insurers Thought They'd Dodged Is Looming Anyway*, WASH. POST (Mar. 24, 2020 11:20 AM), https://www.washingtonpost https://www.washingtonpost.com/business/on-small-business/virus-fight-insurers-thought-theyd-dodged-is-looming-anyway/2020/03/24/aef84e06-6de1-11ea-a156-0048b62cdb51_story.html; Kate Rogers & Betsy Spring, *On Main Street, Business Owners Push for Greater Protection from Coronavirus-related Lawsuits*, CNBC (June 15, 2020 1:37 PM), https://www.cnbc.com/2020/06/12/on-main-street-a-push-for-protection-from-coronavirus-related-lawsuits.html ("'It turns out that business interruption insurance is not what it sounds like,' [Robert Cresanti, president and CEO of the International Franchise Association] said. 'Most of the insurance companies are telling our people that business interruption insurance is actually business destruction insurance. So if your business is burned down or destroyed by a flood, you're covered. But you're not [covered] in a crisis like this where your business is truly interrupted.'"); Karen Epper Hoffman, *Business Interruption: Insurers Balk at Paying Claims*, CFO.COM (Sept. 10, 2020), https://www.cfo.com/risk-management/2020/09/pandemic-losses-out-in-the-cold ("Robert Gordon, senior vice president for policy, research, and international for the American Property Casualty Insurance Association (APCIA), says that because government emergency orders closed businesses to limit human transmission of COVID-19 and not because there had been direct property loss or damage, business interruption policies are not relevant.").

[46] *See, e.g.*, Ron Hurtibise, *Sorry, That's Not Covered: Insurers Fight Businesses Over COVID-19 Shutdowns*, S. FLA. SUN SENTINEL (Sept. 12, 2020 8:55 AM), https://www.sun-sentinel.com/business/fl-bz-owners-losing-covid-related-business-interruption-suits-20200912-46jlyxsftjenvlyrxg4tfbqyam-story.html ("the industry has reinforced its message by boasting about nearly every court ruling that has gone its way. 'Another court agrees: Business Interruption Insurance Does Not Cover Pandemic-Related Losses,' said the subject line of an email release by the Insurance Information Institute, a trade group created by the industry to educate consumers about insurance-related issues."); Judith Bachman, *Judges Are Deciding Whether Business Interruption Policies Cover Pandemic-Related Losses*,

as well as scholarly journals.[47] When insurers prevailed in litigation, victory was quickly trumpeted.[48]

A similar public relations campaign by small business policyholders was harder to mount given the disparate number and dispersion of random policyholders with potential claims.[49] Although plaintiff law firms fulfilled some of this function in banging the drum for coverage, their efforts were (in our view) problematic in that many of these lawyers were not insurance coverage specialists from experienced policyholder-side coverage firms. In addition, early pro-coverage efforts were (in our view) too grandiose and not well-targeted.

For example, plaintiff firms sought mass consolidation of claims, including a request for consolidation by the federal Judicial Panel on Multi-District Litigation

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ROCKLAND CNTY. BUS. J. (Oct. 8, 2020), https://rcbizjournal.com/2020/10/08/judges-are-deciding-whether-business-interruption-policies-cover-pandemic-related-losses.

[47] *See, e.g.*, Robert Hartwig, Greg Niehaus & Joseph Qiu, *Insurance for Economic Losses Caused by Pandemics*, 45 GENEVA RISK & INS. REV. 134, 134 (2020) ("Private insurance coverage for economic losses caused by pandemics is limited [due in large part] to the high levels of capital that would be required to credibly insure pandemic economic losses with cross-sectional pooling mechanisms.").

[48] Leslie Scism, *Insurance Firms Gain Early Lead in Coronavirus Legal Fight With Businesses*, WALL ST. J. (Sept. 1, 2020 9:00 AM), https://www.wsj.com/articles/insurers-gain-early-lead-in-covid-19-legal-fight-with-businesses-11598965200 ("Insurers say the policies are intended to help policyholders as they recover from events, such as fires, that lead to repairs and rebuilding, and were never intended to cover virus-related claims."); Alison Frankel, *Latest COVID-19 Insurance Coverage Loss Shows Narrowing Path for Policyholders*, REUTERS (Sept. 15, 2020 6:54 PM), https://www.reuters.com/article/legal-us-otc-insurance-idUSKBN2663HC; Andrew G. Simpson, *Judges Nix Consolidating COVID Business Interruption Suits Against Big Insurers*, INS. J. (Oct. 4, 2020), https://www.insurancejournal.com/news/national/2020/10/04/585092.htm.

[49] This is not to say that the business community did not on occasion make itself heard on the issue. *See, e.g.*, Stephen Gandel, *Companies Say Insurance Companies Are Stiffing Them Over Coronavirus Losses*, CBS NEWS (Sept. 21, 2020 11:16 AM), https://www.cbsnews.com/news/covid-insurance-business-continuity-interruption-declined-coverage; Kate Rogers & Betsy Spring, *On Main Street, Business Owners Push for Greater Protection from Coronavirus-related Lawsuits*, CNBC (June 12, 2020), https://www.cnbc.com/2020/06/12/on-main-street-a-push-for-protection-from-coronavirus-related-lawsuits.html. *See also,* Tim Carman, *Restaurants Are Suing Insurance Companies Over Unpaid Claims—And Both Sides Say Their Survival Is at Stake*, WASH. POST (May 19, 2020 1:37 PM), https://www.washingtonpost.com/news/voraciously/wp/2020/05/19/restaurants-are-suing-insurance-companies-over-unpaid-claims-and-both-sides-say-their-survival-is-at-stake (reporting both insurers and small businesses taking positions that adverse coverage decisions will be financially ruinous).

(MDL), which almost everyone (including the judges on the Panel) viewed as inapt unless confined to the same policy forms of a single insurer in light of the varying facts and policies of different cases.[50] More extremely, lawyers and legislators sympathetic to business sought to legislatively require coverage by insurers regardless of the policies at issue—a seemingly rather clear attempt to violate the Contract Clause of the U.S. Constitution that gave insurers a rather effortless public relations victory.[51]

As discussed below, we find the insurers' industry-wide disparagement of coverage as legally misplaced as it may have been rhetorically brilliant. While we cannot help but admire the manner in which insurers moved quickly and uniformly to spin public opinion against coverage, we are dismayed that the tactic seems to have worked on judges. There are real arguments to be made about whether and how policyholders may have coverage for COVID-related losses. In fact, we think the insurance industry's main contention about coverage—the "physical loss or damage" requirement—can be refuted in most cases. But this requires a more searching analysis of the question and less reflexive recoil than has been displayed in the bulk of court decisions to date.

In several states, legislation was introduced to require insurers to pay for lost policyholder revenue. There was also congressional inquiry pushing for such coverage without regard to the actual insurance policy terms at issue in a particular case. Predictably—and correctly in our view—insurers opposed any such legislative mandates or compulsion as violative of the Contract Clause of the U.S. Constitution.[52] In doing so, they took the doctrinaire position—with which we

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[50] *See* Andrew G. Simpson, *Judges Nix Consolidating COVID Business Interruption Suits Against Big Insurers*, INS. J. (Oct. 4, 2020), https://www.insurancejournal.com/news/national/2020/10/04/585092.htm. However, more limited consolidated treatment has been approved for particularized groupings of policies with the same operative language. *See* Jacob Rund, *Ski Pass Insurance Row Highlights Complex Route for Virus Suits*, BLOOMBERG L. (Oct. 20, 2020, 6:31 AM), https://news.bloomberglaw.com/insurance/ski-pass-insurance-row-highlights-complex-route-for-virus-suits (approving consolidation of 30 actions by policyholders against Society Insurance "for denying business interruption claims of restaurants and other hard-hit shops" as well as skiers' lawsuits against Arch Insurance Co. and United Specialty Ins. Co. for denials of cancellation insurance purchased in connection with season-long ski passes). Regarding MDL proceedings generally, see DAVID F. HERR, MULTIDISTRICT LITIGATION MANUAL: PRACTICE BEFORE THE JUDICIAL PANEL ON MULTIDISTRICT LITIGATION (2020 ed.).

[51] *See infra* text accompanying notes 51–53.

[52] *See* Letter from Nat'l Ass'n of Ins. Comm'rs & Ctr. for Ins. Pol'y and Rsch. to Members of Cong. (May 20, 2020) (supporting insurer arguments against legislation forcing

disagree—that business interruption insurance was never intended (apparently under any circumstances) to provide coverage for any losses related to infectious disease like COVID.[53]

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coverage). *See also* H.B. 589, 133d Gen. Assemb., 2019-2020 Sess. (Ohio 2019) introduced by Representatives Crossman and Rogers. The bill would "require insurers offering business interruption insurance to cover losses attributable to viruses and pandemics and to declare an emergency" that presumably would support further orders providing for government-mandated closure of non-essential businesses. *See also* Elizabeth Blosfield, *Despite Insurance Industry Concerns, More States Introduce COVID-19 BI Bills*, INS. J. (Apr. 15, 2020), https://www.insurancejournal.com/news/east/2020/04/15/564920.htm ("'It's just not constitutional,' Don Hayden, co-founder and partner of Mark Migdal & Hayden, added. 'I mean, what you're essentially doing is creating insurance where there is nothing. You're essentially throwing out the underwriting and the risk evaluation that insurance companies have done before writing a policy and saying, "You have to cover this. Even though you had expressly said that you would not cover it in your exclusion and in your insurance agreement."'"). *But see* Mark A. Packman, *Constitutionality Under the Contracts Clause of Proposed Legislation Enabling Policyholders to Obtain Insurance Coverage for Coronavirus Claims*, 55 TORT TRIAL & INS. PRAC. L.J. 509 (2020) (concluding that such legislation is constitutional due to emergency nature of pandemic and economic harm to particular businesses).

[53] Erin Ayers, *Insurers Decline Congress' Request To Pay All COVID-19 Business Interruption Claims*, ADVISEN FRONT PAGE NEWS (Mar. 23, 2020), https://www.advisen.com/tools/fpnproc/fpns/articles_new_1/P/363166470.html?rid=363166470&list_id=1 (responding to congressional inquiry re insurer coverage of COVID business loss claims, insurer interest groups state that "[b]usiness interruption policies do not, and were not designed to, provide coverage against communicable diseases such as COVID-19") (statement from leadership of American Property Casualty Insurance Association, National Association of Mutual Insurance Companies, Council of Insurance Agents and Brokers, and Independent Insurance Agents & Brokers of America) (also taking position that the members of these insurance industry organizations "include many small businesses and employers grappling with the same issues as many businesses."). *See also id.* (acknowledging that COVID coverage claims will be brought concerning other types of insurance policies); Jeff Sistrunk, *4 Coronavirus Developments Insurance Lawyers Should Know*, LAW360 (Mar. 20, 2020, 5:31 PM), https://www.law360.com/articles/1255415/4-coronavirus-developments-insurance-lawyers-should-know (listing the four important topics with subheadings as follows: "Insurers Spurn Call to Expand Business Interruption Coverage"; "NJ Lawmakers Mull Business Interruption Coverage Bill"; "House Lawmakers Press Travel Insurers on Claim Denials"; and "Calif. Regulator Seeks 'Grace Period' on Policy Cancellations").

Insurers also consistently maintained that they would go broke and the insurance industry would be destroyed if carriers were forced to provide COVID coverage.[54] Risk managers and brokers, who are normally viewed as representing policyholder interests, tended to align with insurers, presumably because they feared disruption of the industry more than denial of coverage to policyholder employers or clients, many of which were likely to fail in the absence of prompt payment of insurance coverage.[55] Regulators also sided with insurers,[56] in our view, without sufficient reflection and consciousness of their mission as public servants.[57] These entities also seemed to overlook the likely perception of policyholders who expected (perhaps with sufficient objective reasonableness to obtain coverage) that the premiums they had paid for years for something deemed "business interruption" coverage would provide at least some assistance in the face of the largest business interruption of this type in a century.[58]

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[54] *See, e.g.*, Kate Smith, *Pandemic Partnerships*, BEST'S REV. (Aug. 2020), news.ambest.com/articlecontent.aspx?refnum=299433&altsrc=43 ("Even with pandemic excluded from most business interruption policies, COVID-19 is expected to cost the insurance industry more than $200 billion."). *But see* Kate Smith, *The COVID Catastrophe*, BEST'S REV. (June 2020), http://news.ambest.com/ArticleContent.aspx?pc=1009&altsrc=158&refnum=297254 (stating that "The COVID-19 outbreak could dwarf other catastrophe losses insurers have seen. . . ." but also noting that "[e]ven with the economic downturn, the insurance industry, on the whole, is in a strong capital position"). Carman, *supra* note 49. *Accord*, Andrew G. Simpson*, P/C Insurers Put a Price Tag on Uncovered Coronavirus Business Interruption Losses*, INS. J., (Mar. 30, 2020), https://www.insurancejournal.com/news/nationa/2020/03/30/562738.htm.

> "Pandemics are an extraordinary catastrophe that can impact nearly every economy in the world, so it is hard to predict and manage the risk," Sean Kevelighan, CEO of the Insurance Information Institute, stated. "Pandemic-caused losses are excluded from standard business interruption polices because they impact all business, all at the same time."
>
> Moreover, he said, the exclusion for pandemic-caused losses have been incorporated into standard business interruption policies for years.

Simpson*, supra. See also* Elizabeth Pineau & Maya Nikolaeva, *Insurer AXA Must Pay Restaurant's COVID-19 Losses*, French Court Rules, REUTERS (May 22, 2020, 2:08 PM) https://uk.reuters.com/article/us-health-coronavirus-insurance-axa/french-court-orders-insurer-axa-to-pay-restaurants-covid-19-losses-idUKKBN22Y2LR. ("AXA reacts to decision by stating that it would appeal."); Elizabeth Blosfield, *Despite Insurance Industry*

Concerns, More States Introduce COVID-19 BI Bills, INS. J. (Apr. 15, 2020), https://www.insurancejournal.com/news/east/2020/04/15/564920.htm.

> "I think in layman's terms, [legislation forcing payment of covid claims] would implode the industry," Doug Jones, managing director of JAG Insurance Group, told *Insurance Journal* in a March webinar on business interruption and the coronavirus. "At the end of the day, the ripple effect of what that would cause down the road, and I'm talking short-term, not long-term; I'm talking about months from now, not years from now. It would be difficult for anybody to buy any type of insurance."
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> Additional concerns among the insurance industry about this type of legislation surround The Contracts Clause in the U.S. Constitution, which places limitations on states' ability to interfere with private contracts.
>
> "It's just not constitutional," Don Hayden, co-founder and partner of Mark Migdal & Hayden, added. "I mean, what you're essentially doing is creating insurance where there is nothing. You're essentially throwing out the underwriting and the risk evaluation that insurance companies have done before writing a policy and saying, 'You have to cover this. Even though you had expressly said that you would not cover it in your exclusion and in your insurance agreement.'"

Blosfield, *supra*.

[55] The tone of reporting appears to suggest that this element of the risk management and insurance community tacitly accepted widespread lack of coverage and economic danger to the insurance industry. As reported in one publication geared toward risk managers and brokers only 14 percent of surveyed risk managers and corporate insurance buyers planning to add new pandemic coverage. Andy Toh, *2020 Property Insurance Survey*, BUS. INS. 31 (June 2020). But 27 percent state that their current policies provide coverage related to diseases and epidemics while 49 percent deny having such coverage. *Id.* 41 percent of policyholders are expecting to make a pandemic claim, with 28 percent not planning such claims. *Id*

> 67% of risk professional expect direct business interruption losses due to COVID-19. 77% expect the losses to be over $1 million, of which 36% estimate losses to be more than $25 million. 91% support a federal backstop for pandemic risk insurance similar to the Terrorism Risk Insurance Act. 65% of risk professionals would be willing to pay up to 5% more in premium for pandemic risk insurance coverage.

Claire Wilkinson, *Pressure Builds for Pandemic Backstop*, BUS. INS. 4 (May 2020). A draft Pandemic Risk Insurance Act of 2020 then circulating "would establish a federal backstop

for business interruption losses resulting from a future pandemic and would be triggered when insurance industry losses exceed a $250 million threshold and capped at $500 billion . . . ." *Id.* "The growing momentum among insurance buyers and others for a government backstop to cover pandemic risks comes as insurers continue to maintain that most commercial property policies do not provide coverage for business interruption losses arising form the COVID-19 pandemic." *Id.*

> The question of whether a potential Pandemic Risk Insurance Act should be retroactive to the to the COVID-19 pandemic is an issue RIMS is still exploring, she [Mary Roth, RIMS CEO] said
>
> . . . .
>
> RIMS doesn't want to 'get into the business of' altering contractual agreements that were 'legally and freely entered into,' said Whitney Craig, RIMS government relations director.
>
> 'We would be very wary of supporting legislation that has that. We don't want to bankrupt an industry that we as risk managers rely on,' Ms. Craig said.

Id.

[56] *See* Leslie Scism, *Companies Hit by Covid-19 Want Insurance Payouts—Insurers Say No*, WALL ST. J. (June 30, 2020, 10:24 AM), https://www.wsj.com/articles/companies-hit-by-covid-19-want-insurance-payouts-insurers-say-no-11593527047. ("Insurers have some conceptual backing for their stance that business-interruption coverage isn't meant for pandemics. The National Association of Insurance Commissioners, a standards-setting group for state regulators, says pandemics violate a cardinal principle of insurance, which is that large numbers of policyholders pool their risk to fund a few losses at any one time. In a pandemic, almost all policyholders suffer losses, and simultaneously.").

[57] We appreciate NAIC's concern that large coverage obligations could imperil the insurance system generally. But we remain more than a little puzzled that a regulatory group charged with protecting the public seems uninterested in supporting policyholders, particularly small business policyholders, in cases where there is arguable coverage. Insurers are in the business of risk transfer and insurance is one of the largest, most profitable industries in the world. Although it may be regrettable if an insurance company (or several or dozens) should fail, we consider it at least equally regrettable if policyholders who paid for coverage fail after wrongfully being denied coverage due to fears of bankrupting the insurance industry. Past insurer claims that their financial sky was falling proved to be exaggerated, something regulators should know and appreciate. *See* Jeffrey W. Stempel, *Assessing the Coverage Carnage: Asbestos Liability and Insurance After Three Decades of Dispute*, 12 CONN INS. L. J. 349, 353 (2006) (citing asbestos mass torts, despite the massive costs, estimated to have been only a three percent drag on insurer earnings).

In addition, we note that there is more than a little disconnect between NAIC as an entity tending to back the insurer mantra that "everyone knows pandemics are not insured" while

As noted, insurers or their counsel campaigned in earnest to label COVID an uncovered loss in both the general media and what might be termed the insurance trade media.[59] Part of the insurer effort to disparage coverage claims was the continued assertion that nearly all property insurance with business interruption coverage also contained clear virus exclusions precluding coverage.[60] This claim may be overstated. In the COVID coverage decisions to date, more than twenty percent of the policies at issue lacked a virus exclusion.[61] Thus, even if the insurer contention that "most" property policies have such an exclusion, there appear to be

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some individual state commissioners have gone in the opposite direction and attempted to force coverage irrespective of the language, intent, and purpose of particular policies. Our preferred position is between these two extremes.

[58] Matthew Lerner, *Policy Wordings Tested by Interruption Losses*, BUS. INS. 27 (May 2020).

> Business interruption claims have fast become one of the principal legal battlefronts between commercial policyholders and insurers since the outbreak of the coronavirus pandemic.
>
> Dozens of businesses, including numerous restaurants, have filed state and federal lawsuits against their insurers seeking declaratory rulings that income lost due to the government-mandated lockdowns is covered by insurance.
>
> Insurers argue that many of the policies include exclusions for virus related losses and most of those that don't still won't cover lost income because physical damage to an insured property must occur to trigger claims payments.

Id.

[59] *See* CARRIER MGMT, supra note 44. *See, e.g.*, *Larry* P. Schiffer, *Does the Novel Coronavirus Cause Direct Physical Loss of or Damage to Property?*, X NAT'L L. REV. 114 (Apr. 13, 2020), https://www.natlawreview.com/article/does-novel-coronavirus-cause-direct-physical-loss-or-damage-to-property (concluding that "[b]ased on the case law and the nature of the novel coronavirus, it appears unlikely that courts will conclude that viral contamination causes 'direct physical loss.'").

[60] Erin Ayers, *Insurers Decline Congress' Request to Pay All COVID-19 Business Interruption Losses*, ADVISEN FRONT PAGE NEWS (Mar. 23, 2020), https://www.advisen.com/tools/fpnproc/fpns/articles_new_1/P/363166470.html?rid=363166470&list_id=1 ("The vast majority of commercial property insurance policies contain not only direct physical damage, but also contain exclusions for viral/bacterial contamination due to the unpredictability of the risk.").

[61] *See* Baker*, supra*, note 10 (visited Oct. 21, 2020).

a large number of cases where policyholders have a substantially better chance of success than suggested by the insurance industry shibboleth of no coverage.

As part of its aggressive "no coverage" strategy, insurers did more than rest on the virus exclusion (which we agree can be a strong defense to coverage where the policy actually contains such a limitation) even when policies at issue contained the exclusion. Rather, insurers dug in on a remarkable first line of defense: that COVID did not and could not cause *any* direct physical loss or damage to property, which is a prerequisite to most commercial property and business interruption coverage.

> [T]he mere **threat** of COVID-19 at the property or the **preemptive closure** of businesses due to the threat of COVID-19 should not be considered "direct physical loss or damage" to property. Additionally, neither **government-ordered closure** of businesses nor a **government's official statement** regarding COVID-19 damage at properties generally should be sufficient for a court to find "direct physical loss or damage" to a particular property. However, those insured that can prove the actual presence of the virus on the surfaces of or otherwise in covered property may be able to establish "direct physical loss or damage" to property.[62]

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[62] Edward M. Koch & Elizabeth C. Dolce, *"Direct Physical Loss or Damage": The Gatekeeper to Property Insurance Coverage and COVID-19*, WHITE & WILLAIMS (Mar. 24, 2020), https://www.whiteandwilliams.com/resources-alerts-Direct-Physical-Loss-or-Damage-The-Gatekeeper-to-Property-Insurance-Coverage-and-COVID-19.html (emphasis in original). *Accord*, Randy Maniloff, *First Coronavirus Coverage Suit Filed for Business Interruption*, COVERAGE OPS. (Mar. 17, 2020), https://www.coverageopinions.info/Vol9Issue2/FirstCOVIDcase.html.

> In general, and putting aside any precise policy language that may apply, one critical requirement, for the potential availability of business interruption insurance, is that there has been physical damage to property. This is either to the insured's own covered premises, or, for purposes of losses on account of the actions of civil authority, another's premises.
>
> Either way, it will be necessary [for policyholders] to prove that the presence of the coronavirus causes physical loss to the affected premises. Thus, we can expect to see arguments, like the one being made [in the first filed case], that there has been physical loss to a premises because the virus stays on the surface of objects or materials—'fomites'—for some amount of time.

> [A]ny legislative action to compel insurers to pay business interruption claims arising out of the coronavirus [would be] breathtaking. To achieve their result, lawmakers would not only obviate the "virus" exclusion, but, in addition, the fundamental 'physical damage' requirement of business interruption coverage.

Maniloff*, supra. See* Randy J. Maniloff & Margo Meta, *New DJ Takes Different Tack on Business Interruption Coverage for COVID-19*, WHITE & WILLAIMS (Mar. 27, 2020) https://www.whiteandwilliams.com/resources-alerts-New-DJ-Takes-Different-Tack-on-Business-Interruption-Coverage-for-COVID-19.html (describing French Laundry Partners, LP v. Hartford Fire Ins. Co. case seeking declaration of coverage and noting that loss of business use was caused primarily by government ordered suspension rather than tangible property destruction. Maniloff & Meta are skeptical of the claim and argue that "in general, to implicate 'Civil Authority' coverage, there must be physical damage to property other than the covered premises. But businesses have been closed principally to foster social distancing and not on account of the presence of the virus inside a premises." Maniloff & Meta also note that French Laundry is represented by the same attorney as policyholder Oceana Grill, a New Orleans restaurant, that filed the nation's first COVID coverage case).

> Policyholders will sometimes be asserting that insurers, that issued immediate denials for [COVID]-19 claims, did so in bad faith on account of an alleged failure to investigate the claim under applicable law[.]
>
> One business interruption coverage theory in particular is getting attention from policyholders [what the author dubs the "public space" theory that the ubiquitous COVID-19 virus has filled the air and attached to tangible property, making it physically damaged—which in turn means that the injury trigger of the typical policy is satisfied].
>
> Another business interruption coverage issue has not received a lot of attention. The biggest push for coverage has been for businesses that have been shut down by order of a civil authority. However, even if owed, such coverage is likely quite limited. Civil authority-based business interruption coverage, per policy language, is usually available for only up to four weeks.
>
> The restaurant industry is beating the loudest drum in the pursuit of business interruption coverage.

Randy Maniloff, *Covid-19 And Coverage: Four Weeks and Four Takeaways*, COVERAGE OPS. (Apr. 5, 2020), https://www.coverageopinions.info/COVID19ISSUE/COVIDandCoverage.html. These comments are but from one law firm, albeit a particularly large and prestigious insurer-side firm. Many other lawyers representing insurers wrote in the same vein in various publications and on law firm and other websites.

> The New Jersey legislature has premised its actions on the need to take out the "virus" exclusion from business interruption policies. But that's a tonsillectomy compared to what it is really doing—removing the heart of the policy.[63]

Although there were of course stories highlighting the difficulties faced by businesses and other policyholders due to the COVID pandemic,[64] insurers succeeded in simultaneously pooh-poohing the merits of business interruption claims and painting a scenario of risk management ruin if they were required (either by legislatures or courts) to provide coverage they purportedly never agreed to provide.[65]

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[63] Randy Maniloff & Edward Koch, *COVID-19: The Real Operation of New Jersey's Proposed Insurance Legislation*, COVERAGE OPS. (Mar. 19, 2020), https://www.coverageopinions.info/Vol9Issue2/COVIDOperation.html.

[64] *See, e.g.,* Suzanne Barlyn, *U.S. University Insured Chinese Student Tuition Against Virus. Then COVID-19 Hit*, REUTERS: BUS. NEWS (Aug. 17, 2020, 6:25 AM), https://in.reuters.com/article/us-health-coronavirus-university-insuran-idINKCN25D15P (reporting that despite paying annual premium of $424,000 for coverage, University of Illinois found harder market emerging in early 2020, with only limited coverage and premiums increasing to nearly $2 million).

[65] *See, e.g*., Lucca De Paoli & Franz Wild, *Don't Be Tricky With Virus Clams, Watchdog Warns U.K. Insurers*, BLOOMBERG (Mar. 19, 2020, 10:49 AM), https://www.bloomberg.com/news/articles/2020-03-19/u-k-fca-requests-coronavirus-contingency-plans-from-insurers (noting that the U.K. Financial Conduct Authority [FCA] has stated that "insurers must also [like policyholders] be adaptable" in lieu of the problems posed by COVID and must take care to communicate clearly and nondeceptively with policyholder claimants).

> The industry has worked to reduce its exposure to pandemics since the 2003 outbreak of SARS in Asia. Over the years, they've tightened up their policies, inserting communicable-disease exclusions to prevent potential losses. That means consumers and companies will bear the brunt of the cost for disruptions related to the virus—which has infected more than 217,000 people worldwide and left at least 9,000 dead.

Id. Laura Foggan & Michael A. Sabino, *Feeling the Effect*, BEST'S REV. (May 2020), http://news.ambest.com/articlecontent.aspx?pc=1009&AltSrc=108&refnum=296290 (predicting claims across various lines of insurance, particularly property insurance with business interruption coverage, and stating that "[i]t is essential that legislators—and the courts—recognize the limits of insurance in accordance with policy terms and exclusions."); Cheri Trites-Versluis, *Renewal Language Scrutiny: COVID-19 Litigation is Generating a*

Policyholder counsel noted and criticized the perceived insurer public relations campaign.[66] And some in the industry had reservations about the industry's aggressive and rather blanket opposition to coverage.[67] Some observers also

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Resurrection of Arguments Asserted at the Height of Asbestos and Silica Coverage Litigation, NAT'L UNDERWRITER 1, 42–43 (Sep. 2020), https://www.sapiens.com/wp-content/uploads/2020/09/NUP_0920-dl.pdf (citing Above It All Roofing & Construction, Inc. v. Security Nat'l Insurance Co. and RLI Insurance v. Gonzalez, which found asbestos to be a "pollutant" within policy's pollution exclusion, and Garamendi v. Golden Eagle Ins. Co., which found silica dust to be a pollutant, implying similar approach apt for COVID cases). Mr. Trites-Versluis is identified in the article as "the director of policy analysis for RiskGenius," the same company whose CEO is extensively quoted in the media disparaging policyholder claims for business interruption coverage. *Id.*

[66] *See, e.g.*, Andrew G. Simpson, *P/C Insurers Put a Price Tag on Uncovered Coronavirus Business Interruption Losses*, INS. J., (Mar. 30, 2020), https://www.insurancejournal.com/news/nationa/2020/03/30/562738.htm (quoting policyholder attorney John Houghtaling II) ("'To avoid payments for a civil authority shut down the insurance industry is pushing out deceptive propaganda that the virus does not cause a dangerous condition to property.' [] 'This is a lie, it's untrue factually and legally.'").

[67] *See, e.g.*, Kate Smith, *Pandemic Partnerships*, BEST'S REV. (Aug. 2020), http://news.ambest.com/articlecontent.aspx?refnum=299433&altsrc=43.

> Stephen Catlin's mobile buzzed nonstop. It was early April, and he had just written a thought leadership piece on the need for a swift and coherent insurance industry response to pandemic. Frustrated by the falling reputation of the industry and the "clumsy" comments and defensive posture of some insurers, the Convex CEO called on the insurance community to be proactive in finding a long-term solution to pandemic. His message struck a chord.

Id. Mr. Catlin is a 50-year veteran of the insurance industry and founder of an insurer and consulting group as well as a member of the International Insurance Society Insurance Hall of Fame, he elaborated on his views in an Op-Ed piece.

> [First,] insurers and brokers should do a much better job when communicating with the public and with governments, especially regarding the true value that insurance provides. Secondly, it's in the nature of our business to focus on the past, and therefore we often neglect giving adequate thought about the future. Finally, I regret that—when an event occurs that causes extreme human suffering—the insurance industry often views the event primarily in terms of dollars and cents.

wondered whether the more receptive negotiable attitude of some European insurers might be more productive.[68] But in the main, American insurers were on the

> Over the years, we have identified a list of potential 'Big Ones,' events that could cause severe financial stress for insurers and reinsurers. These events range from a Category 5 hurricane that strikes at the heart of Miami to a powerful earthquake devastating Los Angeles or Tokyo. Over the past two decades, an extreme act of terrorism was added to the list.
>
> However, until recently, relatively few insurers would have guessed that a pandemic could be the costliest event the industry could face. I believe that neither governments nor insurers had truly contemplated the economic consequences of a pandemic, in part because the financial impact of such an event is extremely difficult to model.
>
> Unfortunately, the coronavirus has amplified some of the things that I believe the industry often does poorly.
>
> It is not my place to comment on whether individual policies provide coverage for potential claims arising from COVID-19. However, I can say that I was dismayed at the defensive nature of some insurers' statements as the crisis began to expand. There always has been widespread public distrust—if not distain—for the insurance industry, and the comments uttered by some insurers did not help our relationships with governments and our customers.
>
> As I often have said, it's not what you say, but how you say it.
>
> Now that it appears that COVID-19 may be the costliest event in the industry's history, we must begin to think ahead. Will society face pandemics of a similar magnitude in years to come? While I hope we will not, I suspect that we will. If so, what should be the role of the insurance industry? Should we simply adopt policy wording that make it crystal clear that insurance coverage will be of little benefit to policyholders for future losses arising from a pandemic? Or should we think about how insurers can play a meaningful role in economic recovery while still protecting the industry's capital base?

Stephen Catlin, *Setting the Right Tone: Insrers Must Clarify the Role Insurances Can Play in Recovering from Future Pandemics*, BEST'S REV. (Aug. 2020), http://news.ambest.com/articlecontent.aspx?refnum=299423&altsrc=43.

[68] *See, e.g.*, Sergio F. Oehninger & Daniel Hentschel, *Will European Insurers' Positive Response to COVID-19 Claims Influence US Insurers?*, HUNTON INS. RECOVERY BLOG (July 13, 2020), https://www.huntoninsurancerecoveryblog.com/2020/07/articles/business-interruption/will-european-insurers-positive-response-to-covid-19-claims-influence-us-insurers/.

> The positive response in Europe is in stark contrast with the insurance industry's preliminary positions in the United States. The headlines on this side of the hemisphere demonstrate certain insurers' attempts to avoid liability for COVID-19 related losses, despite accepting billions in premiums form policyholders in exchange for broad coverage promises.
>
> In addition, the regulatory structure abroad may make for more collaborative attack on coverage problems. Describing the role of the Financial Conduct Authority [FCA] in England regarding COVID coverage, one article noted:
>
> Business interruption insurance generally only covers losses where a company is forced to close temporarily form property damage, like a fire. The FCA said those types of policies did not offer protection from pandemics, but it was interested in the minority that have so-called nondamage extensions.
>
> Those extensions can protect against the closure of a property either from the outbreak of an infectious disease or by the denial of access by a public authority.
>
> The FCA said it had examined more than 500 policies from 40 insurers and narrowed down its selection to just 17 policy wordings it felt were both the most contentious and representative.

Id. Martin Croucher, *FCA Picks 8 Insurers for Pandemic Coverage Test Case*, LAW360 (June 1, 2020), https://www.law360.com/articles/127811 ("Colin Edelman QC of Devereuz Chambers, Leigh-Ann Mulcahy QC and Richard Coleman QC of Fountain Court Chambers will represent the FCA in the case, instructed by Herbert Smith Freehills LLP."). For additional background on the Financial Conduct Authority, *see* Daniel Schwarcz, *Redesigning Consumer Dispute Resolution: A Case Study of the British and American Approaches to Insurance Claims Conflict,* 83 TUL. L. REV. 735 (2009).

In the test case litigation in the U.K., policyholders largely prevailed, but upon somewhat different issues and policy language than has to date been litigated in the United States. *See* The Fin. Conduct Auth. v. Arch In. (UK) [2020] EWHC 2448 (Comm) (UK).

In addition, continental insurers may have been nudged toward a less confrontational style due to judicial decisions supporting policyholders. *See, e.g*., Oehninger, *supra* (noting that after initially stating it would appeal trial court ruling requiring it to provide business interruption coverage to policyholder with lost revenue due to COVID-19, AXA has relented and agreed to provide coverage; "AXA reportedly has already agreed to pay over 200 COVID-19 related claims."). *See also id*. ("Despite initially denying liability, Swiss insurance company, Helvetia Insurance, announced that most of its policyholders in the hospitality industry have accepted settlements following coverage disputes for COVID-19 related business interruption losses. The settlements reportedly included policyholders form Switzerland, Austria, and Germany.").

defensive. COVID business interruption claims were to be strongly resisted, even where policies lacked a virus exclusion, on the ground that these claims failed to satisfy the "physical loss or damage" trigger for coverage. And, to perhaps state the obvious, insurers were denying COVID claims.[69] Unsurprisingly, this produced litigation by upset policyholders on the brink of financial ruin.[70]

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[69] For an example of rather brusque insurer denial of coverage, *see* Letter from Susan Sabouni, Property Claims Supervisor, Philadelphia Indemnity Insurance Company, to Steve Powell, Chief Officer of Policyholder, The Goddard School (May 7, 2020) (on file with author). The Letter repeats portions of the policy verbatim for nine pages and then simply states that the insurer "considers the issues outlined above to be dispositive of coverage" and that the insurer's "Policy does not provide coverage to the Goddard School for the Claim" and thus "respectfully [?] declines coverage for the Claim" in connection with the school's forced closure due to government order because of the COVID pandemic, even though the policy also contained a "Communicable Disease Endorsement." *See id.* at 10. The insurer stated that the policyholder's loss was "not 'due to an outbreak of a 'communicable disease' . . . that caused[d] an actual illness" at the School. The insurer did, however, agreed to "reimburse the Goddard School for the cost of disinfecting the insured premises due to reported symptoms of COVID-19 within the premises." *Id.* at 10.

[70] *See* Randy Ellis, *Coronavirus in Oklahoma: Tribes Sue Insurance Companies Over Business Interruption Coverage*, THE OKLAHOMAN (Mar. 25, 2020 1:22 AM), https://oklahoman.com/article/5658477/coronavirus-in-oklahoma (describing Chickasaw and Choctaw nations suits involving various insurers); *Coronavirus Coverage Issues Loom: Policy Details Crucial to Determine Success of Commercial Claims*, BUS. INS. 4 (April 2020) (surveying possible COVID-related claims implicating Property Business Interruption insurance, Directors and Officers Liability insurance, Cyber Risk insurance, Medical Malpractice insurance, and Workers Compensation insurance); Joseph P. Monteleone, *COVID-19's Management Liability Concerns,* INS. EXCH. AGENCY (Sept. 14, 2020), https://www.ieagency.com/post/covid-19s-management-liability-insurance-concerns (noting that COVID-related losses will prompt substantial coverage claims involving D&O Insurance, Transactional Risk, and EPL insurance as well as Property Insurance); Patricia Vowinkel, *An Insurance Journey: Significant Coronavirus-Related Losses and Legal Battles Over Coverage May Force Some Insurers to Rethink Their Strategic Game Plans*, BEST'S REV., 1 (May 2020); Bob Reville, *Making Waves: COVID-19 Reveals a Possible Future Upswell of Liabilities for Insurers*, BEST'S REV., 16 (Aug. 2020); Celeste Bott, *Coronavirus Litigation: The Week in Review*, LAW360 (Oct. 8, 2020 7:15 PM), https://www.law360.com/articles/1318126/coronavirus-litigation-the-week-in-review (summarizing recent legal developments, including several insurer wins; also noting that the "Judicial Panel on Multidistrict Litigation has centralized in Illinois over 30 lawsuits accusing Society Insurance Co. of wrongfully denying coverage for business losses during the COVID-19 pandemic, but declined to create MDLs to group similar cases against The Hartford, Travelers, Cincinnati Insurance Co., and Lloyd's of London underwriters."); Lauren Berg, *In-N-Out Sues Zurich To Cover COVID-19 Shutdown*, LAW360 (May 29, 2020

To be sure, policyholder counsel were not silent during the time of insurer pleas of poverty and assertion of absolute defenses to coverage. But they seemed to have reduced prominence in both insurance trade and lay media.[71]

10:56 PM), https://www.law360.com/articles/1278397.; *See also* Hannah Smith, *A Closer Look: Coronavirus Insurance Lawsuit Trends*, PROPERTY CASUALTY 360 (Sept. 4, 2020 12:00 AM), https://www.propertycasualty360.com/2020/09/04/a-closer-look-coronavirus-insurance-lawsuit-trends/?slreturn=20210107191656 ("The main issue that courts must decide in addressing these claims is whether businesses whose operations were shut down during the crisis can demonstrate 'direct physical loss or damage.'") (describing several lawsuits where insurers had prevailed in motions to dismiss, including *French Laundry Partners, LP v. Hartford Fire Ins. Co*., *In-N-Out Burgers v. Zurich American Ins. Co*., and several claims where insurers had prevailed in motions to dismiss including *Plastic Surgeons of Lexington, PLLC v. Liberty Mut. Ins. and Ohio Sec. Ins. Co.* and noting that in *Gavrilides Management Co. v. Michigan Ins. Co*., the "plaintiff alleged that the physical requirement of the policy was met because customers could not physically use the dine-in services. The judge denied this allegation, determining that in order to meet the requirement, the insured must show a physical alteration of the premises."). *See also id.* ("So far, courts have ruled in favor of insurers in cases of business interruption coverage vs. COVID-19. But the vast majority of these cases are still yet to be seen."). For additional examples of COVID coverage complaints, *see* Complaint and Demand for Jury Trial, Prime Time Sports Grill, Inc. v. DTW1991 Underwriting Ltd, No. 8:20-cv-00771-CEH-JSS (M.D. Fla. May 4, 2020); *see also,* Motion to Dismiss Pursuant to Rule 12(b)(6), *supra* (contending that plaintiff restaurant was not "ordered to close" by Florida Gov. Ron DeSantis Order of March 17, 2020 but was permitted to continue operating restaurant at fifty percent occupancy).

Insurers of course approve of the *Gavrilides Management* decision and were undoubtedly pleased that the insurance trade press has given prominent display to the case even though it is a "mere" state trial court case, albeit one of the first decisions in the area. *See* Wilson Elser, *Michigan Judge Rules Direct Physical Loss Required to Trigger Business Interruption Coverage,* LEXOLOGY (Jul. 23, 2020), https://www.lexology.com/library/detail.aspx?g=a9de8e82-e549-44f9-83df-7b66cfd10009 (noting that "Judge [Joyce Draganchuk] stated that direct physical loss [of or damage to the property] must be something 'with material existence . . . that alters the physical integrity of the property.'").

[71] *See, e.g.,* Christine Spinella Davis, *Business Interruption Coverage for COVID-19 Losses: You Can Satisfy the "Physical Loss or Damage" Requirement in Your Commercial Property Policy*, BRADLEY (Apr. 24, 2020), https://www.itpaystobecovered.com/2020/04/business-interruption-coverage-for-covid-19-losses-you-can-satisfy-the-physical-loss-or-damage-requirement-in-your-commercial-property-policy ("Temporary loss of use and loss of functionality alone may satisfy the physical loss or damage requirement in a property policy."); Mark Packman & Jason Rubinstein, *COVID-19 Claims May Survive Insurers' Physical Loss Defense*, LAW360 (Sept. 1, 2020), https://www.law360.com/articles/1306134

> Because COVID-19 does not destroy or tangibly alter the structure of property, the insurers have asserted there is no coverage for claims arising from the pandemic. Initial decisions on this issue broke the insurance industry's way. But the litigation of disputes has barely begun. There is significant evidence to suggest there are many legal paths available to plaintiffs as they struggle with losses related to COVID-19. We explore the findings and implications to date.
>
> Policyholder counsel, for example, argued:
>
> In most property insurance policies, business interruption coverage is triggered when the property at issue suffers "direct physical loss or damage." Structural damage to the property, however, is not a requirement for coverage; proof that contamination or other relatively intangible conditions like bacteria, gases, and fumes that "rendered the insured property temporarily or permanently unusable or uninhabitable may support a finding that the loss was a physical loss to the insure property."
>
> Additionally, many insurance policies include civil authority coverage, which covers losses that occur when government authorities restrict access to the area where a business is located or that the business depends on for its operations.
>
> Many property insurance policies also provide contingent business interruption coverage, triggered by damage to or disruption of a business's suppliers, customers, or other key partners. While the policyholder itself need not be physically damaged, it does need to have coverage for the type of damage that affected its suppliers, busines partners, or customers.

Packman & Rubinstein, *supra*. Pamela D. Hans & Marshall Gilinsky, *Insurance Coverage for Losses Stemming from the Coronavirus*, INS. J. (Feb. 26, 2020), https://www.insurancejournal.com/news/national/2020/02/26/559383.htm (citing Mellin v. Northern Sec. Ins. Co., 115 A.3d 799, 805 (N.H. 2015) and also citing Gregory Packaging, Inc. v. Travelers Prop. Cas. Co. of Am., 2014 U.S. Dist. LEXIS 165232, *15-17 (D.N.J. Nov. 25, 2014) "[C]ourts considering non-structural property damage claims have found that buildings rendered uninhabitable by dangerous gases or bacteria suffered direct physical loss or damage.").

> Business owners are submitting claims for business interruption insurance losses, but many insurance companies' knee-jerk reaction is to deny. This has led to a proliferation of lawsuits. While the viability of these suits depends on each business's unique circumstances and policy language, the prospects look very good for many Pennsylvania business owners.

There has also been, in our view, something of a race-to-the-courthouse problem in that a number of the initial policyholder claims appear to be brought by counsel without substantial experience in insurance coverage litigation, something that more seasoned coverage lawyers noted with some dismay (along with voicing concerns that the efforts of some plaintiff counsel to consolidate proceedings was hurtful to the COVID coverage cause).[72]

> Many Pennsylvania businesses bought all-risk commercial property insurance policies that contain business interruption coverage. The coverage provisions are broad . . . .
>
> Many insurance companies will dispute that COVID-19 losses satisfy the direct physical loss or damage requirement. . . . Courts have rejected this view on numerous occasions in numerous contexts.

Patrick Campbell, Charles Casper & Brett Waldron, *Pa. Insureds' Path to Pandemic Biz Interruption Coverage*, LAW360 (May 19, 2020 5:50 PM), https://www.law360.com/appellate/articles/1274214/pa-insureds-path-to-pandemic-buz-interruption-coverage (also arguing that there should be coverage even if policy has virus exclusion due to rule that exclusions are construed narrowly and government shutdown orders rather than the virus itself are the cause of business interruption).

[72] *See, e.g.*, Chip Merlin, *What is Multidistrict Litigation (MDL) and Will It Impact Virus Business Income Claims?*, PROP. INS. COVERAGE L. BLOG (May 10, 2020), https://www.propertyinsurancecoveragelaw.com/2020/05/articles/commercial-insruance-claims/what-is-multidistrict-litigation-mdl-and-will-it-impact (writing by noted policyholder coverage attorney expresses some doubt about efficacy of consolidation). A large and prominent policyholder firm was less tentative and more critical of consolidation.

> Savvy policyholders and experienced counsel may also find consolidated and class action proceedings ill-suited to the resolution of insurance coverage disputes. That is because claim-specific differences are likely to predominate over common issues in three fundamental respects: (1) the specific facts of any particular insurance claim, and how that claim is best presented and substantiated, often vary greatly from claim to claim, place to place, and industry to industry; (2) the specific language of any given insurance policy is critical, and there can be enormous variation in policy language on the material issues implicated by COVID-19; and (3) insurance coverage is a matter of state law, which varies widely across jurisdictions on issues of importance for many policyholders.
>
> For these reasons, sophisticated insureds should carefully review their own insurance policies, claims, and circumstances before signing on to any

As discussed in the next section, we take issue with the insurance industry's rush to judgment opposing COVID-related coverage across the board. We also are concerned that insurers are exaggerating both their potential financial responsibility if COVID coverage claims succeed and the industry's purported inability to absorb such claims.

First, the estimated costs. Insurers have suggested that if covered, the costs of business interruption claims would range as high as $800 billion per month.[73] But

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> of the current efforts to aggregate coronavirus-related insurance cases into MDL or class action proceedings.

David Goodwin, Allan B. Moore & Rani Gupta, *Policyholders Beware: The Risks of Multi-District and Class Action Treatment of COVID-19 Insurance Claims*, COVINGTON, 1–2 (May 4, 2020), https://www.cov.com/-/media/files/corporate/publications/2020/05/policyholders-beware-the-risks-of-multidistrict-and-class-action-treatment-of-covid-19-insurance-claims.pdf.

> Strong claims should be timely noticed and pursued aggressively by experienced insurance coverage counsel, particularly if insurers do not meet their obligations to pay promptly. Decisions to pursue coverage litigation must take into account the most favorable jurisdictions, procedures, and timing to maximize recovery for policyholders affected by COVID-19. In knowledgeable counsel is able to litigate the strongest claims first, those cases will set appropriate precedents that will establish insureds' rights to recover COVID-19 losses and benefit other policyholders.

Id. at 5.

In addition, despite being defendants, insurers have considerable power to shape early case outcomes by making motions to dismiss when presented with favorable facts, policy language, or courts while simply answering the complaint when faced with unfavorable facts, policy language or tribunals, thereby delaying any legal rulings from these less favorable forums until the industry could accumulated the momentum of early Rule 12 victories.

[73] As reported in one prominent industry periodical:

> It's hard to quantify the full financial impact COVID-19 will have on the industry. But one thing is certain, this pandemic is on track to become the largest event in insurance history.
>
> "It is truly a catastrophic event the proportion of which we have not seen before," Stefan Holzberger, chief rating officer for AM Best, said. "The breadth and depth of the event, how it is affecting multiple

> geographics and multiple segments of the insurance market—this is really something that dwarfs the other major events in recent history."
>
> . . .
>
> And yet, the insurance industry has been prepared to handle this event.
>
> . . .
>
> There is a caveat to this, however. The industry's ability to absorb the impact of COVID-19 hinges on business interruption. As of early May, seven states had introduced legislation requiring insurers to provide retroactive business interruption coverage, in some cases regardless of whether policies included a virus exclusion, as most do.
>
> If forced to pay retroactive BI, the insurance industry could be facing losses of $150 billion to $200 billion per month, according to the Best's Commentary, Legislation to Nullify BI Exclusions Poses Existential Threat to P/C Insurers. The Insurance Information Institute's estimates are even higher. The III [Insurance Information Institute] forecasts costs of up to $380 billion per month, which it said would "break" the insurance industry within months. That scenario, however, is unlikely [because of lack of coverage.]
>
> If you take business interruption out of the equation, the industry as a whole is on solid financial footing.

Kate Smith, *The COVID Catastrophe: The Global Pandemic is on Track to be the Costliest Event in Insurance History. It's also a Defining Moment for the Industry Special Risk Section Sponsored by Lexington Insurance*, BEST'S REV. (Jun. 2020), http://news.ambest.com/articlecontent.aspx?refnum=297254&altsrc=123. *See also* Robert Hartwig, Greg Niehaus & Joseph Qui, *Insurance for Economic Losses Caused by Pandemics*, 45 Geneva Risk and Ins. Rev. 134, 135 (2020) (estimating losses at one trillion dollars per month for business interruption alone).

We like hyperbole as well as the next authors, but we think it is a bit much to suggest that possible business interruption coverage would "dwarf" the financial consequences of major insurance events such as the asbestos mass tort or pollution claims. We are not dismissive of the potential magnitude of COVID claims but remain concerned that the insurance industry has been a bit cavalier in suggesting such large losses and generally wailing gloom and doom in the event of coverage. It may be a good public relations strategy that will gain sympathy from the courts but strikes us as overblown. And, as discussed later in the article, there is something concerning about attempts to convince courts and policymakers that insurers are too vulnerable to be saddled with COVID losses when the alternative is saddling much more vulnerable small businesses with these losses. If that is the fate decreed by contractual agreement, perhaps there is no escape (save for invocation of reasonable expectations, unconscionability, and public policy canons for construing those

at this juncture, we have not seen any detailing of this estimate or the methodology behind it. We remain skeptical, particularly so in light of the commonly found sublimits (either temporable or monetary) on coverage for business interruption occasioned by government order that insurers contend is contained in most policies and which appears popular in policy forms. One article provides a flavor of the industry's tone.

> The Insurance Information Institute and American Property Casualty Insurance Association place the estimates much higher: The APCIA forecast losses of up to $668 billion per month, while the III estimated retroactive BI could cost the industry up to $380 billion per month. "That's an industry-breaking event," James Lynch, chief actuary for the II, said. "That would break the industry in two directions. One, the financial load it would place on companies to have to pay claims they had priced the business for, and had specifically excluded, would create financial ruin. Moreover, that intervention into clear policy language would call into question the entire insurance business model."
> . . . .
> "They're trying to make the case that they're shutting down because of physical loss and damage from the virus," said RiskGenius CEO Chris Cheatham, whose company uses software to help insurers evaluate policy language. "That's not an accident. That's not how people talk."
> Bob Hartwig, director of the Risk and Uncertainty Management Center at the University of South Carolina's Darla Moore School of Business, said politicians were fed such language from plaintiffs' attorney groups who are "looking at this as a potentially huge payday."
> . . . .
> "The State of New York cannot alter the laws of physics to satisfy its trial lawyer masters, "Hartwig said. "That's essentially what happened. They developed this language in an attempt to overruled the virus exclusion."
> "All legal scholars agree this will fail a Constitutional test. There's no question about it."

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contracts) from this bothersome result. But, as discussed later, the insurance industry's extreme anti-coverage position is incorrect.

> The battle over business interruption will, without doubt, make its way into the courts. And most agree the courts will side with insurance companies.
> "The exclusion for viruses is not an ambiguous one," Lynch said. "It's an exclusion of loss due to virus or bacteria. When it was filed, the filing specifically mentioned the potential for a pandemic similar to SARS CoV-1. And the current pandemic is SARS CoV-2. So I don't think there's a lot of ambiguity here about what the exclusion was meant to exclude.
> Stefan Holzbeger, chief rating officer of AM Best, agreed.
> "Those well-defined, long-instituted, regulator-approved exclusions for pandemics or viruses should hold," Holzberger said. "The business interruption policies that have that exclusion, which is the vast majority in the U.S., should not have to honor claims associated with a loss of revenue related to COVID-19.
> [Holzberger further predicted that if legislation negating virus exclusions was enacted and upheld in court] we would see widespread insolvency because the magnitude of lost revenue in relation to the capital surplus is so great. The insurance industry could not bear those losses. Which is why they weren't covered in the first place."[74]

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[74] Smith, *supra* note 73. Best's Review loved the inflammatory quote about trial lawyers so much, it was emphasized in a pull-quote from the sidebar in large print, complete with a 20-year-old picture of Professor Hartwig, a former insurer lobbyist before entering academia.

> The property/casualty industry estimates that business interruption losses from the coronavirus just for small businesses in the U.S. could be between $220-$383 billion per month—or a quarter to half of total industry surplus available to pay all P/C claims.
>
> David A. Sampson, president and CEO of the American Property Casualty Insurance Association, said the $200-383 billion per month loss estimate assumes there could be as many as 30 million claims from small business that suffered coronavirus-related losses. According to APCIA, that is 10 times the most claims ever handled by the industry in one year. The industry processed more than three million from the 2005 hurricane season that included Hurricanes Katrina, Rita, Wilma and several other storms, the trade group said.

Second, as to insurer ability to pay: if the insurance industry were a sovereign nation, it would have the third largest economy in the world.[75] Insurers receive hundreds of billions of dollars in premium income alone each year,[76] which in turn has usually been invested for some time before the funds are required to be paid in claims. Insurance is generally a more consistently profitable business than most, advantaged by its ability to amass large sums that can be invested, perhaps for years (or decades in the case of liability insurance) before payment. This "float," as Warren Buffett calls it, enables even insurers with weak underwriting to survive and even thrive. Insurers with sound underwriting and investment do particularly well.[77]

So, what of the effect of the insurance industry's initial media messaging? We are not in a position to pinpoint entirely the impact of the industry's anti-coverage messaging on legal developments to date. We cannot count the claims that

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> Sampson said the combined capital of the top business insurance underwriters represents only a fraction of the amount that might be expected in coronavirus losses form just small businesses.
>
> "Insurance stability is especially important in a time of increased natural catastrophes. Spring flood season is underway, hurricane season is around the corner, and wildfires pose a threat year-round," he said.

Simpson, *supra* note 66.

[75] *See* Richard V. Ericson, Aaron Doyle & Dean Barry, Insurance as Governance, 1, 4 (2003) (noting the degree to which insurance shapes behavior by setting contours of coverage and conduct in order to obtain insurance).

[76] Ranked by 2019 net premiums written, the smallest of the Top 200 (HCI Ins. Group) collects $228,488,000 in annual premiums; 82 insurers have $1 billion or more in annual premium income. *See Top 200 U.S. Property/Casualty Writers*, BEST'S REV. (July 2020), http://www.ambest.com/review/displaychart.aspx?Record_Code=274586&src=43&_ga=2.171650912.1123988532.1612739172-73892297.1612560642. Some household name insurers have astounding volumes of premium income, e.g.: State Farm ($65.1 billion); Berkshire Hathaway ($53.75 billion); Progressive ($37.6 billion); Allstate ($34 billion); Liberty Mutual ($32.3 billion); Travelers ($27.2 billion); USAA ($23 billion); Chubb INA ($18.2 billion); Nationwide ($18 billion); AIG ($14.8 billion); Farmers ($14.5 billion); Harford ($11.9 billion); American Family ($11.8 billion); Auto-Owners ($8.6 billion); Fairfax ($7.6 billion); Erie ($7.5 billion). *Id.* Cincinnati Insurance, a defendant in several prominent COVID coverage actions, received almost $5.4 billion in premiums in 2019. *Id.*

[77] *See* Jeffrey W. Stempel, Erik S. Knutsen & Peter N. Swisher, Principles of Insurance Law § 1.06 (5th ed. 2020) ("A Note on Insurer Operations"); Stempel & Knutsen, *supra* note 33, at § 1.01 (describing insurer operations, using in part description provided by Buffett (who is typically ranked as one of the world's ten richest people) in his annual letter to Berkshire Hathaway shareholders; Berkshire's success, according to Buffett, is due in large part to investment funds generated by its insurance and reinsurance operations).

were not filed because a business or a business' lawyer read in the newspaper that "COVID claims are not covered." Nor can we precisely discern the effect on judges as the majority of COVID-related claims were dismissed in favor of insurers at the pleadings stage (though we find that result quizzical). We have yet to learn the effect of the messaging on lay juries, as these cases have not yet made it far enough in litigation (because most are bounced out on the pleadings alone).

But we are able to say that perhaps it is more influential to get out in front of a story and control the narrative than to be correct. If nearly every insurance trade publication, lawyers' publication and popular news press sees the same message, surely there must be some even subliminal effect on how one approaches the insurance coverage question for COVID cases. Moreover, and most concerning to us, there appear to be absolutely no ramifications if the message proffered in the media is actually incorrect! Are we entering a new phase of insurer public relations tactics that are, at least in part, designed with a motive to affect coverage results in legal cases?

In Part III below, we explain how the main coverage question of "direct physical loss or damage" is counter to the main thrust of the insurance industry's message in the media to date. We conclude with our thoughts as to where the issues will resolve in the end.

III. THE KEY COVERAGE ISSUE: DISCERNING THE (REASONABLE) MEANING(S) OF "DIRECT PHSYICAL LOSS OR DAMAGE"[78]

A. THE INSURER ARGUMENT FOR REQUIRING TANGIBLE DESTRUCTION TO TRIGGER COVERAGE

Insurer efforts to dismiss business interruption claims as strained have resonated with most in the industry, including respected authorities who should in our view be less dismissive of claims of loss or damage. A prominent editor of the Fidelity, Casualty & Surety (FC&S) organization has, for example, approached the question as follows.

> When policies don't define a term, courts generally refer to a standard dictionary. Merriam-Webster defines damage as "loss or harm resulting from injury to person, property or reputation." This

[78] In this article, we focus almost exclusively on coverage issues concerning first-party property insurance and its business interruption component as these policies have been those at issue in the first wave of coverage litigation. We expect significant coverage litigation concerning liability insurance to emerge in the future.

> is not definitive, so we look at the definitions of loss and harm. Loss is defined as "destruction, ruin," and harm is defined as "physical or mental damage."
> The virus does not harm physical property. The virus may be cleaned off like other germs or bacteria. The property does not need to be replaced or repaired, just sanitized as advised by public health authorities.[79]

Continuing in this vein, and seeking a trifecta of sorts of no coverage pursuant to government order provisions plus the prevalent pollution exclusion, she wrote:

> ISO has a mandatory virus and bacteria exclusion, but what about carriers not using ISO forms? What about carriers that have adopted parts of ISO forms, such as the business interruption language, but have not adopted the rest and did not adopt the mandatory endorsement?
> . . . .
> The issue at hand with the virus is business interruption and action of civil authority. Is there coverage when local authorities require bars, restaurants, gyms and other establishments to close because of the chances of spreading the virus? For this, we need to look at an endorsement; for the sake of discussion, we are looking at the Business Income (and Extra Expense) Coverage Form CP 00 30.
> Coverage is provided for the actual loss of business income due to the necessary suspension of business operations during the period of restoration. The period of restoration must be due to direct physical loss of or damage to coverage property. Also covered is loss triggered by a civil authority prohibiting access to the insured property because of damage to other property, but two conditions must apply. That other property must be within one mile of the insured property, and the action of the civil authority is taken in response to dangerous physical conditions resulting form the loss, continuation of the covered cause of loss that caused the damage, or to allow the authority unimpeded access to the property.

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[79] Christine G. Barlow, *Does COVID-19 Cause Physical Loss*?, NAT'L UNDERWRITER 1, 10 (May 2020), https://www.property-casualtydigital.com/propertycasualty/202005?pg=12#pg12.

> So herein lies the rub. Coverage is provided only when a property has been physically damaged. COVI-19 does not cause physical damage to property. Even if it is considered physical damage, then you have the pollution exclusion to deal with, and the virus is a pollutant. Pollutants are excluded when they are dispersed, discharged, seep, migrate or otherwise escape. So it comes down to whether an individual can be considered to be dispersing, discharging, or otherwise releasing the virus, action that would trigger the pollution exclusion.
>
> Recently a physician from San Francisco attended a conference with hundreds of other physicians in New York. Upon returning home, he felt ill and was tested for the virus, which came back with positive results. Those people attending the conference were possibly exposed to the virus. Does this count as dispersing the virus, even though unintentionally? It seems so.
>
> This is different from closing businesses, because the threat of the threat of exposure or spread of the virus, a threat is not physical damage, and therefore there is no coverage.[80]

B. THE FLAWS OF THE INSURER-ADVANCED CONVENTIONAL WISDOM

1. Dictionary Fetishism: Improperly Collapsing "Loss" and "Damage"

Notwithstanding our respect for this author and the FC&S organization,[81] we are constrained to disagree. Although the "Order of Civil Authority" coverage provided in many policies is limited to four weeks of lost income[82] and the presence of the basic ISO virus exclusion may typically preclude coverage,[83] the FC&S

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[80] *Id.* at 10–11.

[81] And Ms. Barlow's dismissiveness toward COVID claims may be mild compared to what is coming from another prominent coverage expert. *See* Bill Wilson, WHY INSURANCE DOESN'T COVER THE COVID-19 PANDEMIC (2020) (e-book format released Oct. 29, 2020). Mr. Wilson is the author of the widely celebrated coverage analysis WHEN WORDS COLLIDE: RESOLVING INSURANCE COVERAGE AND CLAIMS DISPUTES (2018).

[82] *See supra* notes 30–35 and accompanying text discussing order of civil authority coverage.

[83] *See infra* notes 180–202 and accompanying text discussing virus exclusion.

analysis is severely deficient regarding the question of physical loss or damage and utterly absurd regarding application of the pollution exclusion.[84]

Property insurance policies can vary significantly. While many do not include business interruption or "business income" coverage (a plus for insurers in light of the lost business revenue caused by COVID), many also lack a virus exclusion (a plus for policyholders). But almost all make a finding of "direct physical loss or damage" an initial requirement for coverage.[85] As discussed below, in decades of coverage litigation preceding COVID claims, courts have divided over the meaning of these terms. But prior to examining case law, courts might profitably examine the facial clarity of these terms, neither of which is usually defined in the insurance policy despite its separate "Definitions" section that normally contains specifically defined terms.

FC&S's analysis tends not to look to case law but to focus on policy text. This is historically a typical insurer response, as a contextless reading of insurance policy terms most often favors the insurer. This is so because the policyholder litigating the claim probably suffered a loss within the grey areas of coverage (otherwise, why litigate?). The potential pitfalls of the standard insurer textual approach are reflected in its analysis above: seek out the plain meaning of policy terms so as to have the interpretive analysis stop at the plain meaning stage of determining policy coverage—and thus avoid any interpretive ambiguity in the meaning of those terms (otherwise, the policyholder-favoring tools of *contra proferentem* or reasonable expectations are visited upon the entire analysis).

First, the insurer COVID coverage language assessment tends to collapse the terms "loss" and "damage" into one—a rhetorical move that is both unwarranted

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[84] Due to space limitations, we will not present a full examination of the pollution exclusion in the context of COVID-19 in this article. But for reasons we have set forth at length elsewhere, it is absurdist textual literalism to argue that infection of premises by a virus (or bacteria, fungus or the like) is "pollution" as the term is ordinarily understood. It is similarly laughable to suggest that a conference attendee is "dispersing" "pollutants" when sneezing. What, pray-tell, is next, insurers asserting that an attendee's nausea at the office cocktail party is a pollution event? Such broad construction of an exclusion—part of the insurance policy upon which the insurer bears the burden of persuasion must be narrowly and strictly construed against the insurer who—would operate to undermine the basic purpose of property insurance or liability insurance. *See* STEMPEL & KNUTSEN, *supra* note 33, at § 14.11; Jeffrey W. Stempel, *Reason and Pollution: Construing the "Absolute" Pollution Exclusion in Context and in Light of its Purpose and Party Expectations*, 34 TORT & INS. L.J. 1 (1998); Jeffrey W. Stempel, *Unreason in Action: A Case Study in the Wrong Approach to Construing the Liability Insurance Pollution Exclusion*, 50 FLA. L. REV. 463 (1998).

[85] *See* French*, supra* note 4, at n. 21–22 and accompanying text.

(we think the two words are distinct) and misleading in its use of "the dictionary." As the fetishism of textualism in American judicial interpretation of insurance policy terms rages on, we think that taking the insurer-led textual charge head-on leads to the opposite result that the insurers advocate. Indeed, this is doubly bizarre because historically, insurers have favored a textualist and literalist approach to policy language—probably because historically they have benefitted from such application. But here, in determining coverage for "direct physical loss or damage," the use of one of the key textualist interpretive tools—the use of dictionary definitions to discern the ordinary lay meaning of policy terms—actually spins counter to insurer interests, when deployed properly.

Regarding the distinction between the words "loss" and "damage", it should be noted that courts typically subscribe to the "surplusage" canon of construction, which posits that each word in a document (statute, contract, regulation) should be given its own meaning and not treated as a mere repetition by synonym.[86] Although it is in some ways a problematic canon,[87] it is nonetheless one of the "rules" of interpretation. And insurers, when it suits their purpose, embrace the surplusage canon.

For example, when litigating the application of the pollution exclusion, insurers routinely argue that each of the seventeen words in the exclusion (e.g., irritant, contaminant, chemical, waste) deserves independent meaning rather than reinforcing a core concept of pollution,[88] with courts frequently agreeing and giving

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[86] The "surplusage" canon of construction posits that "[i]f possible every word and every provision should be given effect (*verba cum effectu sunt accipienda*). None should needlessly be given an interpretation that causes it to duplicate another provision or to have no consequence. 'These words cannot be meaningless, else they would not have been used." ANTONIN SCALIA & BRYAN GARNER, READING LAW: THE INTERPRETATION OF LEGAL TEXTS 174 (2012) (citing U.S. v. Butler, 297 U.S. 1, 65 (1936) (Roberts, J.)).

[87] *See* Laurence Solan & Jeffrey W. Stempel, *Rethinking Redundancy: The False Premises and Practices of the Surplusage Canon* (Jan. 2020) (manuscript on file with author) (describing drawbacks of surplusage and tendence for drafters to use redundancy as a means of attempting to achieve clarity). *Accord*, Ethan J. Leib & James Brudney, *The Belt-and-Suspenders Canon*, 105 IOWA L. REV. 735 (2020) (suggesting that in practice many courts treat drafting repetition as clarifying a particular intent rather than using each word to convey its own concept).

[88] The typical definition of "pollutants" in a standard form general liability, which has been widely used for thirty years or more, includes "any solid, liquid, gaseous or thermal irritant or contaminant, including smoke, vapor, soot, fumes, acids, alkalis, chemicals, and waste" with wasted "include[ing] materials to be recycled, reconditioned or reclaimed." *See, e.g*., Commercial General Liability Policy Form CG 00 01 01 96, *in* DONALD S. MALECKI & ARTHUR L. FLITNER, COMMERCIAL GENERAL LIABILITY 271 (6th ed. 1998).

the words literal application even though they are contained in an exclusion that is, according to contract construction rules, supposed to be strictly and narrowly construed against the insurer with the insurer bearing the burden of persuasion to demonstrate the applicability of the exclusion.[89] If the insurers are to be consistent in their interpretative arguments, the word "loss" should be viewed as meaning something different than "damage."

Perhaps more important, if one is "making a fortress" out of the dictionary (something cautioned against by the great Second Circuit Judge Learned Hand),[90] that fortress provides quite a lot of protection to policyholders—and this should be conceded by insurer advocates, who have to date disappointingly taken a self-serving view of the terms "loss" and "damage," with too much acquiescence from courts. Even if one is not ready to concede that dictionary definitions favor policyholders more than insurers, it seems to us undeniable that there are many dictionary entries supporting the policyholder perspective. This in turn means that policyholder textual arguments are reasonable. And this further means that the term

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[89] *See, e.g.*, *Quadrant Corp. v. Am. States Ins. Co.*, 110 P.3d 733 (Wash. 2005) (taking broad view of pollution exclusion as precluding coverage for policyholder negligence in application of sealant exposing apartment resident to noxious fumes). *See* William P. Shelley & Richard C. Mason, *Application of the Absolute Pollution Exclusion to Toxic Tort Claims: Will Courts Choose Policy Construction or Deconstruction?*, 33 TORT & INS. L.J. 749 (1998) (detailing a prominent insurer counsel advocate's broad application of the exclusion to cover claims of policyholder negligent injury with any involvement of chemicals).

[90] *See* Cabnell v. Markham, 148 F.2d 737, 739 (2d Cir. 1945) ("But it is one of the surest indexes of a mature and developed jurisprudence not to make a fortress out of the dictionary; but to remember that statutes always have some purpose or object to accomplish, whose sympathetic and imaginative discovery is the surest guide to their meaning.") By this, Judge Hand sensibly meant that words should be construed in accord with party intent and overall purpose rather than through textual assessment alone. We agree and also note that there may well be extrinsic evidence supporting the insurance industry's view that when drafting property policies, it intended to provide coverage only for the sort of tangible structural injury that comes from external forces such as fire, windstorm, a sudden flooding, vandalism or other actions that wreak palpable destruction on property. But to date, insurers have not done so, preferring to fight on the metaphorical "hill" of ahistorical, acontextual textualism. In COVID decisions to date, they have been holding that hill. Should they start to die on the hill (*e.g.*, if courts begin in greater degree to recognize that "physical loss or damage" does not inexorably mean tangible destruction), one would expect them to proffer supporting extrinsic evidence that this is what was meant or intended or required by sound risk management practice. If they cannot provide such evidence, policyholders deserve to win on the "physical loss or damage" question, even in jurisdictions with a weak application of the *contra proferentem* principle.

"physical loss or damage" is sufficiently ambiguous that policyholders should enjoy the benefit of the *contra proferentem* principle and avoid dismissal of their claims on this basis unless insurers can proffer sufficient extrinsic evidence to support their preferred meaning of the term—something insurers have not done to date.

2. Dictionary Definitions Support Policyholders as Least as Much as Insurers

In arguing that coverage requires tangible destruction that can not be easily rectified, FC&S refers to the Merriam-Webster dictionary, editions of which are on our respective desks, but selects and presents the definitions in a pronouncedly anti-policyholder fashion. The more complete excerpt of key terms presented below provides an alternative meaning of "loss" that distinguishes it from "damage."

> **damage** [means] **1** : loss or harm resulting from injury to person, property, or reputation . . .
> **loss** [means] **1** : DESTRUCTION, RUIN **2 a** : the act of losing possession **b** : the harm or privation resulting form loss or separation **c** : an instance of losing . . . **4 a** : failure to gain, win, obtain, or utilize . . . **5** : decrease in amount, magnitude, or degree. . .
> **lose** [means] **1 a** : to bring to destruction . . . **3** : to suffer deprivation of: part with esp. in an unforeseen or accidental manner . . . *vi* **1**: to undergo deprivation of something of value . . .
> **physical** [means] **1 a** : having material existence : perceptible esp. through the senses and subject to the laws of nature . . . b : of or relating to material things . . .[91]

Applying this mix of Merriam-Webster definitions suggests that one might reasonably find a "physical loss" when a policyholder is deprived of something material—such as use of one's business, especially if the loss takes place in an unanticipated manner through something like a pandemic that spurs government-ordered use of the business property.

Similarly, it is perfectly reasonable to state that one's physical property has been lost or harmed or injured by a virus on surfaces or in the air on the property. Insurers argue that because the virus can be "wiped off," there has been no loss or

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[91] MERRIAM-WEBSTER'S COLLEGIATE DICTIONARY 291, 689, 689, 877 (10th ed. 1996).

damage. The "virus damages lungs, not property"[92] has become an insurance industry aphorism akin to "the CGL [commercial general liability] policy is not a performance bond," a cliché invoked by CGL insurers seeking to avoid coverage for damage inflicted by defective construction.[93] Actually, the damages-lungs-not-property mantra is more misleading.

The not-a-performance-bond trope is true as a general rule. But, as courts have come to recognize almost uniformly, this general rule is not applicable where a CGL policyholder's negligence inflicts damage (defined as "physical injury to tangible property") upon other property and the CGL coverage is not based on merely correcting substandard work but compensating victims for damage done to other property by the substandard work.[94]

The damages-lungs-not-property trope is not true—period—or is only true if one excises the word "loss" from the trigger term "physical loss or damage." Even under the view that a cleaning will make infected property "as good as new" (which may not be the case), the property has nonetheless been lost to its owner for at least some period of time, perhaps a significant period of time depending upon the cleaning and public health requirements to which the property is subject (let alone serious public relations issues with regard to perceived safety of the premises).

Further, a facility in which COVID has been found is, at least temporarily, "damaged" goods. The susceptibility of COVID to cleaning is relevant to questions of the degree of injury and the period of restoration required for a COVID-infected business. COVID infection is not the same as a fire or explosion, and in many cases is more easily rectified than water damage from a burst pipe. But there nonetheless is at least some physical damage and considerable physical loss of property if the cleaning and disinfecting is time-consuming or if government authorities restrict operation of the facility.

In addition, remediation of COVID damage to property is likely to be fleeting in many situations. COVID-inflicted injury may be susceptible to

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[92] Transcript of Teleconference Order to Show Cause at 5:3–4, Soc. Life Magazine, Inc. v. Sentinel Ins. Co., No. 20 Civ. 3311 (S.D.N.Y. May 14, 2020).

[93] *See* Jeffrey W. Stempel, *Rediscovering the Sawyer Solution: Bundling Risk for Protection and Profit*, 11 RUTGERS J. OF L. & PUB. POL'Y 170, 210, n. 89 (2013) (noting the prevalence of this argument by liability insurers in defective construction cases). *See, e.g.*, Nationwide Mut. Ins. Co. v. Wenger, 278 S.E.2d 874 (Va. 1981) (exemplifying a general liability insurer arguing to receptive court that coverage for construction defects, absent injury to non-policyholder property, would improperly convert the liability policy into a performance bond).

[94] *See* STEMPEL & KNUTSEN, *supra* note 33, at § 14.13; STEMPEL, SWISHER, & KNUTSEN, *supra* note 77, 657–61. *See, e.g.*, Am. Family Mut. Ins. Co. v. Am. Girl, 673 N.W.2d 65 (Wis. 2004).

disinfection but may be repeated within hours as customers or employees return to a restaurant, bar, retail outlet, or factory. COVID damage may even be re-imposed almost as quickly as it first struck if members of the cleaning crew are COVID-positive, which may be the case even if the workers show no detectible symptoms of infection.

A brief survey of other dictionaries reveals a nesting of definitions of the key words of COVID coverage disputes that is more consistent with our broader view of the meaning of the terms "physical loss or damage" than the seemingly cherry-picked FC&S emphasis on irreversible tangibility as a prerequisite to finding such loss or damage. Consider the following entries, all from mainstream sources.

> **damage** [means] [i]mpairment of the usefulness or value of person or property . . .
> **loss** [means] **b.** The condition of being deprived or bereaved of something or someone . . .
> **lose** [means] **2.a.** To come to be deprived of the ownership, care, control of (something one has had) . . . [95]

or

> **damage** [means] **1.** Harm or injury to property or a person, resulting in loss of value or the impairment of usefulness.
> **loss** [means] **1.** The act or an instance of losing . . . **b.** The condition of being deprived or bereaved of something or someone.
> **lose** [means] **2a.** To be deprived of (something one has had).
> **physical** [means] **2.** Of or relating to materials things . . . [96]

or

> **damage** . . . See breakage, harm [as a noun]. See injure [as a verb].
> **loss** [means] The act or an instance of losing something : losing, misplacement. . . . See also deprivation.
> **deprivation** [means] The condition of being deprived for what one once had or ought to have : deprival, dispossession, divestiture, loss, privation.
> **lose** [means] To be unable to find : mislay, misplace.

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[95] THE AMERICAN HERITGAE COLLEGE DICTIONARY 350, 801, 1031 (3rd ed. 1993).
[96] THE AMERICAN HERITAGE COLLEGE DICTIONARY 357, 817, 818, 1050 (4th ed. 2004).

> **physical** [means] **1.** Composed of or relating to things that occupy space and can be perceived by the senses: concrete, corporeal, material, objective, phenomenal, sensible, substantial, tangible.[97]

or

> **damage** [means] **1.** Impairment of the worth or usefulness of person or property: harm.
> **loss** [means] **1.** The damage or suffering that is caused by losing. **2.** One that is lost.
> **lose** [means] **3**. To be deprived of . . .
> **physical** [means] **1.** Of or relating to the body rather than the emotions or mind. **2.** Material rather than imaginary. **3. a.** Of, pertaining to, or produced by nonliving matter and energy.[98]

Perhaps most surprising is that many standard-fare dictionaries actually use the term "damage" in defining the term "loss" to indicate that "loss" can mean "loss of use" or deprivation of property.

3. Apt Use of Dictionaries in COVID Coverage Controversies Often Supports Coverage

This is perhaps the time to note that in most every dictionary, the order of definitions does not proceed from most popular to least used, as many people (including lawyers) often mistakenly think. Rather, the presentation proceeds from earliest usage to most recent usage.[99] The first definition presented is simply the oldest and not the primary or best or most widely used or accepted definition. In many cases, the oldest definition may be considerably less popular or representative or "correct" than definitions listed later in the dictionary entry. As a result, we believe it is inappropriate for courts or commentators to argue that a term is clear and unambiguous based on presentation order in the dictionary. For example, a lawyer's argument that definition number one is what was meant because it is the first definition seems to us quite misplaced.

Insurers might seize upon this to suggest that a definition of "loss" that includes "destruction" or "ruin" is ***the*** clearly correct definition because it emerged

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[97] ROGET'S II: THE NEW THESAURUS 105, 265, 117, 265, 314 (3d ed 1995).

[98] WEBSTER'S II NEW RIVERSIDE DICTIONARY 177, 407, 406, 515 (rev. ed. 1996).

[99] WEBSTER'S NINTH NEW COLLEGIATE DICTIONARY 19 (9th ed. 1984) (the "[o]rder of senses [in the dictionary] is historical.").

relatively later in the usage. But that is too ambitious a claim. Rather, each of the different definitions in a dictionary entry would appear to us to be per se reasonable constructions of the word, at least in the absence of context. Contextual material may make it clear that Definition X should prevail rather than Definition Y. But to claim that the words of the definitions themselves admit of clear choice strikes us as simply incorrect.

In examining dictionary definitions, it is also important to remember the dangers of motivated reasoning. As noted D.C. Circuit Judge Harold Leventhal apparently observed when discussing court use of legislative history, it can be a bit like "looking out over a crowd and spotting your friends."[100] But the same, of course, is true regarding selection of a preferred dictionary definition. Insurers (and, of course, policyholders as well) know what they want to be the answer and will naturally be drawn, at least subconsciously, to the definition that best meets their coverage dispute and litigation needs. In addition, dictionary use may mislead through simple happenstance when a judge (or law clerk or counsel writing a brief that influences the judge) reaches for the dictionary that just happens to be on the closest desk or shelf or reads only the first dictionary entry resulting from a browser search. To the extent that there are differences in dictionaries, this human foible of taking the path of least resistance may mislead. In addition, it has been our experience that many dictionary users operate under the false impression that the first definitional entry in a dictionary is the primary or main meaning of a term when, as noted above, it is merely the earliest use of the term.

Thus, decision by dictionary is more than a little problematic. Notwithstanding this human tendency, we think the above excerpts (and we could have listed another dozen or two of similar definitions or associations) establishes that the words "physical loss or damage" admit of construction quite favorable to policyholders.[101] FC&S and others supporting insurers in the COVID coverage

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[100] *See, e.g.* Patricia M. Wald, *Some Observations on the Use of Legislative History in the 1981 Supreme Court Term*, 68 IOWA L. REV. 195, 214 (1983) (citing a conversation with Judge Leventhal), *quoted in* Exxon Mobil Corp. v. Allapattah Servs., Inc., 545 U.S. 546, 568 (2005); Conroy v. Aniskoff, 507 U.S. 511, 519 (1993) (Scalia, J., concurring) (paraphrasing Leventhal); Abner J. Mikva, *Statutory Interpretation: Getting the Law to Be Less Common*, 50 OHIO ST. L.J. 979, 981–82 (1989); Adam M. Samaha, *Looking Over a Crowd—Do More Interpretive Sources Mean More Discretion*?, 92 N.Y.U. L. REV. 554 (2017) (discussing the genealogy and meaning of the quote attributed to Judge Leventhal).

[101] Another possible avenue for assessing the meaning of text is corpus linguistics analysis, which involves assessing the collates and clusters of words as an aid to interpretation. *See* Lawrence M. Solan & Tammy Gales, *Corpus Linguistics as a Tool in Legal Interpretation*, 6 B.Y.U. L. REV. 1311, 1315 (2017). Although in our view, it would be a mistake to attach talismanic power to the use of big data in assessing insurance policy

battles are simply not being fair or reasonable in arguing that this key coverage provision "clearly" or "unambiguously" requires some sort of structural change of insured property as a prerequisite to coverage. Too many courts have accepted this unsupportable shibboleth. Even if their decisions finding no coverage are correct (due to the presence of a virus exclusion or other bar to coverage), these courts have done unnecessary "damage" to norms of insurance policy construction that impacts not only COVID coverage claims but construction of insurance policies as a whole.

As discussed below, insurers typically argue that "damage" entails a requirement of structural change in covered property and that "loss" is largely a synonym for "damage." In our view, the term "loss" connotes something quite different than "damage." For example, dictionaries commonly define "loss" as deprivation of something (whether as a result of "damage," or theft or something else). Government shutdown orders (described below) by definition deprive policyholders of the use of their property—property that is physical, corporeal, choate, and tangible. Although alternative definitions of loss are also common in dictionaries, definitions connoting deprivation, lack of access, or the like are sufficiently common that a reasonable interpreter must concede that the concept of "loss" proffered by a policyholder forced to curtail operations is at least a reasonable meaning of the term.

According to well-established ground rules for insurance policy interpretation, if both policyholder and insurer have set forth reasonable constructions of a term, the term is ambiguous and questions of meaning should be resolved against the insurer that drafted the policy and in favor of the policyholder.

When this interpretative debate takes place at the motion to dismiss stage of litigation, *contra proferentem* (which translates as "against the drafter") logically should have particular force. An early ruling favoring the insurer's implicit argument (that "loss" or "damage" requires structural change in property) effectively involved the court ruling as a matter of law that a definition of loss drawn from dictionaries is not reasonable—an absurd result. If such a construction of the term "loss" was not reasonable, it presumably would not be in a published dictionary.

4. Prior Insurer Industry Action Contradicts Insurers' Current Interpretation Angle

In addition to taking an insurer-serving approach to defining "physical loss or injury," the FC&S assertion that COVID claims fail to involve triggering loss is

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term meaning, this sort of broader based linguistic analysis may be superior to simply "looking it up" in the dictionary at random due to the potential unconscious bias or happenstance of dictionary use.

inconsistent with prior FC&S action. Consider, for example, the following FC&S assessment that predated the COVID pandemic by eight years. An insurance agent made the following inquiry.

> Our insured accidently threw away some digital x-ray sensors in the trash. Now, they want to be compensated for them. The BOP policy, Section 1 Property, Coverage agreement states, "We will pay for direct physical loss . . . ."
> I believe the coverage agreement precludes coverage as this is not "direct physical loss." Nothing happened to them—they were simply thrown away.
> Do you believe coverage exists?

Oregon Subscriber[102]

FC&S replied as follows.

> There is no exclusion that applies to this loss. There does not need to be any impact on or damage to the items themselves for there to be a direct physical loss—just like when items are stolen. But ***there is a loss in that they are no longer available to the insured***.[103]

If FC&S was being consistent with this prior analysis, it would have to acknowledge that businesses forced to close due to either site-specific infection or government mandate have suffered a loss in that the physical business facilities are "no longer available" to them, at least until a government order is lifted or infected property is cleaned and otherwise rehabilitated.

This prior inconsistent statement in the insurance press raises the spectre of how important it is to view all media on an issue in its context and not simply that purpose-built for a particular cause. If insurers wish to flood the current press with commentary, past press on the same and related issues will require defense or acknowledgement, to be fair.

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[102] *Direct Physical Loss Under BOP*, NAT'L UNDERWRITER (June 27, 2011), https://www.nuco.com/fcs/2011/07/12/direct-physical-loss-under-bop-422-12966.

[103] *Id.*

5. Prior Judicial Treatment of the "Physical Loss or Damage" Clauses Has Been More Favorable to Policyholders than Initial COVID Coverage Decisions Suggest

The COVID insurance coverage cases to date have shown that courts prefer some allegations of tangible physical harm to property that alters its essential character and structure in order to trigger business interruption or civil authority coverage for pandemic-related losses. "Direct physical loss of or damage to property" thus seems to require that some external force touches the property and alters it in order for insurance coverage to attach. There is no definition of the coverage clause or its individual composite words in any property insurance policy. In attempting to provide meaning to the coverage clause, courts may have inadvertently hyper-focused on the parsed-out words of the clause as standing alone (i.e. "physical," "loss' and "damage"). The dictionary sections noted in the prior section underline the problems with doing so, because dictionary definitions are inconsistent, are presented in chronological and not frequency order, and can be cherry-picked to "say" what one wants.

Review of the current batch of COVID coverage cases shows that it is possible in some jurisdictions that a policyholder does not need tangible structural harm to property in order to trigger the coverage clause in the policy. The virus does not need to "wreck" some property; it just has to be present to make the property unusable to the policyholder. This reasoning tracks the better-reasoned decisions of courts interpreting "direct physical loss" in other property insurance contexts.[104] Courts have held that the following causes of loss are covered as "direct physical loss or damage:"

a) noxious particles post-9/11 World Trade Center disaster;[105]
b) contamination with radioactive dust and radon gas;[106]

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[104] *See* Scott G. Johnson, *What Constitutes Physical Loss or Damage in a Property Insurance Policy?*, 54 TORT TRIAL & INS. PRAC. L.J. 95 (2019) (surveying caselaw and finding trend and dominance of better reasoned decisions finding loss or damage without palpable destruction or tangible structural alteration of property); Steven Plitt, *Direct Physical Loss in All-Risk Policies: The Modern Trend Does Not Require Specific Physical Damage, Alternation*, CLAIMS J. (Apr. 15, 2013), https://www.claimsjournal.com/magazines/idea-exchange/2013/04/15/226666.htm.

[105] Schlamm, Stone & Dolan, LLP v. Seneca Ins. Co., 800 N.Y.S.2d 356 (Sup. Ct. 2005).

[106] Am. All. Ins. Co. v. Keleket X-Ray Corp., 248 F.2d 920, 925 (6th Cir. 1957).

c) smoke from wildfires cancelling a theatre performance;[107]
d) unpleasant odor making premises uninhabitable (i.e. "locker room" smell, cat urine, or meth lab);[108]
e) drywall releasing poisonous gas rendering home uninhabitable;[109]
f) asbestos in carpeting impaired building's function;[110]
g) asbestos in buildings;[111]
h) mold spores and bacteria rendering home uninhabitable;[112]
i) release of unknown substance in sewage treatment plant causing plant shutdown;[113]
j) hidden building decay due to seawater damage;[114]
k) e-coli contamination in a well;[115]
l) carbon monoxide poisoning;[116]
m) trace amounts of benzene in beverages;[117]
n) metal parts contaminated with lead;[118]
o) salad dressing exposed to vaporized agricultural chemicals;[119]

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[107] Or. Shakespeare Festival Ass'n v. Great Am. Ins. Co., No. 1:15-cv-01932-CL, 2016 WL 3267247, at *5 (D. Or. June 7, 2016).

[108] Essex Ins. Co. v. BloomSouth Flooring Corp., 562 F.3d 399 (1st Cir. 2009) ("locker room" smell); Mellin v. N. Sec. Ins. Co., Inc. 115 A.3d 799 (N.H. 2015) (cat urine odor); Farmers Ins. Co. of Or. v. Trutanich, 858 P.2d 1332 (Or. 1993) (meth lab odor).

[109] TRAVCO Ins. Co. v. Ward, 715 F. Supp. 2d 699, 708 (E.D. Va. 2010).

[110] Sentinel Mgmt. Co. v. Aetna Cas. & Sur. Co., 615 N.W.2d 819, 826 (Minn. 2000).

[111] Yale Univ. v. Cigna Ins. Co., 224 F. Supp. 2d 402, 413 (D. Conn. 2002); Bd. of Educ. of Twp. High School Dist. No. 211 v. Int'l Ins. Co., 720 N.E.2d 622, 625–26 (Ill. App. Ct. 1999).

[112] Sullivan v. Standard Fire Ins. Co., 956 A.2d 643 (Del. 2008); Prudential Prop. & Cas. Ins. Co. v. Lillard-Roberts, No. CV-01-1362-ST, 2002 WL 31495830, at *8–10 (D. Or. June 18, 2002) (applying Oregon law).

[113] Azalea, Ltd. v. Am. States Ins. Co., 656 So. 2d 600, 602 (Fla. Dist. Ct. App. 1995).

[114] Three Palms Pointe, Inc. v. State Farm Fire & Cas. Co., 250 F. Supp. 2d 1357, 1360–61 (M.D. Fla. 2003).

[115] Motorists Mut. Ins. Co. v. Hardinger, 131 F.App'x 823, 823 (3d Cir. 2005).

[116] Matzner v. Seaco Ins. Co., No. Civ. A. 96-0498-B, 1998 WL 566658 (Mass. Super. Aug. 12, 1998).

[117] National Union Fire Ins. Co. of Pittsburgh v. Terra Indus., 346 F.3d 1160 (8th Cir. 2003).

[118] Stack Metallurgical Servs., Inc. v. Travelers Indem. Co. of Conn., No. 05-1315-JE, 2007 WL 464715, at *2 (D. Or. Feb. 7, 2007).

[119] Henri's Food Prods. Co. v. Home Ins. Co., 474 F. Supp. 889, 892 (E.D. Wis. 1979) (applying Wisconsin law).

p) loss of soil supports due to adjacent landslide, even though home itself not damaged;[120]
q) buildup of gas beneath church rendering church uninhabitable;[121]
r) ammonia release;[122]
s) infestation of brown recluse spiders;[123]
t) organisms in canned creamed corn;[124] and
u) cereal oats treated with a non-FDA approved pesticide, even though chemically identical to approved pesticide.[125]

There are also a much smaller group of cases which deny claims for what appear to be very similar or even identical causes of loss like:

a) mold, which apparently could be removed by cleaning;[126]
b) odors or bacteria in an HVAC system;[127] and
c) asbestos contamination which apparently did not alter the structure of the building.[128]

The reasoning featured in the first list of cases finding coverage for more ephemeral physical losses also tracks the better-reasoned decisions in recent cases involving coverage for cyber-losses under property policies. Insurance claims for electronic data losses also went through a similar wave as COVID insurance claims as courts wrestled with whether or not electronic data stored on a computer could experience a "direct physical loss or damage" because it appears to be intangible and

[120] Hughes v. Potomac Ins. Co. of D.C., 199 Cal. App. 2d 239, 248 (1962).
[121] W. Fire Ins. Co. v. First Presbyterian Church, 437 P.2d 52, 55 (Colo. 1968).
[122] Gregory Packaging, Inc. v. Travelers Prop. & Cas. Co. of Am., No. 2:12-cv-04418, 2014 WL 6675934 at *5–6 (D.N.J. Nov. 25, 2014) (applying New Jersey and Georgia law).
[123] Cook v. Allstate Ins. Co., No. 48D02-0611-PL-01156, 2007 Ind. Super. LEXIS 32, at *7–9 (Ind. Super. Ct. Nov. 30, 2007).
[124] Pillsbury Co. v. Underwriters at Lloyd's, 705 F. Supp. 1396, 1401 (D. Minn. 1989).
[125] Gen. Mills, Inc. v. Gold Medal Ins. Co., 622 N.W.2d 147, 152 (Minn. Ct. App. 2001).
[126] Mastellone v. Lightning Rod Mut. Ins. Co., 884 N.E.2d 1130, 1144–45 (Ohio Ct. App. 2008).
[127] Universal Image Prods. v. Chubb Corp., 703 F. Supp. 2d 705, 713 (E.D. Mich. 2010).
[128] Great N. Ins. Co. v. Benjamin Franklin Fed. Sav. & Loan Ass'n, 793 F. Supp. 259 (D. Or. 1990), *aff'd*, 953 F.2d 1387 (9th Cir. 1992).

is unseen by the naked eye, existing as data on a hard drive or in the online cloud.[129] Courts have treated losses relating to electronic data and computer equipment in sometimes strange ways.

The more reasonable and now widely accepted approach has been to find that electronic data losses are capable of being covered as a "direct physical loss" under a property policy when the data is corrupted, lost or damaged. Many courts have found that, although data cannot be seen or touched, it nevertheless exists in some fashion electronically and microscopically as property and can suffer a direct physical loss.[130] Indeed, it would be foolish to have a property policy cover data loss if the data were stored in hard paper copy and destroyed, but then deny coverage for a similar loss if the data exists in electronic form. That would make for perverse record-keeping incentives.

Holding that a virus like COVID-19 can at least potentially damage property makes sense in this regard. The virus does render surfaces unusable to humans for a period of time. It is potentially deadly and spreads quickly, through touched surfaces or the air. One would assume insurers would not want business owners putting employees and customers in infected stores if such would vastly increase the risk of an even larger claim if a person became ill or died (though such a claim would be made under a different insurance product: liability insurance or workers compensation).

The long list of cases that have considered various external forces' impact on property as a "direct physical loss" demonstrate that courts are willing to find coverage if the force is a disease-causing agent or poison, if it is purely airborne, and if it does not permanently affect or even alter in any way the physical property insured. "Loss" or "damage" can mean "lost to the policyholder" in terms of use, in a variety of ways that do not involve actual physical destruction of the property.

The case law supports a conclusion that physical damage from a virus does not have to be permanent; it can be transient.[131] With a virus like COVID-19, an

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[129] *See* Stempel & Knutsen, *supra* note 33, at §23; Erik S. Knutsen & Jeffrey W. Stempel, *The Techno-Neutrality Solution to Navigating Insurance Coverage for Cyber Losses,* 122 PA. STATE U. L. REV. 645, 646–47 (2018).

[130] *See, e.g.*, Ashland Hosp. Corp. v. Affiliated FM Ins. Co., No. 11-16-DLB-EBA, 2013 WL 4400516, at *5 (E.D. Ky. Aug. 14, 2013) (finding disk drive damage due to excessive temperatures is a "direct physical loss" at a microscopic level); Se. Mental Health Ctr., Inc. v. Pac. Ins. Co., 439 F. Supp. 2d 831, 837 (W.D. Tenn. 2006) (finding data corrupted by power loss at pharmacy is a covered "direct physical loss").

[131] *See, e.g.*, Phibro Animal Health Corp. v. Nat'l Union Fire Ins. Co. of Pittsburgh, No. A-5589-13T3, 2016 WL 3884255, at *9–10 (N.J. Super. Ct. App. Div. July 14, 2016) (finding that medicine given to chickens that stunted their growth constituted

insured property may be impacted, and a loss may ensue in two typical scenarios: immediately after an infected customer or employee becomes ill on the premises or, more broadly, while the virus itself is highly prevalent in the community in question and therefore must be on the premises.

For the first scenario—that of immediate infection of an employee—it would seem that physical loss or damage would be simple to prove. There was virus present on the property. No one can tell where it spread or on what surfaces. It may well be in the air or ventilation system. Entry to the property is thus dangerous until the illness reasonably subsides, decontamination has occurred, and it is again safe to enter.

But for the second scenario—that of virus generally prevalent in the community—can coverage attach simply because the illness is potentially 'out there?' In that instance, reasoning such as that featured in the *Studio 417, Inc. v. Cincinnati Insurance Company*[132] case is helpful: where the virus is so highly prevalent such that a large proportion of the population is ill (and sometimes without any knowledge of being ill) to the degree that civil authorities are making orders restricting both use of property and peoples' movement, then one can probably assume actual presence of virus on the property somehow, especially at a place of business open to the public. At a certain point in time, the harm will of course subside. Those cases holding that physical damage does not have to be permanent to trigger coverage support reasoning that coverage would last as long as the danger is rendering the property unfit for use.

A number of cases have found coverage due to the imminent threat of physical loss or damage:

a) government shutdown due to impending riots;[133]
b) evacuation from an imminent building collapse;[134]
c) an impending hurricane;[135]

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property damage, despite the possibility of the chickens being restored to their original conditions, because property damage need not be permanent).

[132] No. 20-cv-03127-SRB, 2020 WL 4692385 (W.D. Mo. Aug. 12, 2020) (applying Missouri law).

[133] *See, e.g.*, Sloan v. Phoenix of Hartford Ins. Co., 207 N.W.2d 434, 437 (Ct. App. Mich. 1973) (finding loss of use due to government shutdown in response to riots is covered even though there is no direct physical loss to property).

[134] *See, e.g.,* Hampton Foods, Inc. v. Aetna Cas. & Sur. Co., 787 F.2d 349, 352 (8th Cir. 1986).

[135] *See, e.g.*, Houston Cas. Co. v. Lexington Ins. Co., No. H-05-1804, 2006 WL 7348102, at *6 (S.D. Tex. June 15, 2006) (finding coverage for business interruption due to

d) imminent landslide;[136]
e) imminent threat of release of asbestos fibres.[137]

However, other cases have found that fears of future threats did not constitute a covered loss because there was no loss to property.[138]

The threat of something can make property uninhabitable. The threat of COVID-19 is quite serious: the virus is highly contagious, spreads through the air and surfaces, and can be deadly. Those in close indoor quarters to the virus also have a high possibility of contracting the disease. To that end, the COVID-19 situation perhaps differs from those cases that have found that future threats did not equate to a loss in property. The possibility of damage in the COVID-19 situation is relatively high if virus is in the vicinity. It is not like taking a preventative measure after an event out of concern for a follow-up event (like ordering a curfew after a socially disruptive event). Rather, it is a highly likely scenario that putting someone in close indoor proximity to the virus will make that person ill. It is more similar to the impending earthquake and hurricane cases where one knows the event is on its way, than it is to those where losses stemmed from concerns of more vague future events occurring. With COVID-19, a significant number of people sufficiently exposed indoors will get sick.

This highlights one other area of coverage concern: actual physical damage versus loss of use or function of property to the policyholder. There is support in

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evacuation arising from impending Hurricane Floyd, even though policyholder did not suffer physical damage to property from hurricane).

[136] *See, e.g.*, Murray v. State Farm Fire & Cas. Co., 509 S.E.2d 1, 16–17 (W. Va. 1998) (finding threat of imminent landslide enough to satisfy "direct physical loss" for coverage to attach).

[137] Port Auth. v. Affiliated FM Ins. Co., 311 F.3d 226, 236 (3d Cir. 2002).

[138] *See, e.g.,* United Air Lines v. Ins. Co. State of Pa., 439 F.3d 128, 133–35 (2d Cir. 2006) (finding no civil authority coverage where a government halt of airport operations is based on fears of future attacks after Sept. 11, 2001 and no property damage to adjacent property); Paradies Shops, Inc. v. Hartford Fire Ins. Co., No. 1:03-CV-3154-JEC, 2004 WL 5704715, at *6–8 (N.D. Ga. Dec. 15, 2004) (finding no property damage from air ground stop order after Sept. 11, 2001 as the order did not prohibit access to airports and their businesses); Syufy Enters. v. Home Ins. Co. of Ind., No. 94-0756 FMS, 1995 WL 129229, at *2 (N.D. Cal. Mar. 21, 1995) (finding curfews imposed to curb looting were not the result of damage to adjacent property); Two Caesars Corp. v. Jefferson Ins. Co. of N.Y., 280 A.2d 305, 307–08 (D.C. Cir. 1971) (finding acts of avoiding civil unrest had no causal relation to damage to property).

case law such as *Gregory Packaging*[139] where loss of use or function of a particular property can equate to direct physical loss without tangible physical harm to the property. While property may not be permanently damaged by COVID-19, a policyholder loses the use of that property in a reasonable fashion if there is an infection on the premises or the virus present in the surroundings. Some courts have held that the disjunctive "or" between "physical loss of or damage to" property must mean that "loss" must mean something different than "damage" (typically it is held to mean an absence of property, as in theft). In that regard, "loss" could mean "loss of use" or "loss of function" such that it renders the property useless to the policyholder (i.e. if you lost the useful use of the property, it is as if you lost it, even though it did not physically go away). In fact, the textualist dictionary analysis as noted above also provides support for "loss" equating to "loss of use."

There is, however, a line of cases often cited by courts adjudicating this first wave of COVID insurance coverage cases—from *Source Food Technology, Inc. v. United States Fidelity and Guaranty Co.*[140] and *Mama Jo's, Inc. v. Sparta Insurance Co.*[141]—that would hold that only tangible physical alteration of property would qualify as "direct physical loss or damage." But unlike in those cases, where the courts held respectively that an import ban did not damage imported beef or construction dust did not damage music speakers, the COVID-19 situation has a dangerous substance actually physically present on the property, either in the air or through employees and customers spreading it. This tracks the reasoning in COVID insurance coverage cases finding for the policyholder like *Studio 417,*[142] *Blue Springs Dental Care v. Owners Ins. Co*[143] and *Mudpie, Inc. v. Travelers Casualty Ins. Co. of America*,[144] where the courts there held that pleading actual physical presence of the virus made the analytical difference in proving coverage through a "direct physical loss."[145] Indeed, in many of the past non-COVID cases that found a "direct physical loss" due to the invasion of some harmful substance, the substance

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[139] Gregory Packaging, Inc. v. Travelers Prop. Cas. Co. of Am., No. 2:12-CV-04418 WHW, 2014 WL 6675934, at *8 (D. N.J. Nov. 25, 2014) (applying New Jersey and Georgia law).

[140] 465 F.3d 834 (8th Cir. 2006) (applying Minnesota law).

[141] 823 Fed. App'x 868 (11th Cir. 2020) (applying Florida law).

[142] 2020 WL 4692385 (W.D. Mo. Aug. 12, 2020) (applying Missouri law).

[143] No. 20-CV-00383-SRB, 2020 U.S. Dist. LEXIS 172639 (W.D. Mo. Sept. 21, 2020).

[144] No. 20-CV-03213-JST, 2020 WL5525171 (N.D. Cal. Sept. 14, 2020) (applying California law).

[145] We discuss these cases, particularly *Studio 417*, *supra* note 142, in more detail in the next section, *infra*, as we find their reasoning quite superior to that of most of the courts dismissing policyholder claims on grounds of no physical loss or damage—as a matter of law.

merely resulted in the property owner not being able to use the property until decontamination occurred. This strongly suggests that dismissing COVID claims merely because property can be disinfected is incorrect.

In some jurisdictions, merely partially restricted access to a property does not equate to a prohibition of access by civil authority.[146] In other instances, a recommendation from a civil authority (as opposed to a direct command) may be not enough to provide coverage because access was not "prohibited."[147] For COVID-19-related losses, it can be challenging to argue that government ordered alterations in service provision—such as a mandated move from in-person dining to take-out and delivery only—results in lost or restricted access to the property or even use of the property.[148] However, on balance, a restaurant faced with this imposed condition could certainly argue that a large proportion of its property typically used for dine-in customers has been rendered entirely unusable by a civil authority.[149]

As the cases now stand, courts appear to be receptive to finding coverage for direct physical loss or damage if the policyholder alleges some factual aspects of physical presence of the virus on the commercial premises. The courts in *Studio 417* and *Blue Springs Dental Care* found the possibility of coverage for this reason and

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[146] *See, e.g.*, Ski Shawnee, Inc. v. Commonwealth Ins. Co., No. 3:09-CV-02391, 2010 WL 2696782 (M.D. Pa. July 6, 2010) (stating there is no coverage when Department of Transport closed main route to policyholder's ski resort because customers could travel to the resort via an alternate route); Abner, Herrman & Brock, Inc. v. Great N. Ins. Co., 308 F. Supp. 2d 331 (S.D.N.Y. 2004) (noting that after World Trade Center disaster, civil authority coverage only provided where order completely prohibited access to property and not during periods where traffic restrictions made access merely more difficult); 54th St. Ltd. Partners v. Fid. & Guar. Ins. Co., 306 A.D.2d 67 (asserting that although traffic to property was diverted, the public was not denied access).

[147] *See, e.g.*, Kean Miller LLP v. Nat'l Fire Ins. Co. of Hartford, No. 06-770-C, 2007 WL 2489711, at *6 (M.D. La. Aug. 29, 2007) (holding that an advisory to stay off streets during Hurricane Katrina did not prohibit access; no civil authority coverage).

[148] *See, e.g.*, Phila. Parking Auth. v. Fed. Ins. Co., 385 F. Supp. 2d 280 (S.D.N.Y. 2005) (finding that government order eliminated need for policyholder's parking services but did not prohibit access to its garage).

[149] Although this line of argument was unsuccessful in Henry's La. Grill, Inc. v. Allied Ins. Co. of Am., No. 1:20-cv-2939-TWT, 2020 WL 5938755 (N.D. Ga. Oct. 6, 2020) (applying Georgia law), where the policyholder restaurant argued that a physical change to the property had occurred because the restaurant had to reconfigure its premises for take-out, not dine-in, as a result of governmental orders. The court held that "loss" means "total destruction" and simply moving things around was not a "loss" or "damage." *See also* Hajer v. Ohio Sec. Ins. Co., No. 6:20-cv-00283, 2020 WL 7211636 (E.D. Tex. Dec. 7, 2020) (applying Texas law) (finding no damage and dismissing case after policyholder argued it had to physically alter its rug business to follow governmental safety order).

the court in *Mudpie* notes it would have, had the policyholder alleged the presence of the virus.

At its heart, this logic follows the case law stemming from *Gregory Packaging* as opposed to the *Source Foods/Mama Jo's* line of reasoning. Whether or not there needs to be tangible physical damage to property in order for coverage to be triggered, there must be some invasion of the virus physically on the premises in question for coverage to attach.

IV. THE DISAPPOINTING EARLY CASELAW CONCERNING COVID-19 BUSINESS INTERRUPTION CLAIMS

A. THE PREVAILING ANALYSIS

Cases testing the extent of business interruption insurance coverage for COVID-19 pandemic-related losses are still winding their way through the legal system. To date, court decisions have been made largely in the context of motions to dismiss a policyholder's claim on the pleadings, with no factual record except the pleadings taken by the court as true. Thus, the emerging caselaw is currently limited in its predictive ability as a fulsome canvassing of the issues.

Two distinct lines of reasoning and factual trends have emerged thus far in the case law. Courts are split as to whether the main coverage clause which requires "direct physical loss of or damage to" covered property is even triggered as a result of COVID-19 business interruption losses.

The majority of decisions to date have held that, for "direct physical loss of or damage to" property to have occurred, the property in question must have been physically altered in some tangible fashion. As COVID-19 does not permanently alter the physical characteristics of property, but rather makes people ill by infecting through the air or on touchable surfaces, most courts have found that there is thus no coverage for business interruption losses unless the policyholder specifically alleges the actual physical presence of the virus was on its premises (i.e. on surfaces, in the air, or through infected customers or employees).

If a policyholder alleges physical presence of the virus, some courts to date have found that the covered property was requisitely affected directly and physically by the alleged presence of the virus, even though the virus is microscopic and the property itself appears to be capable of decontamination. The loss of use of the property either through necessary decontamination or as a result of virus presence was enough for those courts to hold that business interruption coverage was triggered as a result of "direct physical loss of or damage to" property.

When determining coverage for losses resulting from civil authority orders, courts have split along the same line. If a policyholder can allege the actual physical presence of the virus on adjacent property that resulted in the order being made, the claim is not dismissed. However, if there are no allegations of the physical presence of the virus on other or adjacent property that prompted governmental authorities to restrict property access, governmental orders to quell the spread of the virus are not enough to trigger loss of use of the property to a degree that it is "direct" and "physical." These courts denying coverage rest their reasoning on a causation analysis: the virus, not the orders, caused the loss and the virus does not cause direct physical loss unless actual tangible property damage is alleged.

If a property policy has an exclusion for losses caused by viruses or bacteria, courts appear to be ready to deny coverage to policyholders on the face of the exclusionary language, without much more than a cursory analysis. Courts appear to link the cause of any governmental orders restricting property access to the reason for those orders: the virus, an excluded cause of loss. If the virus exclusion has an anti-concurrent cause clause, courts appear even more ready to deny coverage for business interruption or civil authority claims without much substantive analysis.

The cases wrestling with coverage for pandemic-related losses due to COVID-19 commonly engage with lines of reasoning from three prior precedents: the 11th Circuit 2020 decision in *Mama Jo's, Inc. v. Sparta Insurance Co.*[150] (applying Florida law), the 2014 U.S. District Court for the District of New Jersey case of *Gregory Packaging, Inc. v. Travelers Property and Casualty Co. of America*[151] (applying New Jersey and Georgia law), and the 8th Circuit 2006 decision in *Source Food Technology, Inc. v. United States Fidelity and Guaranty Co.*[152] (applying Minnesota law). These cases highlight the tension between two possible approaches to pandemic-related insurance coverage issues: a strict requirement that the insured property suffer tangible physical alteration to property as a result of some external force (the *Mama Jo's* and *Source Food* approach) versus the notion of loss of "use" of the property equating to physical loss or damage to property, even though the physical property itself is not permanently altered by some external force (the *Gregory Packaging* approach).

In *Mama Jo's*, the policyholder restaurant was denied its business interruption and remediation claims when the restaurant's lighting and audio equipment was coated with dust from outside road construction. Under Florida law, the court held that surfaces that can be cleaned have not suffered a direct physical

[150] 823 Fed. App'x 868 (11th Cir. 2020) (applying Florida law).

[151] No. 2:12-CV-04418, 2014 WL 6675934 (D. N.J. Nov. 25, 2014) (applying New Jersey and Georgia law).

[152] 465 F.3d 834 (8th Cir. 2006)(applying Minnesota law).

loss: the damage must be tangible and physical, resulting in an actual change in the property. Although dust in the accumulations involved in that case is a tangible contaminant, the court regarded the property as undamaged because it could be wiped away, even though cleaning on this scale exceeded that required for normal business operations.

In *Source Food Technology*, a beef wholesaler brought a claim for business interruption insurance due to lost revenue resulting from an embargo of Canadian beef after reports of "mad cow" disease. Source Food's sole supplier of beef was located in Ontario, Canada. The beef was not contaminated by mad cow disease. The claim for losses was as a result of the inability to ship the beef across the border. The court held that there was no direct physical loss or damage to the beef—it simply could not be shipped across the border. Thus, there was no coverage for the loss. The court specifically refused to adopt the position that "direct physical loss or damage is established whenever property cannot be used for its intended purpose."[153]

A different approach was taken by the court in *Gregory Packaging*.[154] In that case, the accidental release of ammonia in a juice box manufacturing plant required that the facility be decontaminated and evacuated. According to the court, the ammonia release physically transformed the air within the manufacturer's facility to make it unsafe. Because the facility was unusable for a period of time, the court held that the property suffered a direct physical loss. Even though, under Georgia law, coverage requires an actual physical change in property, the court held that that requirement was satisfied because the ammonia release physically changed the facility's condition to such a state that it needed repair.

B. MISAPPLYING TRADITIONAL CONTRACT AND INSURANCE LAW

Our own preference is for the *Gregory Packaging* approach rather than the *Mama Jo's* or *Source Foods* approach. But we find the early cases dismissing policyholder COVID claims disturbing not only because of their doctrinal choices but also because they in our view reflect a reductionist view and absence of judicial humility. In particular, the courts finding no "direct physical loss or damage" have been insufficiently appreciative of the range of meanings for these words that in turn makes it inappropriate for courts to declare a lack of triggering loss or damage as a matter of law.

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[153] *Id.* at 838 (citing Marshall Produce Co. v. St. Paul Fire & Marine Ins. Co., 98 N.W.2d 280 (Minn. 1959)).

[154] 2014 WL 6675934 (applying New Jersey Law).

1. Glib Tautology and False Consensus Bias

Particularly troubling examples are *Social Life Magazine, Inc. v. Sentinel Insurance Company*[155] (in which the court blithely declared that there was no loss or damage to covered property because COVID "damages lungs. It doesn't damage printing presses"), *Sandy Point Dental, PC v. Cincinnati Insurance Company*,[156] *Gavrilides Managment Company. v. Michigan Insurance Co*mpany,[157] and *Rose's 1, LLC v. Erie Insurance Exchange*.[158]

The *Social Life Magazine* statement may make for a clever punchline but it is not even particularly accurate as a medical statement, let alone as an analysis of potential insurance coverage.[159] COVID's impact is not confined to lungs but includes many other organs such as kidneys and the brain as well as senses of hearing and smell.[160] More to the point for insurance purposes, viral infestation of a printing

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[155] No. 1:20-cv-03311-VEC (S.D.N.Y. Apr. 29, 2020).

[156] No. 20 CV 2160, U.S. Dist. LEXIS 171979 (N.D. Ill. Sept. 21, 2020).

[157] No. 20-000258-CB (Mich. Cir. Ct., Ingham Cty. July 1, 2020) (explaining that direct physical loss to property requires tangible alteration or damage that impacts the integrity of the property, and dismissing the case because plaintiff failed to allege that the coronavirus had any impact to the premises).

[158] No. 2020 CA 002424 B, 2020 WL 4589206, at *5 (D.C. Super. Aug. 6, 2020) (granting summary judgment for insurer on restaurant's claims of lost business caused by coronavirus closure orders because there was no direct physical loss to property).

[159] A similar sort of reasoning featured in Plan Check Downtown III, LLC v. Amguard Ins. Co., No. cv 20-6954-GW-Skx, 2020 WL 5742712 (C.D. Cal. Sept. 10, 2020) (applying California law), where a restaurant's claim was dismissed because the court anchored its finding that "loss" requires tangible alteration to property because otherwise any regulatory change from any governmental order that affected any business in any fashion would trigger business interruption insurance. It went further to opine that even a snowstorm interferes with "use" of premises for the business by customers and employees and surely covering losses from snowstorms would make business interruption coverage far too broad.

[160] The same concept was picked up by the court in Uncork & Create LLC, v. Cincinnati Ins. Co., No. 2:20-cv-00401, 2020 WL 6436948 (S.D.W. Va.) (applying West Virginia law) which denied coverage and went so far as to state that it would deny coverage even if there was physical presence of the virus. The court held that COVID-19 does not harm inanimate structures, can be eliminated with disinfectant and routine cleaning. *Id.* at 5. The court went so far as to state that even the actual presence of the virus on the property is not enough to trigger the coverage clause "physical damage or physical loss to the property." *Id.* at 6. *See also* Promotional Headwear Int'l v. Cincinnati Ins. Co., No. 20-cv-2211-JAR-GEB, 2020 WL 7078735 (D. Kan. Dec. 3, 2020) (applying Kansas law) where the court (on a motion to dismiss on the pleadings!) does not accept the policyholder's allegations that the virus contaminated its property, citing both Source Food Technology, Inc. and Mama Jo's, Inc.;

facility does, for the reasons discussed above, damage the facility's air quality and its equipment. Although the "fix" may be relatively straight-forward cleaning, it is damage nonetheless and renders the facility unusable until cleaned—a process that may become so repetetive due to re-infection as to constitute long-term damage and loss of use. More important, if this and other pandemic injury result in government-ordered limitations on operation of the policyholder's property, this produces rather direct physical loss to the policyholder.

Sandy Point Dental makes a similarly breezy and overly restrictive reading of the direct physical loss or damage trigger. Although the court recognizes that Illinois law is applicable, it cites no Illinois cases regarding loss or damage[161] even though there are important state law decisions finding that adulterated air or surfaces can constitute physical damage to property.[162] If *Sandy Point Dental* had merely

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Terry Black's Barbecue, LLC v. State Auto. Mut. Ins. Co., No. 1:20-cv-665-RP, 2020 WL 7351246 (W.D. Tex. Dec. 14, 2020) (applying Texas law) (citing Uncork & Create, LLC and holding that, even assuming the virus is present, the court held it can be cleaned).

[161] The *Sandy Point Dental* court's citation of Illinois law is limited to general pronouncements, including the axiom that a court construing an insurance policy should be "giving effect to every provision, if possible, because it must be assumed that every provision was intended to serve a purpose." No. 20-cv-2160, 2020 U.S. Dist. LEXIS 171979, at *3-4 (quoting *Valley Forge Ins. Co. v. Swiderski Elecs., Inc*., 860 N.E. 307, 314 (Ill. 2006). But this "surplusage" canon of construction (discussed *supra* text accompanying notes 85–86) augers in favor of giving "loss" a sufficiently distinct meaning from "damage." But instead of doing this, the *Sandy Point Dental* court treats the words as synonyms but then focuses only on the term "damage," which connotes more tangibility than "loss." The court also notes that Illinois requires words in a policy to be giving their "plain, ordinary, and popular meaning." *See* U.S. Dist. LEXIS 171979 at *4 (citing Central Ill. Light Co. v. Homes Ins. Co., 821 N.E.2d 206, 213 (Ill. 2004)). As previously discussed, (*see supra* test accompanying notes 90–99), there is ample evidence in dictionaries and thesauruses suggesting the plain and ordinary meaning approach augers in favor of finding loss when a policyholder's use of property is restricted by viral infection or government order.

[162] Illinois has had more than its share of asbestos coverage cases, the bulk of which have concluded that the presence of asbestos materials in a structure or in the interior air of a building constitutes physical damage. *See, e.g*., J.R. French Auto. Castings, Inc. v. Factory Mut. Ins. Co., No. 02-c-9479, 2003 U.S. Dist. LEXIS 13060 (N.D. Ill. July 23, 2003) (noting that the presence of human remains in a press machine constituted contamination that was physical damage even though equipment not tangibly structurally altered but no coverage because of exclusionary language in policy); Affiliated FM Ins. Co. v. Board of Educ., No. 90-c-6040, 1992 U.S. Dist. LEXIS 15151 (N.D. Ill. Oct. 5, 1992) (noting that contaminated air is physical damage and the inability to use because of contamination is physical loss); Lapham-Hickey Steel Corp. v. Prot. Mut. Ins. Co., 655 N.E.2d 842 (Ill. 1995) (finding no duty to defend because a formal lawsuit was not filed but suggesting that contamination can

followed this applicable law, it would have reached a correct decision on the motion to dismiss. But the court simply failed to locate (whether due to deficient advocacy or something else) or examine these precedents.

In addition, the *Sandy Point Dental* court seems to have forgotten that even in a world of heightened pleading requirements, the court faced with a Rule 12(b)(6) motion to dismiss must (absent extreme circumstances) treat the allegations of the plaintiff's complaint as true.[163] Instead, the court in essence second-guessed those allegations, with the judge refusing to accept them at face value.

And in perhaps its lowest moment of judicial craft, *Sandy Point Dental* sought to distinguish an important decision favoring the policyholder.

> Plaintiff heavily relies on *Studio 417 Inc. v. The Cincinnati Insurance Company, 20 C 3127-SRB, 2020 U.S. Dist. LEXIS 147600 (S.D. Mo. Aug. 12, 2020)*, a Missouri case that found that the coronavirus caused a physical loss to property warranting insurance coverage. That court rested its decision on that policy's expansive language, language very different from the policy in the instant case. The unambiguous language in the instant policy warrants a different conclusion—physical damage that demonstrably alters the property is necessary for coverage, and the coronavirus does not cause physical damage.[164]

Unfortunately, *Sandy Point's* characterization is simply not true. The Cincinnati policy form at issue in *Studio 417* (and the *KC Hopps* and *Blue Springs Dental* cases also decided in the Western District of Missouri) is the same (at least regarding the direct physical loss requirement and the absence of a virus exclusion) as the Cincinnati policy at issue in *Sandy Point*.

In an opinion read from the bench, *Gavrilides Management*,[165] like *Sandy Point*, conflates the term "loss" and the term "damage," robbing them of their respectively different connotations and emphases. Worse yet, it engrafts on the term

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be physical damage and lack of access can be physical loss of property); Universal Underwriters Ins. Co. v. LKQ Smart Parts, Inc., 963 N.E.2d 930 (Ill. Ct. App. 2011) (noting that the deprivation of use of a vehicle is physical loss) (but there was also tangible physical damage to vehicle); Board of Educ. v. Int'l Ins. Co., 720 N.E.2d 622 (Ill. Ct. App. 1999) (finding that the presence of asbestos fibers in air constituted physical damage to property).

[163] *See* Ashcroft v. Iqbal, 556 U.S. 662 (2009); BROOKE D. COLEMAN, ET AL., LEARNING CIVIL PROCEDURE 285–302 (3d ed. 2018).

[164] No. 20-cv-2160, 2020 U.S. Dist. LEXIS 171979, at *7 n. 2.

[165] No. 20-000258-CB (Mich. Cir. Ct., Ingham Cty. July 1, 2020).

(having collapsed loss and damage into one) a requirement that property must have been permanently, structurally altered to be considered sufficiently "damaged" to merit coverage from the property insurer that, in return for premium dollars (sometimes years of premium dollars), promised to indemnify the policyholder from property loss and attendant business revenue loss.

Although one can argue that this was a correct reading of Michigan law, we are not convinced in that there appears to be no controlling Michigan precedent requiring this approach, which essentially denies coverage unless property is crushed.[166] Consequently, although not compelled to take a more nuanced view of the loss-or-damage requirement, the *Gavrilides Management* judge could (and in our view should) have done so.

Rose's 1, LLC v. Erie Insurance Exchange,[167] is disturbing in that, as that court acknowledges, the policyholder proffered definitions of the terms "loss" and "damage" that supported its position. But the court essentially ignored these definitions and adopted definitions it prepared—refusing to recognize that reasonable alternative constructions of a term or provision create ambiguity requiring resolution against the insurer. This is certainly true at the pleading stage. Although *Rose's 1* was a summary judgment decision, we think the same caution in terminating a case in the face of reasonable conflicting constructions of a policy should govern.

It appears that despite the summary judgment posture of the case, the record before the court did not include any extrinsic or discovery-unearthed evidence illuminating the meaning of policy language. Rather, the parties appear to have briefed the case based on textual argument alone, making the posture of the case akin to a 12(b)(6) motion. But instead of deferring to the facts as alleged and resolving any reasonable doubts against the nonmovant, the *Rose's 1* court granted summary judgment after it concluded—based on nothing we can discern—that "loss" requires "a direct physical intrusion on to the insured property."[168] As we

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[166] Although there are federal trial court cases requiring structural change to property to constitute sufficient physical loss or damage, there does not appear to be state court precedent binding on the *Gavrilades* court. *But see* Universal Image Prod. v. Chubb Corp., 703 F. Supp. 2d 705 (E.D. Mich. 2010) (finding that intangible harms such as odor or mold contamination insufficient to constitute physical loss or damage even though property was rendered unusable).

[167] No. 2020-CA-002424-B, 2020 WL 4589206 (D.C. Super. Ct. Aug. 6, 2020*)* (granting summary judgment for insurer on restaurant's claims of lost business caused by coronavirus closure orders because there was no direct physical loss to property).

[168] *Id.* at *7.

hope we have demonstrated, government orders limiting or forbidding use of physical facilities constitute a physical loss to the owner.

Diesel Barbershop, LLC v. State Farm Lloyds[169] displays a similarly disturbing approach to textual analysis. The court, like others finding for insurers, collapses what should be the distinct terms "loss" and "damage" and despite the many dictionary and thesaurus entries supporting a reading of the policy favorable to policyholders, selects the entries most favorable to the insurer contention requiring tangible and rather substantial, long-lasting, structural and character altering injury before there can be coverage. Likewise, the real loss of a physical facility due to COVID-spurred government restriction is given short shrift. To be fair, the *Diesel Barbershop* court recognizes cases that "some courts have found physical loss even without tangible destruction to the covered property."[170] However, "[e]ven so," *Diesel Barbershop* found "that the line of cases requiring tangible injury to property are more persuasive here."[171] That was in essence the scope and depth of the court's "analysis."

The problem with the court's conclusion is that it was to a large degree not the court's decision to make if it was following the rules of insurance policy construction. Because ambiguities are to be resolved in favor of the policyholder that did not draft the language at issue, a policyholder that proffers a reasonable construction of disputed language (such as "loss" or "damage") is entitled to the benefit of the doubt—at least regarding a Rule 12(b)(6) motion where another well-established "rule" is that the allegations of plaintiff policyholder's complaint must be accepted as true. Discovery may later provide information refuting those allegations and supporting the defendant insurer. But until such time as such discovery takes place, the factual universe upon which the court decides is supposed to be limited to the complaint.

Although research (such as reading dictionaries or cases) may bring extrinsic material into the inquiry, the policyholder need not shoulder the ultimate burden of persuasion at this stage of the litigation. It need only set forth a reasonable construction of the policy language that supports its claim for coverage. Policyholders seeking COVID coverage have done that. They may ultimately lose

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[169] No. 5:20-CV-461-DAE, 2020 WL 4724305, at *5 (W.D. Tex. Aug. 13, 2020) (granting a motion to dismiss because the coronavirus did not cause a direct physical loss, and "the loss needs to have been a 'distinct, demonstrable physical alteration of the property.'") (citing Hartford Ins. Co. of Midwest v. Mississippi Valley Gas Co., 181 F.App'x 465, 470 (5th Cir. May 25, 2006)).

[170] *Id.* at *14–15.

[171] *Id.* at *15–16 (concluding that "the other cases [finding loss or damage] are distinguishable.").

due to further factual development establishing lack of loss or damage or due to application of a virus exclusion or other factors. But they should not lose on the loss/damage issue at this stage of litigation.

These and other decisions[172] in which courts are willing to declare as a matter of law that the words "direct physical loss or damage" require structural

[172] *See, e.g.*, Mark's Engine Co. No. 28 Rest., LLC v. Travelers Indem. Co. of Conn., No. 2:20-cv-04423-AB-SK, 2020 WL 5938689 (C.D. Cal. Oct. 2, 2020) (applying California law) (involving a restaurant that claimed losses due to orders requiring take-out or delivery service only); Promotional Headwear Int'l v. Cincinnati Ins. Co., No. 20-cv-2211-JAR-GEB, 2020 WL 7078735 (D. Kan. Dec. 3, 2020) (applying Kansas law) (citing both *Source Food* and *Mama Jo's* to hold that physical alteration of property required for coverage to attach); Infinity Exhibits, Inc. v. Certain Underwriters at Lloyd's London, No. 8:20-cv-1605-T-30AEP, 2020 WL 5791583 (M.D. Fla. Sept. 28, 2020) (applying Florida law); Hillcrest Optical, Inc. v. Cont'l Cas. Co., No. 1:20-CV-275-JB-B, 2020 WL 6163142 (S.D. Ala. Oct. 21, 2020) (applying Alabama law); Raymond H Nahmad DDS PA v. Hartford Cas. Ins. Co., No. 1:20-cv-22833-BLOOM/Louis, 2020 WL 6392841 (S.D. Fla. Nov. 2, 2020) (applying Florida law); Palmer Holdings & Invs., Inc. v. Integrity Ins. Co., No. 4:20-cv-154-JAJ, 2020 WL 7258857 (S.D. Iowa) (applying Iowa law); T&E Chicago LLC v. Cincinnati Ins. Co., No. 20 C 4001, 2020 Wl 6801845 (N.D. Ill. Nov. 19, 2020) (applying Illinois law); Whiskey River on Vintage, Inc., v. Ill. Cas. Co., No. 4:20-cv-185-JAJ, 2020 WL 7258575 (S.D. Iowa Nov. 30, 2020) (applying Iowa law); Zwillo V, Corp. v. Lexington Ins. Co., No. 4:20-00339-CV-RK, 2020 WL 7137110 (W.D. Mo. Dec. 2, 2020) (applying Missouri law); Water Sports Kauai, Inc. v. Fireman's Fund Ins. Co., No. 20-cv-03750-WHO, 2020 WL 6562332 (N.D. Cal Nov. 9, 2020) (applying Hawai'ian law); Long Affair Carpet & Rug, Inc. v. Liberty Mut. Ins. Co., No.: SACV 20-01713-CJC(JDEx), 2020 WL 6865774 (C.D. Cal. Nov. 12, 2020) (applying California law); Michael Cette, Inc. v. Admiral Indem. Co., 20 Civ. 4612 (JPC), 2020 WL 7321405 (S.D.N.Y. Dec. 11, 2020) (applying New York law); Real Hosp., LLC v. Travelers Cas. Ins. Co. of Am., No. 2:20-cv-00087-KS-MTP, 2020 WL 6503405 (S.D. Miss. Nov. 4, 2020) (applying Mississippi law); Henry's Louisiana Grill, Inc. v. Allied Ins. Co. of Am., No. 1:20-CV-2939-TWT, 2020 WL 5938755 (N.D. Ga. Oct. 6, 2020) (applying Georgia law); Newchops Rest. Comcast LLC v. Admiral Indem. Co., No. CV 20-1869, 2020 WL 7395153 (E.D. Pa. Dec. 17, 2020) (applying Pennsylvania law); Brian Handel DMD, PC v. Allstate Ins. Co., No. 20-3198, 2020 WL 6545893 (E.D. Pa. Nov. 6, 2020) (applying Pennsylvania law); Hajer v. Ohio Security Ins. Co., No. 6:20-cv-00283, 2020 WL 7211636 (E.D. Texas Dec. 7, 2020) (applying Texas law); Terry Black's Barbecue, LLC v. State Auto. Mut. Ins. Co., No. 1:20-CV-665-RP, 2020 WL 7351246 (W.D. Tex. Dec. 14, 2020) (applying Texas law); Santo's Italian Café LLC v. Acuity Ins. Co., No. 1:20-cv-01192, 2020 WL 7490095 (N.D. Ohio) (applying Ohio law); Graspa Consulting, Inc. v. United Nat'l Ins. Co., No. 20-23245-CIV-WILLIAMS, 2021 WL 199980 (S.D. Fla. Jan. 20, 2021) (applying Florida law); S. Fla. ENT Assocs, Inc. v. Hartford Fire Ins. Co., No. 20-23677-Civ-WILLIAMS/TORRES, 2020 WL 6864560 (S.D. Fla. Nov. 13, 2020) (applying Florida law); Plan Check Downtown III, LLC v. AmGUARD Ins. Co., No. Cv 20-6954-GW-SKx, 2020

alteration of the property only reflect judges succumbing to false consensus bias—the tendency of humans to be overconfident that others see things as they do. Significant research suggests this is a particular problem in the interpretation of contracts and other writings. For example, in one study, respondents were given contract language to read and construe. They then were asked whether they thought other readers could reach a different interpretation.[173]

Overwhelmingly, they expressed confidence that others would agree with their reading of the words and that there was no significant interpretive issue as to the document's meaning. Overwhelmingly, they were wrong. The same contract language was being read by other respondents who were reaching a different conclusion as to the meaning of the words.

This tendency, which also accords with cognitive traits such as self-serving bias (the tendency for people to think they are better at things than is actually the case),[174] can be particularly pernicious in judges who by job description need to be decisive (and move on to the next case), and are consistently the object of deference or even adulation (e.g., more likely to be invited to be graduation speakers or faculty in residence than all but a few celebrity lawyers), and who by definition in an adversary system have half the disputants praising each decision.

The net result can often be a brusque, reductionist, insufficiently reflective approach to reading documentary text, including but not limited to statutes, regulations, rules, exhibits, and contracts in addition to insurance policies. The judge, despite frequently reading the text in a vacuum without background contextual information, the aid of a linguist, or more than the closest dictionary or those cited by counsel, quickly determines that she "knows" what the disputed language means. More troublingly, the judge "knows" this so well that she dispenses with further inquiry and dismisses the case.

WL 5742712 (C.D. Cal. Sept. 10, 2020) (applying California law); Kirsch v. Aspen Am. Ins. Co., No. 20-11930, 2020 WL 7338570 (E.D. Mich. Dec. 14, 2020) (applying Michigan law); Mortar & Pestle Corp. v. Atain Specialty Ins. Co., No. 20-cv-03461-MMC, 2020 WL 7495180 (N.D. Cal. Dec. 21, 2020) (applying California law). *But see, e.g.,* Seifert v. IMT Ins. Co., No. 20-1102 (JRT/DTS), 2020 WL 6120002 (D. Minn. Oct. 16, 2020) (applying Minnesota law) (holding that Minnesota law does not require a showing of structural damage to qualify for coverage).

[173] *See* Lawrence Solan, et al., *False Consensus Bias in Contract Interpretation*, 108 COLUM. L. REV. 1268 (2008).

[174] *See* Linda Babcock & George Loewenstein, *Explaining Bargaining Impasse: The Role of Self-Serving Biases,* 11 J. ECON. PERSPECTIVES 109 (1997) (describing phenomenon and its impact in prompting disputants or negotiating parties to overvalue their own skills, conduct, and position in transactions or litigation).

Although this is troubling to us in any case, it is particularly troubling in the insurance context, where the ground rules of adjudication discussed below, if properly followed, are essentially designed to give policyholders the benefit of the doubt. To borrow a baseball term, "ties" are supposed to "go to the runner." But like the umpire whose right thumb jerks upward if the ball is in the vicinity of first base before the runner has clearly planted a foot, courts taking an aggressively self-reverential view about the meaning of policy language bend the rules in the opposite direction.

In a world where reasonable people may debate the meaning of "direct physical loss or damage" in various contexts, courts should be reluctant to declare meaning as a matter of law. In view of the differing dictionary definitions and case outcomes, such an approach ordinarily amounts to error in COVID claims.

We realize of course that where controlling law provides a clear precedent, it must be followed. If, for example, the Supreme Court of State X has declared in no uncertain terms that both "loss" and "damage" in the property insurance setting always requires tangible, permanent (unless repaired by more than cleaning) injury to the structure or character of property, that precedent must be followed by trial courts no matter how much a trial judge thinks it incorrect. But where case law is mixed, unclear, or absent, trial courts should be taking the more modest approach to perceived certainty of textual meaning.

To be fair, many, perhaps even most, of the courts dismissing policyholder COVID claims have at least considered caselaw taking the broader view of "direct physical loss or damage." But they have then quickly pivoted to the narrower view certainty unwarranted in light of the dictionary definitions favoring the broader view. Couple this with the established insurance policy interpretation principles favoring policyholders that have been given short shrift by courts dismissing COVID coverage claims and the result is error—at least on the questions of whether loss or damage has occurred (and most certainly at the motion to dismiss stage of litigation).

Depending on the specifics of each case, insurers may prevail on any number of other defenses to coverage such as the virus exclusion or non-COVID defenses such as misrepresentation or intentional destruction or insurers may limit their liability based on calculation of lost business income as well as policy limits or sub-limits. But they generally should not be prevailing on the loss/damage question to the extent reflected in opinions to date. A brief review of a few important insurance concepts underscores this assessment.

2. Reasonable Policyholder Expectations of Coverage for Pandemic-related Losses

Consider policyholder and insurer expectations of coverage for pandemic-related losses. If there is rampant confusion as to the scope of coverage such that litigation is arriving at mixed results, perhaps there is a more insidious problem with what is driving that litigation. The reasonable policyholder likely expected that a product marketed and labelled as "business interruption insurance" or "civil authority coverage" would extend coverage to the policyholder's income stream in the event the policyholder was unable to access or reasonably use its business premises. The reasonable policyholder purchasing an "all risk" policy likely would not have thought that such coverage would hang on how the damage—if any—to the property occurred. Rather, their focus would likely be on their income loss due to either virus contamination or prevention of use of their property due to governmental orders.

Particularly in the case of civil authority coverage, few policyholders would likely expect that, in many instances in order to trigger coverage, there would have to be some physical damage to adjacent property that would prompt a civil authority to restrict access to the policyholder's property. Policyholders may ironically be better off if their property or adjacent property had burned down, rather than operations ceased by a virus, strange though it may seem. By the mere label of the product alone—"business interruption insurance"—there are likely many policyholders who simply believe that the insurance insures their profit stream. The impetus for that belief may well, in the end, rest with issues of misleading nomenclature by insurers and misleading sales by brokers and agents.

From an insurer's standpoint, the reasonable insurer may well not have meant nor expected to cover losses relating to a pandemic like COVID-19 in the contexts of business interruption insurance included in commercial property policies. By its nature, a pandemic is a clash event that has the potential to seriously strain insurer resources. Yet surely the industry had modelled a pandemic because it has already seen the effects of SARS, MERS, Ebola, H1N1, swine flu, and HIV/AIDs. And there were products on the market specifically designed to cover pandemic-related losses. The existence of related products like event cancellation insurance makes the generalized insurer contention of "whoever would have predicted COVID-19?" a bit strained.

The more compelling insurer response to pandemic-related losses is perhaps to assert that the business interruption product was never meant to be "guaranteed

profit insurance."[175] It is an insurance add-on coverage to property insurance. There surely must be some risks in commerce that are not covered by a property policy. For example, no one would expect business interruption coverage for profit losses in a nuclear war (though of course there are exclusions for nuclear causes of loss). But what of, say, a zombie apocalypse or alien invasion, that required governments to issue "stay at home" orders or risk being eaten by green beings? Would the standard business interruption coverage tied to commercial property policies kick in then? Is there then a direct physical loss of or damage to property? Likely not. There are zombies or aliens running about. The property is likely just fine. But again, property owners may have difficulty accessing their property or even be barred from it due to civil authority orders or otherwise.

Some insurers included a virus exclusion in their policy wording before the pandemic struck. Does that mean that those insurers without a virus exclusion did not mean to exclude such losses? Is the virus exclusion itself a rock-solid denial of coverage, under all loss scenarios?

Perhaps instead the business interruption (and by corollary, the civil authority) insurance product needs to be retooled and re-messaged to communicate precisely what is and what is not meant to be covered. Otherwise, in the insurance world, if coverage is unclear, ties go to the policyholder—or at least they should. The insurer must provide coverage until new policy language is drafted in new versions of insurance policies.

3. Causation, Civil Authority Coverage and the Virus Exclusion

The trigger of coverage for civil authority business interruption losses rests largely on arguments of insurance causation. Policyholders continue to allege that a civil authority order caused their pandemic-related business interruption losses by restricting their access to their property. To date, courts have perhaps incorrectly declined coverage because they have held that the cause of the policyholder's losses is not the order and that no physical loss or damage occurred to prompt the order in the first place.

It is important to keep in mind how causation works in the insurance law context and how it is different than principles of tort causation. In assessing insurance causation in a property loss context, one should work backward from the

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[175] A notion picked up by the court in Real Hosp., LLC v. Travelers Cas. Ins. Co. of Am., No. 2:20-cv-00087-KS-MTP, 2020 WL 6503405, at *8 (S.D. Miss. Nov. 4, 2020) (emphasis omitted) (applying Mississippi law), which held that "this is a commercial property policy, not a stand-alone business interruption policy—Plaintiff's operations are not what is insured—the building and the personal property in or on the building are."

loss claimed (here, the loss of profit) and ask what external force affected the property to result in the loss and thus potentially trigger the coverage claimed? The analysis is not a temporal one (i.e. last in time) but rather one of effect: what "hurt" the policyholder such that it suffered the loss claimed? For property claims, the answer to insurance causation questions is usually straightforward: what external force damaged the property? The insurance causation analysis does not involve analyzing chains of causation, as one might do in a tort analysis. Fault, blame, or responsibility play no part in insurance causation. Instead, a court is to determine what external force "hurt" the policyholder such that it triggered the particular loss claimed. The inquiry is decidedly contractual.

The loss to the policyholder is the lost profit from an inability to operate the business. The "hurt," so to speak, in the civil authority coverage case, is actually arising from the order of the civil authority restricting access to the property (whether employee or customer access). The virus did not need to touch any of the policyholder's property to result in the economic loss that affected the policyholder. Even the threat of the virus is not necessary. The cause of the loss is thus the civil authority order which restricted access to the policyholder's property.

In a jurisdiction that adheres to the proximate cause doctrine of insurance causation, the proximate cause of the loss in this scenario—for civil authority coverage insurance purposes—is the governmental order. It is analytically incorrect to chase down what made the governmental authority issue the order in the first place—unless the coverage provisions specifically require such a causal inquiry.

In some cases, such an inquiry is necessary if—and only if—the coverage grant requires a finding that the loss must flow from a covered cause which results in direct physical loss or damage to adjacent property. Only if the coverage granting language specifically asks for such an analysis should a court attempt to ask "why" a governmental order was issued. And even then, it should only ask the simple question: was the order issued due to a covered cause which resulted in direct physical loss or damage to property adjacent to the policyholder?

In the case of a civil authority coverage case where there is a virus exclusion in the policy, the causation analysis is a bit more nuanced. If the coverage grant for civil authority insurance does not require direct physical loss or damage to property, but merely the restriction of access to the property, then the virus exclusion has no effect on coverage for the policyholder. The cause of the loss is the governmental order, not the virus.

While the prevention of the virus was the impetus for the order, coverage cannot be ousted simply because the "topic" of the order was "about" the COVID-19 virus. The topic did not harm the policyholder, nor did the virus; the actual effect of the order did. Policyholders should not lose coverage because of the topic of the

times behind a governmental order or even the reasoning behind the order. Coverage should only be ousted when the order did not cause the harm claimed.

However, if the coverage grant for civil authority insurance requires direct physical loss or damage to property, then the policyholder would apparently need to prove that the reasoning behind the civil authority order was indeed related to property damage which occurred. Such can be alleged with the COVID-19 virus by indicating the virus was present in frankly any adjacent property that was in an area affected by COVID-19, so long as that jurisdiction will consider that the presence of the virus can constitute direct physical loss or damage.

The issue is, of course, less clear if the property policy contains a virus exclusion. Some virus exclusions have an anti-concurrent cause clause such that coverage is ousted as long as virus contamination played some role in the ensuing loss. One can argue that the virus did not play a concurrent role in the loss (although it may have been a reason for the order—but the exclusion does not ask about the 'story' behind the order—its focus is the cause of the loss claimed for insurance purposes).

An example of such a scenario occurred when the policyholder massage spa in *Elegant Massage, LLC v. State Farm Mutual Automobile Insurance Company*[176] was forced to close due to a specific governmental order that mandated the closure of spas and massage services due to the inability of those particular businesses to maintain safe social distancing in a time of particularly serious virus spread. The spa and massage business was thus forced to close as a direct result of this specific order. The spa also voluntarily closed even after the order was lifted, because it could not maintain the required social distancing measures and still conduct its business. The policyholder argued the order, not the virus, caused its losses. The court agreed, because the policyholder's specific type of business was targeted by the order—it was not just a general health measure. The court also noted that Virginia does not support anti-concurrent causation clauses; insurers must draft specific language to oust coverage and there must be a direct connection between the exclusion and the loss (not some tenuous connection anywhere in the chain of causation).

The catch-22 is realized when a coverage grant tied to direct physical loss to property is coupled with a virus exclusion. In that instance, alleging that the civil authority coverage is a result of virus contamination may well trigger the virus exclusion.[177]

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[176] No. 2:20-cv-265, 2020 WL 7249624 (E.D. Va. Dec. 9, 2020) (applying Virginia law).

[177] Professor Dan Schwarcz has been quoted as taking the view that where a policy has a virus exclusion, the case against coverage is "open and shut." Caroline Glenn, *Insurers Are Telling Businesses Their Policies Don't Cover Coronavirus Shutdown. John Morgan Attorneys Say They're Wrong*, ORLANDO SENTINEL (May 4, 2020),

4. Ambiguity in Property Coverage for Pandemic-related Losses

It may well be that the coverage clause "direct physical loss of or damage to property" is by now so tortured and unpredictable in caselaw as to be rendered ambiguous in terms of insurance policy construction. Indeed, three courts have found just that.

In *Elegant Massage, LLC v. State Farm Mutual Automobile Insurance Company*,[178] the court noted that the coverage clause does not overtly require structural damage for coverage to attach. Because there was such a "spectrum" of meanings of "direct physical loss of or damage," the court interpreted the clause in a light most favourable to the policyholder. If the property (here, a spa which requires close contact with, and touching of, patrons) was deemed uninhabitable, inaccessible and dangerous to use as a result of governmental orders because of the high risk for spreading COVID-19, then the policyholder suffered direct physical loss. The court drew analogies to those cases where the policyholder could not use its property due to toxic gasses from drywall or odor or asbestos.

In *North State Deli, LLC v. The Cincinnati Insurance Co*.,[179] the court scoured the wide variety of dictionary definitions and determined that "loss" can equate to the loss of a full range of rights and advantages of property use. It held the coverage clause was ambiguous and thus settled on a reasonable definition which favours coverage: that "direct physical loss" can mean loss of use or access, even if the property is not structurally altered.

Finally, in *Hill and Stout PLCC v. Mutual of Enumclaw Insurance Company*,[180] the court held that physical "loss" must mean something different than physical "damage." "Loss" could mean "deprivation." The dental practice at issue in that case had direct physical deprivation of its premises as a result of the

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https://www.orlandosentinel.com/coronavirus/jobs-economy/os-bz-coronavirus-insurance-denials-morgan-lawsuits-20200504-pbrpq6z7ofbevau67cpgq4nzqi-story.html. Although one of us (Stempel) tends to agree that coverage is probably inapt in most such cases, the other (Knutsen) is hesitant. In any event, we think the issue is closer than commonly thought because of the long history of causation doctrine that tends not to look beyond the immediate cause of loss if the cause is a sufficiently dominant factor in bringing about the loss. *See* Erik S. Knutsen, *Confusion About Causation in Insurance: Solutions for Catastrophic Losses*, 61 ALA. L. REV. 957 (2010); Peter Nash Swisher, *Insurance Causation Issues: The Legacy of* Bird v. St. Paul Fire & Marine Ins. Co., 2 NEV. L.J. 351 (2002).

[178] 2020 WL 7249624 (E.D. Va. Dec. 9, 2020) (applying Virginia law).

[179] North State Deli, LLC v. The Cincinnati Ins. Co., No. 20-CVS-02569, 2020 WL 6281507 (N.C. Super. Oct. 9, 2020) (Trial Order).

[180] No. 20-2-07925, 2020 WL 6784271 (Wash. Super.) (Trial Order).

governmental order stopping dental visits because the practice could not see patients or practice dentistry. To that end, because the pleadings were silent about the meaning of "loss," the court held that physical "loss" is an ambiguous phrase, and the case could proceed.

A review of the various dictionary definitions above for these terms certainly should be leading other courts to also consider ambiguity. In some cases, asbestos contamination is a direct physical loss. In others, it is not. In some cases, prevention of access to property by a government order is a direct physical loss. In others, it is not. Under the doctrine of *contra proferentem*, a finding of ambiguity leads to the policy terms being interpreted in favor of the policyholder. If policyholders and insurers alike—and clearly courts—cannot predict the meaning of the phrase and what it is supposed to do as the main coverage trigger for perhaps the most prevalent insurance product on the market, and if so much litigation is produced resulting from this confusion, then ambiguity of the coverage clause may be a reasonable conclusion for courts to make.

C. THE POTENTIAL FOR COVID INSURANCE COVERAGE CASES AS A BLUEPRINT FOR BETTER DECISION-MAKING

A few cases (three decided by the same Western District of Missouri court) have found coverage for COVID-related losses, albeit in a motion to dismiss context and without a full factual record: *Studio 417, Inc. v. Cincinnati Insurance Company*,[181] *K.C. Hopps v. Cincinnati Insurance Company,*[182] *Blue Springs Dental Care v. Owners Insurance Company*,[183] and *Elegant Massage, LLC v. State Farm Mutual Automobile Insurance Company*.[184] The other cases denying coverage have attempted to distinguish these cases on a number of grounds primarily related to the specific facts plead by the policyholders (i.e. the presence of a virus-specific exclusion or the specific allegations of virus particles actually physically present on insured property).

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[181] No. 20-cv-03127-SRB, 2020 WL 4692385 (W.D. Mo. Sept. 12, 2020) (applying Missouri law).

[182] 2020 U.S. Dist. LEXIS 144285 (W.D. Mo. Aug. 12, 2020) (applying Missouri law). *K.C. Hopps v. Cincinnati* is a short opinion that incorporates the Court's analysis in *Studio 417* because that case "involves the same Defendant, similar insurance provisions, and similar factual allegations as those asserted in this case. Defendant also moved to dismiss *Studio 417* under Rule 12(b)(6) based on similar legal arguments that it presents in this case." *Id*. at *2.

[183] 2020 U.S. Dist. LEXIS 172639 (W.D. Mo. Sep. 21, 2020).

[184] 2020 WL 7249624 (E.D. Va. Dec. 9, 2020) (applying Virginia law).

The *Studio 417* and *Elegant Massage* cases remain the most analytically satisfying decisions to date,[185] as they most thoroughly deal with competing precedents and convey a broader understanding of the importance of insurance as a risk-based commercial product packaged to commercial policyholders. The other decisions denying coverage, in the main, tend to resort to a restrictive line of case precedents that narrow insurance recovery based largely on a purely textual parsing of insurance policy language, on a "know it when I see it" basis. Those decisions do not convey a broader understanding of what the coverage clause or property policies generally are meant to do in the consumer marketplace.

The *Studio 417* case more fully accounts for the historical caselaw interpreting the "direct physical loss or damage" coverage clause—both for and against coverage. The case also demonstrates the most doctrinally defensible analysis of the insurance causation elements of the claim. The policyholders in that case operated restaurants and hair salons. They claimed for pandemic-related losses under their business interruption and civil authority coverage contained in their all-risk property policies. Their claims were denied. The policy in question provided coverage for a "direct loss," which is defined as "accidental physical loss or accidental physical damage." Notably, there was no virus exclusion in this policy.

The policyholders alleged that customers and employees were infected with COVID-19 and the insured property became contaminated with the virus as a result. They argued that the virus is a physical substance that is active on tangible surfaces, and renders property unsafe and unusable. This quality of the virus forced the policyholders to suspend operations or at least reduce them. The policyholders also alleged that civil authorities in Missouri and Kansas issued orders that required suspension of businesses at various places, including closure orders. The policyholders alleged that both the presence of COVID-19 on the property plus the government closure orders resulted in direct physical loss or damage to the property and denied the policyholders the full use of the property.

The court found that there is a possibility of coverage despite the fact that the virus could be cleaned from physical surfaces or dies naturally within a few days. The fact that access to the property was prohibited or severely restricted was enough to find a possibility of coverage at this stage. In this regard, the court relied on the *Gregory Packaging, Inc. v. Travelers Property and Casualty Co. of America*[186] case,

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[185] This is not said in derogation of *Blue Springs Dental v. Owners Ins*., which unlike *K.C. Hopps* contains extensive discussion and analysis. Although *Blue Springs Dental* involved somewhat different policy language and business activities, its analysis is heavily shaped by *Studio 417*, discussed at length in this section.

[186] No. 2:12-cv-04418 (WHW)(CLW), 2014 WL 6675934, at *1 (D.N.J. Nov. 25, 2014) (applying New Jersey law).

where ammonia contamination at a juice packaging plant triggered insurance coverage because the manufacturer's buildings were uninhabitable due to the contamination. Even though the policyholders in *Studio 417* likely could not prove that COVID-19 was specifically on their premises, the fact that the virus was so widespread was enough to obviate the issue for the court.

The court held that COVID-19 is a physical substance which lives on surfaces and is transmitted through the air. COVID-19 makes property unsafe and unusable, resulting in "direct physical loss of or damage to" property. One does not need to prove tangible physical alteration of property to trigger coverage.

The court also held that loss of use of property is different than "damage;' otherwise, the word "damage" would be rendered superfluous in the coverage clause. The fact that the property could not be used due to COVID-19 was enough for the court to hold the policyholders had suffered a potential loss of the property. The court distinguished the line of cases that require policyholders to prove a tangible physical alteration to the property in order to trigger the coverage clause. The court distinguished the *Source Food Technology, Inc. v. U.S. Fidelity & Guarantee Co*mpany[187] case, which granted summary judgment to an insurer who denied coverage when the policyholder's meat could not cross the Canadian border due to meat infection concerns. The *Studio 417* court held that the policyholders' allegations posit contamination of the property with a physical substance: the COVID-19 virus. This was therefore a different situation than the *Source Foods* case where there was no evidence the beef was actually contaminated by mad cow disease.

The policyholders also had potential coverage under a claim for civil authority insurance. According to the court, government orders affected hair salons by forcing their closure and affected restaurants by not allowing diners to dine inside the premises. Only drive-through or pick-up or delivery orders were allowed for restaurants. This was sufficient for the court to find that access was prohibited to such a degree as to trigger the civil authority coverage. The court held that the virus was physically present in property other than the policyholder's, because it was "everywhere" and therefore that satisfied the "direct physical loss or damage" coverage requirement.

The court specifically held that the civil authority coverage clause required access to be prohibited but the language did not mandate that all access had to be fully prohibited. The fact that access to the policyholders' property was impeded to a significant degree was sufficient for coverage to attach. Along the same logic, the court held that the policyholders also had potential coverage under the property policy's ingress and egress, dependent property, and sue and labor provisions.

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[187] 465 F.3d 834, 835 (8th Cir. 2006) (applying Minnesota law).

The same federal court denied an insurer's motion to dismiss the claims of policyholder dental clinics in *Blue Springs Dental Care v. Owners Insurance Company*[188] The dental clinics claimed business interruption and civil authority losses when Missouri and corresponding counties issued 'stay at home' orders to quell the virus spread. Three dental clinics completely closed and one remained open only for essential and emergency dental cases. The policyholder pled that its property was damaged because of the presence of COVID-19 on and around its property such that it had to either end or reduce its operations due to actual contamination. It also alleged that employees, customers, and other visitors likely were infected with the coronavirus and thus operations were suspended to prevent physical damage to property and to the people on it. The 'stay at home' orders and general fear of infection or spreading COVID-19 on the property itself meant that customers could not access the property.

The insurer in this case argued that the fact that the one clinic was offering some services meant that its operations were not suspended within the meaning of coverage under the policy. The insurer also argued that the policyholder's clinics suffered no "direct physical loss of or damage to" property. As was the case in *Studio 417*, there was no exclusion for pandemics or communicable diseases in the applicable policy.[189]

The court found that COVID caused the policyholder's alleged physical loss in that the virus physically occupied and contaminated the dental clinics. This deprived the policyholder of use of the clinics, making them unsafe. The court also held that the policyholder necessarily suspended its operations to prevent physical damage from COVID. The COVID virus was the cause of the suspension and implicated business interruption coverage.

The court also held that the policyholder would be entitled to civil authority coverage because the orders by the state and counties do not need to be directed specifically at insured property or property adjacent to it in order to trigger coverage. The court cited *Studio 417* with approval, reiterating that policyholders do not need to completely lose all access to property—coverage could be had for partial impeded access. In this case, although three of the clinics closed entirely and the other had only limited dental services for emergency patients, access was prohibited to such a

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[188] 2020 U.S. Dist. LEXIS 172639.

[189] Nor was there a virus exclusion in the policies at issue in K.C. Hopps v. Cincinnati Ins. Co., 2020 U.S. Dist. LEXIS 144285 (W.D. Mo. 2020). It thus appears that Cincinnati sold a significant number of policies without a virus exclusion and may face significant coverage responsibility in cases where courts take a similar view of the "direct physical loss or damage" requirement and where government orders mandated closure.

degree as to trigger coverage. The court left open the question as to the effect of the order that targeted essential versus non-essential businesses.

The important factor in the *Studio 417* and *Blue Springs Dental Care* cases is that the policyholders alleged specific physical damage through the presence of COVID-19 virus on the insured property in question. That allowed the court to find a direct physical loss, and thus the potential for coverage. The fact that contamination was not permanent was not an issue restricting the coverage analysis. The court also held that direct physical loss could be had through loss of use of the property. The court also had little issue with connecting the causal chain of the presence of COVID-19 virus on property, its prevalence in the community, and the inability of the policyholders to use their property as a result of governmental orders arising directly from the presence of COVID-19.

The court in *Elegant Massage* granted coverage to a massage spa when the spa was forced to close due to governmental orders. The spa's business model required the touching and close proximity to customers which was the very risk the orders were trying to quell in prevention of the virus. After the mandatory closure order ended, the spa still voluntarily closed as it was exceedingly difficult to comply with the mandated physical distancing requirements and still provide massage services. As mentioned above, the court found the coverage clause "direct physical loss of or damage to property" ambiguous because the clause does not specifically require distinct, structural damage for coverage to attach. If the insurer wished such a requirement, it could have added that language. Therefore, by interpreting the clause in a fashion most favorable to the policyholder, the court held that the loss of use of the policyholder's property qualified as a "direct physical loss." The court, however, denied civil authority coverage to the policyholder as it would not show a causal link between any damaged surrounding properties and its own. Simply put, there was no structural damage to the policyholder's premises—only loss of use and access.

V. CASELAW AND THE VIRUS EXLCUSION

As is by now clear, we are concerned, perhaps to the point of being dismayed, that so many courts have so credulously embraced the view that as an absolute matter of law viral infection of premises cannot be physical loss or damage to insured premises and that there is no coverage even where government authorities have deprived policyholders of use of their property. This reading of policy language—especially its cocksure construction that refuses to recognize alternative reasonable reading of the words—poses significant potential problems not only for COVID coverage cases but for property insurance disputes generally.

That said, this first wave of cases may be an example of erroneous judicial reasoning that nonetheless arguably reaches a correct result, at least in many instances. Of the COVID coverage decisions made as this article was written, all but a handful had favored insurers. In nearly all of these cases granting insurer dismissal motions on the basis of what we regard as incorrect application of the physical-loss-or-injury trigger, the policies at issue also contained a virus exclusion. As discussed below, the standard ISO virus exclusion is broadly drafted and was intended by insurers to preclude coverage for certain virus-related losses. In some cases, drafting, communication, or claims-handling errors of an insurer may make a virus exclusion ineffective. Or there may be particular facts of a claim that negate the virus exclusion, like issues of causation.[190]

As discussed below, despite the apparent clarity of the virus exclusion, it may well be ineffective in some loss situations. In addition, the prevalence of virus exclusions in policies is unclear. As noted above, in the decisions to date, a fourth of the policies at issue lacked a virus exclusion. A preliminary study of liability insurance policies suggests that the majority of these policies lack a virus exclusion.[191] Regarding property insurance, however, insurers contend that eighty percent or more of the policies contain virus exclusions. Although that figure that accords with the polices in court decisions to date,[192] it is a sufficiently high percentage that we harbor concerns that may be overstated. For example, the policies of Cincinnati Insurance Company, involved in nearly 200 cases filed, tend not to have a virus exclusion.[193]

Prior to the SARS tragedy of the early Twenty-first Century, insurance policies did not contain virus exclusions, although many did have bacteria, fungus, or mold exclusions. And there is, of course, the pollution exclusion that we think has no application to infection-related loss but that insurers continue to occasionally push as a defense to coverage. Insurers effectively accepted that their policies of the pre-SARS era did not exclude—at least not with sufficient clarity—viral infection losses and responded by drafting a rather comprehensive virus exclusion.

The exclusion and its rationale were presented to regulators in a 2006 ISO circular.[194] The key operative phrase of the exclusion reads: "We will not pay for

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[190] *See, e.g.*, Elegant Massage, LLC v. State Farm Mut. Auto. Ins. Co., No. 2:20-cv-265, 2020 WL 7249624 (E.D. Va. Dec. 9, 2020) (applying Virginia law) (finding no direct connection between exclusion and loss; governmental order, not virus, direct cause of loss; and exclusion inapplicable).

[191] *See* Baker*, supra*, note 10.

[192] *See id.* (identifying 174 cases filed against Cincinnati as of Oct. 21, 2020).

[193] *Id.*

[194] ISO VIRUS EXCLUSION, *supra* note 25.

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."[195] Some virus exclusions also contain an anti-concurrent cause clause, which attempts to exclude coverage regardless as to whether the damaged complained of is concurrently caused with another non-virus-related cause or not.[196] In particular, the circular stated:

> While 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.[197]

Case law to date has supported application of the ISO virus exclusion to exclude coverage for COVID-related losses in a near-automatic fashion, without subjecting the exclusion to any meaningful analysis.[198] The virus exclusion has been

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[195] *Id.*

[196] *See, e.g.*, the policy at issue in Diesel Barbershop, LLC v. State Farm Lloyds, No. 5:20-cv-461-DAE, 2020 WL 4724305 F.Supp.3d (W.D. Tex. 2020) (applying Texas law).

> 1. We do not insure under any coverage for any loss which would not have occurred in the absence of one or more of the following excluded events. We do not insure for such loss regardless of: (a) the cause of the excluded event; or (b) other causes of the loss; or (c) whether other causes acted concurrently or in any sequence with the excluded event to produce the loss; or (d) whether the event occurs suddenly or gradually, involves isolated or widespread damage, arises from natural or external forces, or occurs as a result of any combination of these: . . .
>
> **j. Fungi, Virus Or Bacteria**
>
> . . . (2) Virus, bacteria or other microorganism that induces or is capable of inducing physical distress, illness or disease.

Id.

[197] ISO VIRUS EXCLUSION, *supra* note 25.

[198] *See, e.g.*, Seifert v. IMT Ins. Co., No. 20-1102 (JRT/DTS), 2020 WL 6120002 (D. Minn. Oct. 16, 2020) (applying Minnesota law) (holding that losses resulted from order, not virus, but anti-concurrent loss provision in virus exclusion ousts coverage because virus is part of causal chain of loss); Founder Inst. Inc. v. Hartford Fire Ins. Co., No. 20-cv-04466-VC, 2020 WL 6268539 (N.D. Cal. Oct. 22, 2020) (applying California law) (rejecting

policyholder argument that governmental orders were about spread of saliva and respiration droplets, not virus; virus exclusion applies); Border Chicken AZ LLC v. Nationwide Mut. Ins. Co., No. CV-20-00785-PHX-JJT, 2020 WL 6827742 (D. Ariz. Nov. 20, 2020) (applying Arizona law); Chattanooga Prof. Baseball LLC v. Nat'l Cas. Co., No. CV-20-01312-PHX-DLR, 2020 WL 6699480 (D. Ariz. Nov. 13, 2020) (applying Arizona law); Franklin EWC, Inc. v. Hartford Fin. Servs. Grp., Inc., No. 20-cv-04434 JSC, 2020 WL 5642483 (N.D. Cal. Sept. 22, 2020) (applying California law); Mark's Engine Co. No. 28 Rest., LLC v. Travelers Indem. Co. of Conn., No. 2:20-cv-04423-AB-SK, 2020 WL 5938689 (C.D. Cal. Oct. 2, 2020) (applying California law); Raymond H Nahmad DDS PA v. Hartford Cas. Ins. Co., No. 1:20-cv-22833-BLOOM/Louis, 2020 WL 6392841 (S.D. Fla. Nov. 2, 2020) (applying Florida law); W. Coast Hotel Mgmt., LLC v. Berkshire Hathaway Guard Ins. Co., No. 2:20-cv-05663-VAP-DFMx, 2020 WL 6440037 (C.D. Cal. Oct. 27, 2020) (applying California law); Palmer Holdings & Invs., Inc. v. Integrity Ins. Co., No. 4:20-cv-154-JAJ, 2020 WL 7258857 (S.D. Iowa) (applying Iowa law); Whiskey River on Vintage, Inc., v. Ill. Cas. Co., No. 4:20-cv-185-JAJ, 2020 WL 7258575 (S.D. Iowa Nov. 30, 2020) (applying Iowa law); Natty Greene's Brewing Co. v. Travelers Cas. Ins. Co. of Am., No. 1:20-CV-437, 2020 WL 7024882 (M.D.N.C. Nov. 30, 2020) (applying North Carolina law); Wilson v. Hartford Cas. Co., No. 20-3384, 2020 WL 5820800 (E.D. Pa. Sept. 30, 2020) (applying Pennsylvania law); N&S Rest., LLC v. Cumberland Mut. Fire Ins. Co., No. 20-05289 (RBK/KMW), 2020 WL 6501722 (D.N.J. Nov. 5, 2020) (applying New Jersey law); Long Affair Carpet & Rug, Inc. v. Liberty Mut. Ins. Co., No.: SACV 20-01713-CJC(JDEx), 2020 WL 6865774 (C.D. Cal. Nov. 12, 2020) (applying California law); Real Hosp., LLC v. Travelers Cas. Ins. Co. of Am., No. 2:20-cv-00087-KS-MTP, 2020 WL 6503405 (S.D. Miss. Nov. 4, 2020) (applying Mississippi law); Newchops Rest. Comcast LLC v. Admiral Indem. Co., No. CV 20-1869, 2020 WL 7395153 (E.D. Pa. Dec. 17, 2020) (applying Pennsylvania law); Brian Handel DMD, PC v. Allstate Ins. Co., No. 20-3198, 2020 WL 6545893 (E.D. Pa. Nov. 6, 2020) (applying Pennsylvania law); Hajer v. Ohio Security Ins. Co., No. 6:20-cv-00283, 2020 WL 7211636 (E.D. Texas Dec. 7, 2020) (applying Texas law); Vizza Wash, LP v. Nationwide Mut. Ins. Co., No. 5:20-cv-00680-OLG, 2020 WL 6578417 (W.D. Tex. Oct. 26, 2020) (applying Texas law); Terry Black's Barbecue, LLC v. State Auto. Mut. Ins. Co., No. 1:20-CV-665-RP, 2020 WL 7351246 (W.D. Tex. Dec. 14, 2020) (applying Texas law); AFM Mattress Co. v. Motorists Com. Mut. Ins. Co., 2020 WL 6940984 (N.D. Ill. Nov. 25, 2020) (applying Illinois law); Boulevard Carroll Ent. Grp. v. Fireman's Fund Ins. Co., No. 20-11771 (SDW)(LDW), 2020 WL 7338081 (D.N.J. Dec. 14, 2020) (applying New Jersey law); Santo's Italian Café LLC v. Acuity Ins. Co., No. 1:20-cv-01192, 2020 WL 7490095 (N.D. Ohio) (applying Ohio law); 1210 McGavock St. Hosp. Partners, LLC v. Admiral Indem. Co., No. 3:20-cv-694, 2020 WL 7641184 (M.D. Tenn. Dec. 23, 2020) (applying Tennessee law); Boxed Foods Company, LLC v. Cal. Capital Ins. Co., No. 20-cv-04571-CRB, 2020 WL 6271021 (N.D. Cal. Oct. 27, 2020) (applying California law); LJ New Haven LLC v. AmGUARD Ins. Co., No. 3:20-cv-00751 (MPS), 2020 WL 7495622 (D. Conn. Dec. 21, 2020) (applying Connecticut law); Mortar & Pestle Corp. v. Atain Specialty Ins. Co., No. 20-cv-03461-MMC, 2020 WL 7495180 (N.D. Cal. Dec. 21, 2020) (applying California law).

held to oust coverage because courts have found that, even though some policyholders lost business income due to governmental orders closing or limiting access to their buildings, that access was lost because the governmental orders were issued due to a virus. In short, the courts link the causal chain back to the virus, an excluded cause. Courts summarily find no coverage in those cases where the virus exclusion has an anti-concurrent cause clause (and such a clause is permissible in that particular state).

We are not so certain the application of the virus exclusion to COVID-19-related cases is as straightforward as these court decisions suggest, especially those involving losses caused by governmental orders.[199] We are reminded of the similar path taken by courts first interpreting another seemingly impenetrable exclusion: the absolution pollution exclusion.[200] We might suggest that a more nuanced, contextual approach to the ISO virus exclusion is at least warranted, paying attention to drafting and underwriting history and what was meant in that 2006 ISO circular sent to insurance regulators. No court to date has examined what insurers actually meant to exclude in 2006 and how that plays out—or not—in the property insurance context of the 2019–2020 COVID pandemic. Keep in mind—the 2006 ISO virus exclusion was drafted in response to the SARS crisis, a very different disease scenario without the marked and intermittent governmental closures of the COVID-19 pandemic. It may be that, after such an analysis, the exclusion does exclude most if not all COVID-19-related business interruption losses. But we think it is at least intellectually honest to run the gauntlet with it, as was done with the absolute

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But see Elegant Massage, LLC v. State Farm Mut. Auto. Ins. Co., No. 2:20-cv-265, 2020 WL 72496234 (E.D. Va. Dec. 9, 2020) (applying Virginia law) (holding virus exclusion not applicable because cause of loss for massage spa is government closure order, not virus); Taps & Bourbon on Terrace, LLC v. Underwriters at Lloyds London, No. 20093025, 2020 WL 6380449 (Pa. Com. Pl. Oct. 26, 2020) (Trial Order) (refusing to dismiss case at pleadings stage, even though virus exclusion at issue).

[199] At least one court appears to have had the same concerns, although in a context where the complete insurance policy was not supplied to the court. In Urogynecology Specialist of Fla., LLC v. Sentinel Ins. Co., No. 6:20-cv-1174-Orl-22EJK, 2020 WL 5939172 (M.D. Fla. Sept. 24, 2020) (applying Florida law), the court allowed the policyholder's case to proceed, despite the presence of a virus exclusion, because the court surmised that COVID-19 may be different than other "virus"-type claims and perhaps it may be inappropriate to lump it in with other environmental pollutants like fungi, bacteria, or dry rot.

[200] *See* Jeffrey W. Stempel, *Reason and Pollution: Correctly Construing the "Absolute" Pollution Exclusion in Context and in Accord with Its Purpose and Party Expectations*, 34 TORT & INS. L.J. 1 (1998); Jeffery W. Stempel, *Unreason in Action: A Case Study of the Wrong Approach to Construing the Liability Insurance Pollution Exclusion*, 50 FLA. L. REV. 463 (1998).

pollution exclusion before it (recall that exclusion was eventually found wanting, and certainly did not merit as broad an application as insurers enjoyed in the early years of the exclusion).

However, incredibly, a number of courts have dismissed cases at the pleadings stage because of a cursory read of the virus exclusion and, in so doing, also denied specific policyholder requests for discovery about the ISO virus exclusion and its genesis.[201] After raising what appear to be reasonable queries about what the ISO circular was meant to do, policyholders are apparently faced with a door slammed shut about further factual discovery on the issue. Still other courts have preferred instead to offer—without the assistance of any evidence or context beyond pleadings—their own guesses as to what the boundaries of the exclusion surely must be.[202]

Most noteworthy perhaps is this question: if a policy does not include a virus exclusion, must that then be taken to mean that it covers virus-related losses?[203] Such virus exclusion language has been available since 2006, in direct response to the SARS pandemic. If an insurer has not specifically excluded viruses as a cause of loss, then pandemic-related losses resulting from virus contamination or civil authority orders attempting to quell virus spread would appear to be within the concept of covered losses (as long as the policyholder can prove there was a "direct physical loss of or damage to" covered property).

A. CASES WITHOUT A VIRUS EXCLUSION

In those cases without a virus exclusion, courts did not outright dismiss the policyholder's claim and instead at least inquired about the potential for "physical loss or damage." Unlike the policyholders in *Studio 417*, the policyholder in *Mudpie, Inc. v. Travelers Casualty Insurance Company. of America*[204] did not allege the virus

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[201] *See, e.g*., Mortar & Pestle Corp. v. Atain Specialty Ins. Co., No. 20-cv-03461-MMC, 2020 WL 7495180 (N.D. Cal. Dec. 21, 2020) (applying California law) (denying restaurant policyholder leave to discover genesis of ISO form and circular); Boxed Foods Co. v. Cal. Capital Ins. Co., No. 20-cv-04571-CRB, 2020 WL 6271021 (US Dist. Ct., N.D. Cal.) (applying California law) (denying discovery request about ISO circular and virus exclusion genesis on dismissal).

[202] *See, e.g.*, LJ New Haven LLC v. AmGUARD Ins. Co., No. 3:20-cv-00751 (MPS), 2020 WL 7495622 (D. Conn. Dec. 21, 2020) (applying Connecticut law) (citing ISO circular policyholder submits that exclusion likely limited to "on contact" or "on surface" contamination only; court disagrees and chastises policyholder for importing what is not in the policy (despite clause being an exclusion!)).

[203] *See* French, *supra* note 4.

[204] 2020 WL 5525171 (applying California law).

entered the property. Its business interruption claim rested solely on the governmental "stay at home" order in effect. Thus, the policyholder's putative class action was dismissed. The court held that the lead plaintiff policyholder, a children's clothing store, did not lose its property nor did it have that property damaged by the virus.

The court took a broad view of "direct physical loss of or damage to" property, in that it would consider loss of functionality as triggering coverage without requiring physical alteration of the property. However, to qualify for coverage, a policyholder would have to prove some intervening physical force made the premises uninhabitable or unusable (as was the case in *Gregory Packaging* with the ammonia).

The court did not accept that loss of property functionality or access due to governmental orders equated to "direct physical loss;" the policyholder could go back to its property after the "stay at home" order ended. Loss of use was thus held to be not a direct physical loss in this instance. The court distinguished this claim, based solely on the governmental order causing a loss of use, from that in *Studio 417* where the claimants had alleged actual physical virus microbes damaged the inside of their premises, rendering it unusable.

The court also denied coverage under the civil authority provisions of the store's policy because it found no causal link between any damage to adjacent property and the subsequent denial of access to the store. Because the "stay at home" orders were preventative, and did not involve actual physical damage, there was no causation between the policyholder's business losses and the government closure order.

The policyholder restaurant in *Malaube, LLC v. Greenwich Insurance Company*[205] alleged that Miami's order to close all restaurants to indoor dining (and thus permit only takeout and delivery) as a result of COVID-19, plus the Florida governor's statewide executive order closing all dining on-site restaurants, both resulted in prohibited access to its restaurants and thereby interrupted its business income. The policyholder argued that the full use of its property was limited by the government orders. The case did not survive a motion to dismiss.

The court cited *Mama Jo's, Inc*. and *Source Foods* and held that, under Florida law, an actual, tangible change in insured property must accompany a claim for coverage for "direct physical loss of or damage to" insured property. It distinguished the *Studio 417* case because, in that case, the policyholders alleged the actual presence of virus microbes on the property. The only allegations of loss in *Malaube* involve losses arising from the two Florida emergency orders. Because

[205] No. 20-22615-CIV, 2020 WL 5051581 (S.D. Fla. Aug. 26, 2020) (applying Florida law).

there was no physical intrusion of the property that resulted in an actual physical change to the property, under the *Mama Jo's/Source Foods* line of authority, the court held there was no potential for coverage and the claim was dismissed.

A similar result was reached in *Rose's 1 LLC v. Erie Insurance Exchange*,[206] on a motion for summary judgment in the Superior Court of the District of Columbia. Some DC restaurants were seeking business interruption coverage based on the DC mayor's order that closed all non-essential businesses (which included the restaurants) and told residents to stay inside except for essential reasons. The court held that there were no cases in this jurisdiction where a government edict, standing alone, is considered a direct physical loss, thereby triggering coverage, unless there was some physical damage to property. The court relied on *Brothers., Inc. v. Liberty Mutual Fire Insurance Company*,[207] a case where coverage was denied after a curfew was imposed in DC following riots after Martin Luther King's assassination. The curfew was held to be preventative in nature, and not a result of any physical damage to property. In fact, the point of the curfew was to prevent physical damage to property, so coverage could not possibly be triggered, according to the court.

The San Diego barbershop policyholder in *Pappy's Barber Shops, Inc. v. Farmers Group, Inc.*[208] had its claims for business interruption and civil authority coverage dismissed. The policyholder alleged that the local order banning non-essential gatherings plus then the state-wide "stay at home" order resulted in direct physical loss of or damage to their insured property. The policyholder argued that the precautionary measures taken by the government were the cause of the loss, not the actual presence of virus on any physical surface. The court held that the governmental orders did not prohibit access to the policyholder's place of business and the orders were not issued due to direct physical loss of or damage to either the policyholder's property or other property. Because there were no allegations of what the court considered were direct physical loss or damage, the claim was dismissed.

The overarching pattern is that cases without a virus exclusion at least prompt the courts to grapple with whether or not coverage is to be had for "direct physical loss of or damage to property." Nearly all cases which did not feature a virus exclusion have denied coverage if the policyholder did not allege actual physical loss on the premises.[209] And of course most right-thinking policyholders

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[206] 2020 WL 4589206 (D.C. Super. Ct. Aug. 6, 2020).

[207] 268 A.2d 611 (D.C. 1970).

[208] No. 20-CV-907-CAB-BLM, 2020 WL 5500221 (S.D. Cal. Sept. 11, 2020) (applying California law).

[209] *See, e.g.*, Infinity Exhibits, Inc. v. Certain Underwriters at Lloyd's London, No. 8:20-cv-1605-T-30AEP, 2020 WL 5791583 (M.D. Fla. Sept. 28, 2020) (applying Florida law) (relying on Mama Jo's court requires actual physical damage for coverage; case dismissed

could not allege such loss because to do otherwise would bring the claim squarely within the virus exclusion. So, the common route taken by policyholders—if unsuccessful to date—has been to argue that the governmental orders closing or limiting property access are the cause of the business interruption loss, and not the virus.

B. CASES WITH A VIRUS EXCLUSION

As stated, insurers have been successful in having those cases that featured a virus exclusion dismissed by courts. In probably the earliest claim focusing on pandemic-related losses, a Michigan state court granted the insurer's motion to dismiss the policyholder's claim for business interruption losses in *Gavrilides Management Company v. Michigan Insurance Company*[210] The policyholder in that case owned two restaurants and alleged that it lost revenue due to COVID-19 related closure orders and restrictions. The court held that, because the restaurants only alleged loss of use of their facilities, and not physical loss or damage, the restaurants did not suffer any covered loss. The virus exclusion in the policy operated to oust coverage regardless of whether there had been direct physical loss or damage to property.

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as no facts plead to show physical property damage); Uncork & Create LLC v. Cincinnati Ins. Co., No. 2:20-cv-00401, 2020 WL 6436948 (S.D.W. Va. Nov. 2, 2020) (applying West Virginia law) (distinguishing Studio 417 as there was alleged virus contamination in that case; however, court goes on to state that even if virus was present, coverage would likely not attach as premises can be cleaned); Oral Surgeons, PC v. The Cincinnati Ins. Co., No. 2-20-CV-222-CRW-SBJ, 2020 WL 5820552 (S.D. Iowa Sept. 29, 2020) (applying Iowa law) (finding no allegations of direct physical loss); Promotional Headwear Int'l v. Cincinnati Ins. Co., No. 20-cv-2211-JAR-GEB, 2020 WL 7078735 (D. Kan. Dec. 3, 2020) (applying Kansas law) (declining to accept allegations that virus contaminated property court cites to Source Food and Mama Jo's to require physical alteration); Water Sports Kauai, Inc. v. Fireman's Fund Ins. Co., No. 20-cv-03750-WHO, 2020 WL 6562332 (N.D. Cal Nov. 9, 2020) (applying Hawai'ian law) (distinguishing Studio 417 and Mudpie, where actual threats of contamination were alleged, court finds no actual exposure at stores in this case); Terry Black's Barbecue, LLC v. State Auto. Mut. Ins. Co., No. 1:20-CV-665-RP, 2020 WL 7351246 (W.D. Tex. Dec. 14, 2020) (applying Texas law) (finding no allegations of virus on property; assuming virus there, it does not cause physical loss and can be cleaned); S. Fla. ENT Assocs, Inc. v. Hartford Fire Ins. Co., No. 20-23677-Civ-WILLIAMS/TORRES, 2020 WL 6864560 (S.D. Fla. Nov. 13, 2020) (applying Florida law) (finding no allegations of virus presence); Kirsch v. Aspen Am. Ins. Co., No. 20-11930, 2020 WL 7338570 (E.D. Mich. Dec. 14, 2020) (applying Michigan law) (finding no allegations of virus on property).

[210] No. 20-000258-CB (Mich. Cir. Ct., Ingham Cty. July 1, 2020).

In *Diesel Barbershop LLC v. State Farm Lloyds*,[211] a U.S. District Court in the Western District of Texas dismissed the policyholder barbershop's claims for pandemic-related losses. The policy featured a fungi, virus or bacteria exclusion, which had an anti-concurrent cause clause:

> 1. We do not insure under any coverage for any loss which would not have occurred in the absence of one or more of the following excluded events. We do not insure for such loss regardless of:
>
> (a) the cause of the excluded event; or
>
> (b) other causes of the loss; or
>
> (c) whether other causes acted concurrently or in any sequence with the excluded event to produce the loss; or
>
> (d) whether the event occurs suddenly or gradually, involves isolated or widespread damage, arises from natural or external forces, or occurs as a result of any combination of these:
>
> **j. Fungi, Virus Or Bacteria**
>
> . . .
>
> (2) Virus, bacteria or other microorganism that induces or is capable of inducing physical distress, illness or disease.

The policyholder sought business interruption coverage for COVID-related losses due to the state and county orders restricting access to, or closing altogether of, non-essential businesses. The court preferred the line of cases requiring a direct tangible injury in order to trigger property coverage for a "direct physical loss." It held that Texas law would mandate there be a tangible injury for coverage to be triggered. The policyholder did not allege that the virus was physically on its property and caused tangible harm. Rather, it alleged that the cause of its loss was the governmental orders restricting access to its properties. This was not sufficient to create the potential for coverage as no direct physical loss or damage was alleged, according to the court.

Regardless as to the issue of direct physical loss, the court found that the virus exclusion and its anti-concurrent cause clause would prohibit both business interruption and civil authority coverage for the policyholder. The underlying root cause of the alleged losses was the virus—an excluded cause—according to the court because the virus was the reason for the orders to be issued by the state and county in the first instance.

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[211] No. 5:20-CV-461-DAE, 2020 WL 4724305, at *5 (W.D. Tex. Aug. 13, 2020) (applying Texas law).

The key to the court's reasoning in *Diesel Barbershop* was the view that the virus exclusion negated any possibility for coverage for COVID-19 related losses. The court also preferred to interpret "direct physical loss" as requiring not only a tangible injury to the property in question but a physical injury of sufficient magnitude that the property had been permanently structurally altered—an injury not alleged by the policyholder in that case.

A similar result to *Diesel Barbershop* was reached in *Turek Enterprises, Inc. v. State Farm Mutual Automobile Insurance Company*[212] in a motion to dismiss heard in the U.S. District Court for the Eastern District of Michigan. In that case, a chiropractic clinic's claim for business interruption coverage was dismissed. The clinic claimed for losses due to its inability to access its property as a result of governmental "stay at home" orders. Like *Diesel Barbershop*, the property policy in *Turek* had a similar virus exclusion with an anti-concurrent cause clause. The policyholder clinic specifically argued that COVID-19 virus particles did not attach to or damage any property (presumably to get around the virus exclusion). The court found that this case was similar to the *Source Food* case, in that there was no contamination of the insured property and therefore no possibility of coverage.

The court in *Turek* distinguished *Studio 417* and preferred the reasoning of *Diesel Barbershop* and *Gavrilides Management Company LLC v. Michigan Insurance Company*[213] in holding that Michigan law required a tangible injury to property to trigger the "direct physical loss or damage" coverage clause. The court did not accept the policyholder's argument that COVID-19 was not the proximate cause of the loss and the virus exclusion was only limited in its applicability to the costs of decontamination. Instead, the court held that the governmental orders preventing property access were not the sole cause of the policyholder's loss—the virus was also a cause, thus triggering the anti-concurrent cause portion of the virus exclusion. The court made this holding despite the policyholder raising the fact that the 2006 ISO virus exclusion circular submitted to insurance regulators indicated that the exclusion was meant to preclude losses due to contamination by disease-causing agents.

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[212] No. 20-11655, 2020 WL 5258484 (E.D. Mich. Sept. 3, 2020) (applying Michigan law).

[213] No. 20-000258-CB (Mich. Cir. Ct., Ingham Cty. July 1, 2020) (holding that, when a city order prevented customers from dining in the restaurant, it did not suffer a direct physical loss because there was no physical alteration or tangible damage to the integrity of the building).

Similarly, in *10E, LLC v. Travelers Indemnity Company of Connecticut*,[214] a restaurant in downtown Los Angeles had its claim for business interruption and civil authority-related losses dismissed on motion after it alleged that the Los Angeles Mayor's public health restrictions prohibiting in-person dining at restaurants resulted in lost income. The insurance policy in this case had an exclusion for losses due to virus and bacteria.[215]

The court held that there was no direct physical loss or damage triggering coverage as nothing physically changed in the property. Under California law, the court held that losses from inability to use property do not amount to "direct physical loss of or damage to property." A distinct, demonstrable physical alteration to the property is required for coverage to attach. Furthermore, the court held that temporary impairment to property does not equate to direct physical loss. The policyholder's civil authority claim was dismissed because the virus exclusion ousted coverage for COVID-19 related losses. The government-ordered dining restrictions were entirely attributable to the virus, an excluded cause. Additionally, the court found that no particular adjacent property was damaged so the civil authority coverage could not be triggered in the first place.

The court in *Martinez v. Allied Insurance Company of America*[216] dismissed a dental office's claim for business interruption insurance because the policy contained a virus exclusion.[217] The policyholder claimed that the COVID-19 virus and Florida's emergency shutdown orders, including orders limiting non-essential dental procedures, caused the interruption of its income stream. It also alleged damages due to decontamination of its office. The court dismissed the claim solely on the language of the virus exclusion by holding that all of the office's losses were related to the virus, an excluded cause of loss. This is, in fact, the predominant pattern of courts faced with the virus exclusion when deciding pandemic-related coverage issues: a knee-jerk dismissal.

In perhaps the most shocking example of all, the United States District Court for the Western District of Missouri in *Zwillo v. Corporation. v. Lexington Insurance*

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[214] No. 2:20-cv-04418-SVW-AS, 2020 WL 5359653 (C.D. Cal. Sept 2, 2020) (applying California law).

[215] *Id.* at *1 (noting that the policy reads, "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.").

[216] No. 2:20-cv-00401-FtM-66NPM, 2020 WL 5240218 (M.D. Fla. Sept. 2, 2020) (applying Florida law).

[217] *Id.* at *3 (noting that the exclusion was for loss or damage caused "directly or indirectly," by "[a]ny virus, bacterium or other microorganism that induces or is capable of inducing physical distress, illness or disease.").

Company[218] dismissed a policyholder's claim based on an extremely broadly worded pollution exclusion which included the word "virus" in a long list of possible pollutant contaminants. The court distinguished the *Studio 417*, *KC Hopps*, and *Blue Springs Dental* cases—cases in its own district!—on the basis that the word "virus" was here in an all-encompassing pollution exclusion and not a stand-alone "virus" exclusion. The court did not accept the policyholder's arguments that this pollution exclusion was obviously aimed at environmental or industrial pollution, not pandemic-related losses.

Where cases to date have ruled in favor of an insurer based on knee-jerk embrace of a faulty concept of direct physical loss or injury, the courts may nonetheless have blundered toward the right result in some situations involving the virus exclusion—if insurers win the causation battle. We think that is a big "if" but realize courts may decide to the contrary. If that becomes the majority rule, observers will tend to minimize the significance of judicial decisions construing the physical loss or injury trigger, at least where there is a virus exclusion. Notwithstanding this, we remain critical of the "no direct physical loss or damage" decisions even if they can be defended on the "no harm, no foul" grounds of a more persuasive basis such as the virus exclusion.

But it is far from clear how many policies at issue actually contain a virus exclusion or how that exclusion operates in all loss scenarios. Insurers have promoted the view that nearly all policies contain the exclusion but a quarter of the case law to date involves policies with no such exclusion. Consequently, better juridical reasoning regarding loss and damage may make thousands of policies and millions of dollars in coverage available to policyholders.

VI. CONCLUSION

Insurers have won the bulk of the early COVID coverage battles, with analysis in too many of these early decisions that mangles fundamental insurance policy interpretation doctrine. Fortunately, there is a cluster of better reasoned cases that one hopes will be persuasive to the appellate courts that will ultimately determine the outcome of the COVID coverage war.

The insurance industry's media thrust at the early stages of the COVID pandemic which pushed the no-coverage-for-COVID message appeared to set the stage for the early salvo of claim dismissals from courts across the country. Whether due to media influence or simple subpar analysis, many court decisions fall short in that they have, in varying degrees:

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[218] No. 4:20-00339-CV-RK, 2020 WL 7137110 (W.D. Mo. Dec. 2, 2020) (applying Missouri law).

a) ignored or wrongfully rejected state law precedents regarding the "direct physical loss or damage" coverage trigger;
b) read pro-insurer precedents too broadly, failing to distinguish the ubiquity, reach, and impact of COVID as compared to the more distant and non-physical loss of these precedents;
c) ignored or summarily distinguished similarly analogous cases of insurance coverage for contaminating substances, precedents which would have provided helpful guidance on the insurance coverage issue for COVID-related losses;
d) artificially distinguished insurance policy wording from the wording in past precedents when, in fact, the relevant policy wording is identical to the cases at hand;
e) provided no reasoning as to why one line of coverage cases is preferred over another;
f) fallen into a hyper-literalist dictionary-based argument which cherry-picks only certain dictionary definitions and ignores others which run counter to the conclusions reached;
g) refused to even consider insurance policy term ambiguity in the wake of conflicting dictionary definitions and case precedents, thereby failing to invoke the policyholder-friendly tools of insurance policy interpretation: *contra proferentem* and reasonable expectations;
h) refused to read pleading allegations at face value and as presumptively true, as required at the motion to dismiss stage of litigation; and,
i) dispensed with policyholder claims without any further factual findings or discovery, at the pleadings stage, in a context where factual knowledge of the COVID-19 virus is evolving on a near-daily basis, and where allegations should be enough to get the policyholder in the door of the litigation system.

In response to this list, insurers would certainly argue that the presence of a virus exclusion in the cases on which they have prevailed validates dismissal[219] even

[219] And, as reflected in the tally of decisions to date, courts are receptive to this insurer argument. *See* Baker, *supra* note 10; Erin Ayers, *Insurers Prevail in Two More COVID-19-related BI Lawsuits*, ADVISEN, (last visited Jan. 25, 2020) https://www.advisen.com/tools/fpnproc/fpns/articles_new_1/P/376369872.html?rid=376369872&list_id=1 (discussing Tracker findings); Mike Curley, *Travelers Ducks Counterclaims*

if judicial analysis of the loss or damage questions has been unduly abrupt and reductionist. We reject a "no harm, no foul" justification because there is harm when courts warp prevailing contract and insurance law in a rush to judgment.[220] In particular, the collapsing and narrowing of the concepts of directness, physicality, loss and damage sets unwise precedent sure to wrongfully deprive policyholders of coverage in future non-COVID cases. If the virus exclusion is conclusive, bully for insurers—but if that is the case, decisions should be made on the basis of this express exclusion rather than tortured reasoning about loss and damage.

The judiciary's excessively textual focus-cum-myopia also unnecessarily raises doubts about the correctness of the decisions. If it is fact correct that there cannot be loss or damage without structural change in tangible property or that the concept of damage requires a particularized showing of viral contamination of specific surfaces, one would expect supporting evidence in the drafting history of property policies or similar materials providing context and illuminating the policy purpose and coverage intent. But overconfident hermeneutics-lite decisions in favor of insurers deprive policyholders, the judicial system, and society of access to materials that can determine whether a court's reading of policy verbiage is correct.

Ironically, this type of background information might support the insurer position. The drafting history of the standard ISO virus exclusion, for example, does strongly suggest that insurers were seeking to avoid contamination liability, although the case against civil authority shutdown is less clear.[221] We understand that insurers, who think they can consistently win drafting wars, are reluctant to concede the usefulness of contextual materials and undermine future arguments seeking to restrict court consideration to only policy text. But the insurers' long term

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in Geragos COVID-19 Suit, LAW360, (last visited Jan. 25, 2020) https://www.law360.com/articles/1321151/travelers-ducks-counterclaims-in-geragos-covid-19-suit (California federal district court finds "a virus exclusion in [law firm] policy bars coverage.").

[220] In addition, it appears that many insurance policies lack a virus exclusion. *See* Baker, supra note 10 (last visited Oct. 21, 2020) (noting that in cases with decisions, one-fifth of policies lack virus exclusions); Josh Czaczkes, et. al., *Why We Don't Need COVID-19 Immunity Legislation,* BALKINIZATION (Sept. 26, 2020), https://balkin.blogspot.com/2020/09/why-we-dont-need-covid-19-immunity.html (noting that the majority of general liability insurance policies lack virus exclusion). In the rush to enact limitations on liability for COVID claims, state legislatures appear not to have investigated the prospect that such limitations on liability inure to the benefit of insurers rather than policyholders, at least in the short term. Insurers would presumably argue that in the absence of such legislation, they will be force to raise premiums or restrict coverage.

[221] *See* ISO VIRUS EXCLUSION, *supra* note 25.

agenda should not strangle immediate judicial decision-making. Courts interested in correctly deciding COVID coverage cases would presumably be interested in seeing this material rather than making it moot through a Rule 12 dismissal.

Apart from its possible (we think probable) infection of the judiciary, the insurance industry's public relations narrative is troubling. The insurance industry claims that COVID coverage is a death knell even though it also claims that nearly all policies provide only four weeks of civil authority coverage while all policies of course have policy limits and perhaps even other sub-limits on business interruption coverage or applicable exclusions as well as conditions that policyholders may fail to meet. In light of the liability limiting tools at their disposal, the insurer claims of imminent poverty if COVID is covered seems melodramatic.

The insurer claim of disaster rings particularly hollow in light of the European experience more receptive to coverage. While insurer profitability may have declined for the moment, the insurance industry remains alive and well in both the E.U.[222] and the U.K., where a key test case went well for policyholders.[223] And in the U.S., insurers appear to be doing just fine in spite of—or in some cases because of—the pandemic.[224]

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[222] *See Munich Re Reports €800M of COVID-19-Related Losses During Q3*, INS. J. (Oct. 21, 2020), https://www.insurancejournal.com/news/international/2020/10/21/587446.htm. Although 800 million euros is of course a good deal of money, it is not the hundreds of billions of dollars American insurers claim they will lose (allegedly each month) if COVID business interruption claims must be paid. The Munich Re experience thus suggests that policy limits, sub-limits, and specific exclusions give carriers substantial economic protection eve if their defenses of no-direct-physical-loss-or-damage are rejected by courts.

[223] *See* Carolyn Cohn & Kirstin Ridley, *London Court Rules Some Insurers Should Not Have Denied Business Interruption Claims*, INS. J. (Sept. 15, 2020), https://www.insurancejournal.com/news/international/2020/09/15/582641.htm (describing Financial Conduct Authority v. Arch Insurance (UK) Ltd, [2021] UKSC 1.

[224] *See* Leslie Scism & Allison Prang, *Travelers More Than Doubles Quarterly Income*, WALL ST. J. (Oct. 20, 2020), https://www.wsj.com/articles/travelers-profit-rose-in-third-quarter-11603192181 (noting Traveler's $827 million third quarter profit compared to $396 million in 2019, which included $400 million in subrogation revenue from claims against Pacific Gas & Electric in connection with California fires; and how Travelers stock rose by $3.12 per share). Travelers was also aided in that its auto insurance business did better than usual because of pandemic-stimulated reductions in driving and hence in collisions. We realize that property insurance is expected to have a less successful 2020 than auto or liability insurance but note that insurers have multiple means of enduring difficult times and profiting over the proverbial long-haul, where their longevity records is considerably better than that of their small business policyholders.

Meanwhile, business policyholders appear to be experiencing the type of debacle insurers claim they face if coverage claims succeed. Insurers seem to sing this tune with ease when threatened. We have heard it before regarding asbestos, pollution, product liability, bad faith, and punitive damages claims. But even the massive asbestos mega-tort, Superfund, and other pollution claims—not to mention the credit swap defaults of the Great Recession—did minimal long-lasting damage to insurers and their ability to accumulate capital and regain profitability. In times of such stress, many more policyholders than insurers fail.

Although insurer claims of industry-wide doom tend to ring hollow, their means of survival is not without collateral consequence. The asbestos, pollution, and Superfund coverage wars produced broad exclusions in standard policies and made coverage more expensive and difficult (but not impossible) to obtain. COVID-19 will surely spur restrictions of coverage and increases in premiums—but this is likely even if insurers prevail in today's coverage battles.

The immediately relevant question is whether today's policyholders seeking coverage under policies issued prior to the pandemic—particularly those lacking a virus exclusion—are entitled to coverage. Too many initial decisions on the issue have implicitly embraced a flawed insurer narrative in abruptly turning policyholders away.

ADDENDUM 5

DOCKET NO. X07-HHD-CV-21-6142969-S : SUPERIOR COURT

NEW CASTLE HOTELS, LLC : COMPLEX LITIGATION DOCKET

V. : AT HARTFORD

ZURICH AMERICAN INSURANCE COMPANY : SEPTEMBER 7, 2021

Memorandum of Decision
Partially Granting Motion to Strike

1. With the exception of its Louisiana property, cost due to a virus is excluded from New Castle's property insurance coverage.

New Castle Hotels, LLC owns a number of lodgings. The COVID-19 Pandemic throttled them. New Castle has come to court because it wants its insurer, Zurich American Insurance Company, to pay for these losses.

New Castle certainly had property insurance on these locations through Zurich. But every part of every policy excluded any cost incurred due to a virus. Or rather, every policy but one. Louisiana law wouldn't allow the exclusion, so most of what follows here does not apply to the Louisiana property at issue.

As for the rest, the policy language unambiguously excludes costs caused by viruses and those are the only costs at issue here.

New Castle admits that the policy excludes any cost due to "contamination". It admits that contamination is defined to include "any condition of property due to the actual presence of any . . . virus." It pleads the actual presence of the virus on its properties.

New Castle tries to escape these plain words by claiming a kind of guilt-by-association. New Castle says that *other* things included in the definition of "contamination" make the term so broad that it should be reinterpreted by the court to be an environmental pollution exclusion. New Castle claims the words around the word "virus", viewed together, are aimed at damage caused from the property rather than to the property. It declares that isn't claiming any losses due to the release of the virus from the New Castle property into the environment. Therefore, New Castle claims the exclusion doesn't apply or is at least ambiguous enough to prevent Zurich from winning at this stage.

Apparently, New Castle has drawn hope for this view from our Appellate Court's 2018 decision in *R.T. Vanderbilt Company, Inc. v. Hartford Accident and Indemnity Company*.[1] But New Castle can't use the genuine dilemma the court faced there to create a false dilemma for the court here. *Vanderbilt* involved an insurer's attempt to use a contamination exclusion to defeat a claim for coverage of indoor asbestos contamination. Unlike the policy here, the policy in *Vanderbilt* had no explicit exclusion for costs due to asbestos contamination.

Instead, the insurer in *Vanderbilt* tried to claim that general exclusions for "smoke, vapors, soot, fumes, acids, alkalis, toxic chemicals, liquids or gases, waste materials or other irritants, contaminants or pollutants into or upon land, the atmosphere or any watercourse or body of water" included interior contamination by asbestos.

It should come as no surprise that the *Vanderbilt* Court didn't find interior asbestos contamination to unambiguously be "irritants, contaminants, or pollutants into or upon land, the atmosphere or any watercourse or body of water." This language can easily be

[1] 171 Conn. App. 61.

seen as pointing to the exterior environment. That was decisive in *Vanderbilt*.[2] The breadth of the undefined words "irritant" and "contaminant" was only the Court's fifth ground in support of its view.[3]

And this hardly matters here. None of the language at issue points to contamination of the exterior environment. Why should it? The policy in *Vanderbilt* was an outward-looking liability policy. The policy here is an inward-looking property policy.

That's why the Zurich policy addresses only the "property", not its surroundings. Even more important, while the *Vanderbilt* Court was considering whether an unnamed toxic substance—asbestos—was included among a broad list of exclusions, we are faced here with an explicitly named substance—a virus—that is defined as part of the exclusion for contaminants. And unlike the list in *Vanderbilt*, this list doesn't list viruses among "other pollutants". Instead, it lists them as separate exclusions: i.e., virus...pollutant, etc. This means that New Castle really shouldn't see them as a single species of exclusions based upon reading the policy as a whole and the words in context. That policy and those words make viruses and pollutants distinct from each other.

And to the extent New Castle claims that the virus didn't cause its losses, government orders did, this claim can be easily disposed of on the face of the complaint. The complaint alleges that the virus caused the government to issue orders constraining its business. It doesn't allege some other cause of the government orders. Accordingly, New Castle cannot defend against this motion to strike by contradicting its own allegation about the origin of its woes. The virus is at the root of its allegations. And cost due to virus is excluded.

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[2] Id., 221-28.
[3] Id., 231.

Likewise, New Castle pleading in the alternative imminent rather actual harm from the virus gains it nothing. Imminent harm from something explicitly excluded is just as excluded as actual harm from the thing excluded. Costs incurred because of an imminent harm by a virus are still costs incurred because of a virus and viruses are excluded.

The straight-forward exclusion means that, with the exception of the Louisiana coverage, the court can make its decision from the face of the complaint. It doesn't have to consider evidence outside of the four corners of the policy. That's because it has viewed all the relevant parts of the policy, seen how they work together as a whole, and concluded that the policy language was unambiguous. Specifically, this review led the court to conclude that the virus exclusion doubtless applies. There is no other rational way to read the language.

As our Supreme Court held in *R.T. Vanderbilt Co., Inc. v. Hartford Accident & Indemnity Co.*, plain language like this means the court may interpret the policy coverage as a pure matter of law.[4] Indeed the policy language at issue is in the complaint. Therefore, as our Supreme Court held in 1962 in *Redmond v. Matthies*, the court is free to render its definitive interpretation of the policy language in a ruling on a motion to strike. [5]

The court will enforce this unambiguous virus exclusion everywhere it applies.

2. With respect to its Louisiana claims, New Castle has adequately alleged physical loss or damage.

And that brings us to Louisiana. The parties agree that the exclusion at issue does not apply in Louisiana. So, about the New Castle property in that state, the battle must be

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[4] 333 Conn. 343, 364-65.
[5] 149 Conn. 423, 426-27.

fought on different ground.

Every type of coverage under the policy—for clean-up, lost business, etc.—is tied to "direct physical loss of" or "direct physical damage to" property. But Zurich claims that there is nothing "physical" about the losses or damage flowing from the COVID-19 virus. Zurich notes that some courts in other jurisdictions have addressed this issue—remarkably even at the pleading stage—remarkably with little apparent deliberation. Yes. Zurich can cite decisions where courts, agree with it. Some of them merely note that claimants haven't even alleged physical damage using the words "physical". Others go further. The virus damages lungs not property, they say.

But can this merely be asserted to become true? Maybe this kind of result is the product of an expansive view of "plausibility" under the pleading standard adopted by the United States Supreme Court in *Bell Atlantic Corp. v. Twombly.*[6] But Connecticut's standard prefers a ruling from the evidence rather than the gut. Practice Book §10-1 only requires a party to plead "a plain and concise statement of the material facts on which the pleader relies."

New Castle has done this. Beginning at paragraph 32 of the complaint it alleges that the virus "is a cause of real physical loss or of damage to property". It goes on to cite government and private sources to allege that the virus is extremely damaging to humans and can lie in wait for them by lingering for many hours on the surface of physical property—including for up three days on the plastic and stainless steel surfaces found in New Castle properties. It further alleges that the physical dimensions of affected physical pieces of its property can be microscopically damaged and changed by the virus. It warns

[6] 550 U.S. 544, 556 (2007).

of the possibility that a contaminated property can become a super-spreader viral incubator as the virus jumps from person to property to another person and back.

These are the very things Zurich says aren't true. But of course who is right is a matter of evidence, and whatever the federal standard, Practice Book §10-1 specifically says that pleadings are to contain fact allegations and that they must not contain evidence.

Still, Zurich believes it's so clearly right that it asks the court to take judicial notice that the COVID-19 virus does not physically alter objects. Indeed, it claims this is as plain as it is that the moon isn't made of green cheese.

But to get judicial notice that the virus makes no physical change to physical objects, Zurich would first have to demonstrate to the court that it is generally known that the COVID-19 virus does not degrade the molecules making up a physical object and that this is readily verifiable. And it has not done so. Pointing to scientifically unsupported conclusions from other courts isn't enough. This court has nothing in front of it that establishes these two points as a matter of unquestioned science.

We do know a lot about viruses—but this one? We are learning something new every day. The court simply can't take notice at this stage that the virus does not degrade physical objects on at least a microscopic level. That question will have to wait for another day—on summary judgment perhaps or after trial. What matters for now is that physical damage is specifically alleged here.

And there is a second problem with Zurich's argument. Why must we assume that a physical object isn't damaged unless its molecules are somehow rearranged or degraded? Most people think of mold infestation as damage. Sometimes it can be wiped off. But it is also generally accepted that when mold grows on carpet, insulation, ceiling tiles, drywall or wallboard, these things must be removed and replaced regardless whether they are

molecularly intact.[7] It's obvious that mold can cause a lot of damage without breaking or burning, snapping or scratching, gauging or goring.

Isn't property damaged when vandals paint graffiti over it? Would an insurer say—"the wall is still standing, no physical damage here"? Mythology tells us that Atlantis submerged to the bottom of the sea intact. Is a building under hundreds of feet of water not physically damaged? Was there no physical damage to the buildings in Pompeii in 79 A.D. after Vesuvius erupted? After all many of those buildings were perfectly intact—indeed, they were perfectly usable—they just happened to be buried under twenty feet of ash.

The rush to judgment on the question of physical damage in some courts—without reasoning and without evidence—has been ill advised. For now, in this court, and for this policy, it would be wrong to rush. We know New Castle has stated at length that its property was physically damaged. In another motion on another day or at trial the court will have to consider evidence about the character and compass of the harm alleged here before rendering its judgment. But not today.

Consequently, for New Castle's Louisiana property the complaint will stand. It contains adequate fact allegations that—if true— support a claim under the Zurich policy for physical loss or damage. As our Supreme Court held in 2010 in *Lestorti v. DeLeo*, the court must assume for now that these well-pleaded facts are true. And so it will. And so Zurich's motion to strike the complaint as to Louisiana is denied.[8] To the same extent and for the same reasons, the allegations of breach of the covenant of good faith and fair dealing in count two will also not be stricken.

Count I and II remain as to New Castle's Louisiana property. As to all other properties,

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[7] *See, e.g., https://www.cdc.gov/mold/faqs.htm.*
[8] 298 Conn. 466, 472.

the two counts are stricken because the claims about them are barred by a virus exclusion.

BY THE COURT

434447

Moukawsher, J.

ADDENDUM 6

IN THE COURT OF COMMON PLEAS OF ALLEGHENY COUNTY, PENNSYLVANIA

MACMILES, LLC D/B/A GRANT STREET TAVERN 310 Grant Street, Ste. 106 Pittsburgh, PA 15219-2213,	:	
Plaintiff,	:	No.: GD-20-7753
vs.	:	Hon. Christine Ward
ERIE INSURANCE EXCHANGE 100 Erie Insurance Place Erie, PA 16530,	:	**Memorandum and Order of Court**
Defendant.	:	

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IN THE COURT OF COMMON PLEAS OF ALLEGHENY COUNTY, PENNSYLVANIA

MACMILES, LLC D/B/A GRANT STREET TAVERN 310 Grant Street, Ste. 106 Pittsburgh, PA 15219-2213,	:	
Plaintiff,	:	No.: GD-20-7753
vs.	:	
ERIE INSURANCE EXCHANGE 100 Erie Insurance Place Erie, PA 16530,	:	
Defendant.	:	

MEMORANDUM AND ORDER OF COURT

I. The Parties

MacMiles, LLC d/b/a Grant Street Tavern (hereinafter "Plaintiff") is a restaurant and bar located in the Downtown neighborhood of Pittsburgh, Allegheny County, Pennsylvania.

Erie Insurance Exchange (hereinafter "Defendant") is a reciprocal insurance exchange organized under the laws of Pennsylvania with its principal place of business in Erie, Pennsylvania.

II. Introduction

Defendant issued Plaintiff an Ultra Plus Commercial General Liability Policy for the policy period between September 12, 2019 to September 12, 2020 (hereinafter "the insurance contract"). The insurance contract is an all-risk policy, which provides coverage for any direct physical loss or direct physical damage unless the loss or damage is specifically excluded or limited by the insurance contract.

In March and April of 2020, in order to prevent and mitigate the spread of the coronavirus disease "COVID-19," Governor Tom Wolf ("Governor Wolf") issued a series of mandates restricting the operations of certain types of businesses throughout the Commonwealth of Pennsylvania (the "Governor's orders"). On March 6, 2020, Governor Wolf issued an order declaring a Proclamation of Disaster Emergency. On March 19, 2020, Governor Wolf issued an order requiring all non-life sustaining businesses in Pennsylvania to cease operations and close physical locations. On March 23, 2020, Governor Wolf issued an order directing Pennsylvania citizens in particular counties to stay at home except as needed to access life sustaining services. Then, on April 1, 2020, Governor Wolf extended the March 23, 2020 order, and directed all of Pennsylvania's citizens to stay at home. As of April 1, 2020, at least 5,805 citizens of Pennsylvania contracted COVID-19 in sixty counties across the Commonwealth, and seventy-four (74) citizens died.[1] Unfortunately, since April 1, 2020, the number of positive cases and deaths from COVID-19 has increased dramatically.[2]

As a result of the spread of COVID-19 and the Governor's orders, Plaintiff suspended its business operations. Plaintiff thereafter submitted a claim for coverage under its insurance contract with Defendant. Defendant denied Plaintiff's claim.

On September 29, 2020, Plaintiff filed a complaint in the Court of Common Pleas of Allegheny County. In its complaint, Plaintiff asserted the following counts: [a] count one is for declaratory judgment in regards to the business income protection provision of the insurance contract; [b] count two is for breach of contract in relation to the business income protection

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[1] *See* Governor Tom Wolf, *Order of the Governor of the Commonwealth of Pennsylvania for Individuals to Stay at Home*, (April 1, 2020), https://www.governor.pa.gov/wp-content/uploads/2020/04/20200401-GOV-Statewide-Stay-at-Home-Order.pdf.

[2] As of May 14, 2021, 993,915 citizens of Pennsylvania have contracted COVID-19 and 26,724 citizens have died. *See* Pennsylvania Department of Health, COVID-19 Data for Pennsylvania, https://www.health.pa.gov/topics/disease/coronavirus/Pages/Cases.aspx.

provision of the insurance contract; [c] count three is for declaratory judgment with regard the civil authority provision of the insurance contract; [d] count four is for breach of contract in regards to the civil authority provision of the insurance contract; [e] count five is for declaratory judgment with regard to the extra expense provision of the insurance contract; and [f] count six is for breach of contract in regards to the extra expense provision of the insurance contract. All of Plaintiff's claims require this Court's determination as to whether Plaintiff is entitled to coverage under various provisions of the insurance contract with Defendant for losses Plaintiff sustained in relation to the spread of COVID-19 and the Governor's orders.

On December 22, 2020, Plaintiff filed a Motion for Partial Summary Judgment as to Plaintiff's claims for declaratory judgment with regard to the business income protection and civil authority provisions of the insurance contract. On March 10, 2021, Defendant filed a Cross Motion for Judgment on the Pleadings. On March 31, 2021, this Court heard oral argument on Plaintiff's Motion for Partial Summary Judgment and Defendant's Cross Motion for Judgment on the Pleadings. For the reasons set forth herein, this Court grants Plaintiff's Motion for Partial Summary Judgment, in part, and denies Defendant's Cross Motion for Judgment on the Pleadings.

III. The Contract Provisions

Plaintiff's and Defendant's dispute involves the following provisions regarding coverage under the insurance contract.

> **Section 1 - Coverages**
>
> **Insuring Agreement**
>
> We will pay for direct physical "loss" of or damage to Covered Property at the premises described in the "Declarations" caused by or resulting from a peril insured against.

Omnibus Memorandum in Support of Erie's Cross-Motion for Judgment on the Pleadings and in Opposition to Plaintiff's Motion for Summary Judgment, at 61, Exhibit A.

> **Section II – Perils Insured Against**
>
> * * * * *
>
> **Income Protection – Coverage 3**
>
> **Covered Cause of Loss**
>
> This policy insures against direct physical "loss", except "loss" as excluded or limited in this policy.[3]

Id. at 64.

> **Income Protection – Coverage 3**
>
> **A. Income Protection**
>
> Income Protection means loss of "income" and/or "rental income" you sustain due to partial or total "interruption of business" resulting directly from "loss" or damage to property on the premises described in the "Declarations" or to your food truck or trailer when anywhere in the coverage territory from a peril insured against.[4]

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[3] "Loss" means direct and accidental loss of or damage to covered property. Omnibus Memorandum in Support of Erie's Cross-Motion for Judgment on the Pleadings and in Opposition to Plaintiff's Motion for Summary Judgment, at 96, Exhibit A.

[4] The insurance contract defines "interruption of business" as "the period of time that your business is partially or totally suspended and it: 1. Begins with the date of direct "loss" to covered property caused by a peril insured against: and 2. Ends on the date when the covered property should be repaired, rebuilt, or replaced with reasonable speed and similar quality." Omnibus Memorandum in Support of Erie's Cross-Motion for Judgment on the Pleadings and in Opposition to Plaintiff's Motion for Summary Judgment, at 96, Exhibit A. The insurance contract defines "income" as "the sum of net income (net profit or loss before income taxes) that would have been earned or incurred and necessary continuing operating expenses incurred by the business such as payroll expenses, taxes, interest, and rents." *Id*. The insurance contract defines "rental income" as the following:

> 1. The rents from the tenant occupancy of the premises described in the "Declarations";
>
> 2. Continuing operating expenses incurred by the business such as:
>
> a. Payroll; and
>
> b. All expenses for which the tenant is legally responsible and for which you would otherwise be responsible;
>
> 3. Rental value of the property described in the "Declarations" and occupied by you; or

Id. at 63.

C. Additional Coverages

1. Civil Authority

When a peril insured against causes damage to property other than property at the premises described in the : Declarations", we will pay for the actual loss of "income" and/or "rental income" you sustain and necessary "extra expense" caused by action of civil authority that prohibits access to the premises described in the "Declarations" or access to your food truck or trailer anywhere in the coverage territory provided that both of the following apply:

a. Access to the area immediately surrounding the damaged property is prohibited by civil authority as a result of the damage, and the premises described in the "Declarations" or your food truck or trailer are within that area but are not more than one mile from the damaged property; and

b. The action of civil authority is taken in response to dangerous physical conditions resulting from the damage or continuation of the peril insured against that caused the damage, or the action is taken to enable a civil authority to have unimpeded access to the damaged property.

Id. at 64.

Section III. Exclusions

A. Coverages 1, 2, and 3

We do not cover under Building(s) – Coverage 1; Business Personal Property and Personal Property of others – Coverage 2; and Income Protection – Coverage 3 "loss" or damaged caused directly or indirectly by any of the following. Such a "loss" or damage is excluded regardless of any cause or event that contributes concurrently or in any sequence to the "loss":

* * * * *

10. By the enforcement of or compliance with any law or ordinance regulating the construction, use, or repair of any property, or requiring the tearing down of any

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4. Incidental income received from coin-operated laundries, hall rentals, or other facilities on the premises described in the "Declarations".

Id. at 97. Finally, "Declarations" is defined as "the form which shows your coverages, limits of protection, premium charges, and other information." *Id*. at 96.

property, including the cost of removing its debris, except as provided in Extensions of Coverage – **B.3., B.7.,** and **B.8.**

Id. at 66.

IV. Standard of Review

It is well-settled that, after the relevant pleadings are closed, a party may move for summary judgment, in whole or in part, as a matter of law. Pa. R.C.P. 1035.2. Summary judgment "may be entered only where the record demonstrates that there are no genuine issues of material fact, and it is apparent that the moving party is entitled to judgment as a matter of law." *City of Philadelphia v. Cumberland County Bd. of Assessment Appeals*, 81 A.3d 24, 44 (Pa. 2013). Furthermore, appellate courts will only reverse a trial court's order granting summary judgment where it is "established that the court committed an error of law or abused its discretion." *Siciliano v. Mueller*, 149 A.3d 863, 864 (Pa. Super. 2016).

The interpretation of an insurance contract is a matter of law, which may be decided by this Court on summary judgment. *Wagner. V. Erie Insurance Company*, 801 A.2d 1226, 1231 (Pa. Super. 2002). When interpreting an insurance contract, this Court aims to effectuate the intent of the parties as manifested by the language of the written instrument. *American and Foreign Insurance Company v. Jerry's Sport Center*, 2 A.3d 526, 540 (Pa. 2010). When reviewing the language of the contract, words of common usage are read with their ordinary meaning, and this Court may utilize dictionary definitions to inform its understanding. *Wagner*, 801 A.2d at 1231; *see also AAA Mid-Atlantic Insurance Company v. Ryan*, 84 A.3d 626, 633-34 (Pa. 2014). If the terms of the contract are clear, this Court must give effect to the language. *Madison Construction Company v. Harleysville Mutual Insurance Company*, 735 A.2d 100, 106 (Pa. 1999). However, if the contractual terms are subject to more than one reasonable interpretation, this Court must find that the contract is ambiguous. *Id*. "[W]hen a provision of

a[n insurance contract] is ambiguous, the [contract] provision is to be construed in favor of the [the insured] and against the insurer, as the insurer drafted the policy and selected the language which was used therein." *Kurach v. Truck Insurance Exchange*, 235 A.3d 1106, 1116 (Pa. 2020).

V. Discussion

a. Coverage Provisions

Plaintiff bears the initial burden to reasonably demonstrate that a claim falls within the policy's coverage provisions. *State Farm Cas. Co. v. Estates of Mehlman*, 589 F.3d 105, 111 (3d Cir. 2009) (applying Pennsylvania law). Then, provided that Plaintiff satisfies its initial burden, Defendant bears "the burden of proving the applicability of any exclusions or limitations on coverage." *Koppers Co. v. Aetna Cas. & Sur. Co.*, 98 F.3d 1440, 1446 (3d Cir. 1996) (applying Pennsylvania law). In order to prevail, Defendant must demonstrate that the language of the insurance contract regarding exclusions is "clear and unambiguous: otherwise, the provision will be construed in favor of the insured." *Fayette County Housing Authority v. Housing and Redevelopment Ins. Exchange*, 771 A.2d 11, 13 (Pa. Super. 2001).

First, this Court will address whether Plaintiff is entitled to coverage under the Income Protection provision of the insurance contract for losses Plaintiff sustained in relation to the public health crises and the spread of the COVID-19 virus. With regard to Income Protection coverage, the insurance contract provides that:

> **Section 1 - Coverages**
>
> **Insuring Agreement**
>
> We will pay for *direct physical "loss" of or damage to* Covered Property at the premises described in the "Declarations" caused by or resulting from a peril insured against.

Omnibus Memorandum in Support of Erie's Cross-Motion for Judgment on the Pleadings and in Opposition to Plaintiff's Motion for Summary Judgment, at 61, Exhibit A (emphasis added).

> **Section II – Perils Insured Against**
>
> * * * * *
>
> **Income Protection – Coverage 3**
>
> **Covered Cause of Loss**
>
> This policy insures against direct physical "loss", except "loss" as excluded or limited in this policy.[5]

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> **Income Protection – Coverage 3**
>
> **A. Income Protection**
>
> Income Protection means loss of "income" and/or "rental income" you sustain due to partial or total "interruption of business" resulting *directly from "loss" or damage to property* on the premises described in the "Declarations" or to your food truck or trailer when anywhere in the coverage territory from a peril insured against.[6]

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[5] "Loss" means direct and accidental loss of or damage to covered property. Omnibus Memorandum in Support of Erie's Cross-Motion for Judgment on the Pleadings and in Opposition to Plaintiff's Motion for Summary Judgment, at 96, Exhibit A.

[6] The insurance contract defines "interruption of business" as "the period of time that your business is partially or totally suspended and it: 1. Begins with the date of direct "loss" to covered property caused by a peril insured against: and 2. Ends on the date when the covered property should be repaired, rebuilt, or replaced with reasonable speed and similar quality." Omnibus Memorandum in Support of Erie's Cross-Motion for Judgment on the Pleadings and in Opposition to Plaintiff's Motion for Summary Judgment, at 96, Exhibit A. The insurance contract defines "income" as "the sum of net income (net profit or loss before income taxes) that would have been earned or incurred and necessary continuing operating expenses incurred by the business such as payroll expenses, taxes, interest, and rents." *Id*. The insurance contract defines "rental income" as the following:

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>
> 2. Continuing operating expenses incurred by the business such as:
>
> a. Payroll; and
>
> b. All expenses for which the tenant is legally responsible and for which you would otherwise be responsible;
>
> 3. Rental value of the property described in the "Declarations" and occupied by you; or

Id. at 63 (emphasis added).

In order to state a reasonable claim for coverage under the Income Protection provision of the insurance contract, Plaintiff must show that it suffered "direct physical loss of or damage to" its property. The interpretation of the phrase "direct physical loss of or damage to" property is the key point of the parties' dispute. Defendant contends that "direct physical loss of or damage to" property requires some physical altercation of or demonstrable harm to Plaintiff's property. Plaintiff contends that the "direct physical loss of . . . property" is not limited to physical altercation of or damage to Plaintiff's property but includes the loss of use of Plaintiff's property. Plaintiff further asserts that, because its interpretation is reasonable, this Court must find in Plaintiff's favor.

The insurance contract does not define every term in the phrase "direct physical loss of or damage to" property.[7] As previously noted, Pennsylvania courts construe words of common usage in their "natural, plain, and ordinary sense . . . and [Pennsylvania courts] may inform [their] understanding of these terms by considering their dictionary definitions." *Madison Construction Company,* 735 A.2d at 108. Four words in particular are germane to the determination of this threshold issue: "direct," "physical," "loss," and "damage." "Direct" is

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4. Incidental income received from coin-operated laundries, hall rentals, or other facilities on the premises described in the "Declarations".

Id. at 97. Finally, "Declarations" is defined as "the form which shows your coverages, limits of protection, premium charges, and other information." *Id*. at 96.

[7] Although the insurance contract does define the term "loss" as meaning "direct and accidental loss of or damage to covered property," this definition is essentially meaningless because it is repetitive of the phrase "direct physical loss of or damage to." Omnibus Memorandum in Support of Erie's Cross-Motion for Judgment on the Pleadings and in Opposition to Plaintiff's Motion for Summary Judgment, at 96, Exhibit A. Accordingly, when interpreting the term "loss," this Court relies upon the term's the ordinary dictionary definition as it does with the other terms in this phrase, which the insurance contract did not define.

defined as "proceeding from one point to another in time or space without deviation or interruption . . . [and/or] characterized by close logical, causal, or consequential relationship . . ."[8] "Physical" is defined as "of or relating to natural science . . . having a material existence . . . [and/or] perceptible especially through the senses and subject to the laws of nature . . . ."[9] "Loss" is defined as "DESTRUCTION, RUIN . . . [and/or] the act of losing possession [and/or] DEPRIVATION . . . ."[10] "Damage" is defined as "loss or harm resulting from injury to person, property, or reputation . . . ."[11]

Before analyzing the definitions of each of the above terms to determine whether Plaintiff's interpretation is reasonable, it is important to note that the terms, in addition to their ordinary, dictionary definitions, must be considered in the context of the insurance contract and the specific facts of this case. *See Madison Construction Company,* 735 A.2d at 106 (clarifying that issues of contract interpretation are not resolved in a vacuum). While some courts have interpreted "direct physical loss of or damage to" property as requiring some form of physical altercation and/or harm to property in order for the insured to be entitled to coverage, this Court reasonably determined that any such interpretation improperly conflates "direct physical loss of" with "direct physical . . . damage to" and ignores the fact that these two phrases are separated in the contract by the disjunctive "or."[12] It is axiomatic that courts must "not treat the words in the

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[8] Direct, Merriam-Webster, https://www.merriam-webster.com/dictionary/direct.

[9] Physical, Merriam-Webster, https://www.merriam-webster.com/dictionary/physical.

[10] Loss, Merriam-Webster, https://www.merriam-webster.com/dictionary/loss.

[11] Damage, Merriam Webster, https://www.merriam-webster.com/dictionary/damage.

[12] *See Fayette County Housing Authority v. Housing and Redevelopment Ins. Exchange*, 771 A.2d 11, 15 (Pa. Super. 2001) (explaining that merely accepting the non-binding decisions of other courts "by the purely mechanical process of searching the nations courts for conflicting decisions" amounts to an abdication of this Court's judicial role).

[contract] as mere surplusage . . . [and] if at all possible, [this Court must] construe the [contract] in a manner that gives effect to all of the [contract's] language." *Indalex Inc. v. Nation Union Fire Ins. Co. Pittsburgh, PA*, 83 A.3d 418, 420-21 (Pa. Super. 2013). Based upon this vital principle of contract interpretation, this Court concluded that, due to the presence of the disjunctive "or," whatever "direct physical 'loss' of" means, it must mean something different than "direct physical . . . damage to."

In order to determine what the phrase "direct physical loss of . . . property" reasonably means, this Court looked to the ordinary, dictionary definitions of the terms "direct," "physical," "loss," and "damage." This Court began its analysis with the terms "damage" and "loss," as these terms are the crux of the disputed language. As noted above, "damage" is defined as "loss or harm resulting from injury to person, property, or reputation . . . ,"[13] and "loss" is defined as "DESTRUCTION, RUIN . . . [and/or] the act of losing possession [and/or] DEPRIVATION . . . ."[14]

Based upon the above-provided definitions, it is clear that "damage" and "loss," in certain contexts, tend to overlap. This is evident because the definition of "damage" includes the term "loss," and at least one definition of "loss" includes the terms "destruction" and "ruin," both of which indicate some form of damage. However, as noted above, in the context of this insurance contract, the concepts of "loss" and "damage" are separated by the disjunctive "or," and, therefore, the terms must mean something different from each other. Accordingly, in this instance, the most reasonable definition of "loss" is one that focuses on the act of losing possession and/or deprivation of property instead of one that encompasses various forms of

[13] Damage, Merriam Webster, https://www.merriam-webster.com/dictionary/damage.

[14] Loss, Merriam-Webster, https://www.merriam-webster.com/dictionary/loss.

damage to property, i.e., destruction and ruin. Applying this definition gives the term "loss" meaning that is different from the term "damage." Specifically, whereas the meaning of the term "damage" encompasses all forms of harm to Plaintiff's property (complete or partial), this Court concluded that the meaning of the term "loss" reasonably encompasses the act of losing possession [and/or] deprivation, which includes the loss of use of property absent any harm to property.

In reaching its conclusion, this Court also considered the meaning and impact of the terms "direct" and "physical." Ultimately, this Court determined that the ordinary, dictionary definitions of the terms "direct" and "physical" are consistent with the above interpretation of the term "loss." As noted previously, "direct" is defined as "proceeding from one point to another in time or space without deviation or interruption . . . [and/or] characterized by close logical, causal, or consequential relationship . . . ,"[15] and "physical" is defined as "of or relating to natural science . . . having a material existence . . . [and/or] perceptible especially through the senses and subject to the laws of nature . . . ."[16] Based upon these definitions it is certainly reasonable to conclude that Plaintiff could suffer "direct" and "physical" loss of use of its property absent any harm to property.

Here, Plaintiff's loss of use of its property was both "direct" and "physical." The spread of COVID-19, and a desired limitation of the same, had a close logical, causal, and/or consequential relationship to the ways in which Plaintiff materially utilized its property and physical space. *See* February 22, 2021 Court Order of the United States District Court, N.D. Illinois, Eastern Division case *In re: Society Insurance Co. COVID-19 Business Interruption*

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[15] Direct, Merriam-Webster, https://www.merriam-webster.com/dictionary/direct.

[16] Physical, Merriam-Webster, https://www.merriam-webster.com/dictionary/physical.

Protection Insurance Litigation, Civil Case No. 1:20-CV-05965 at 21 (stating that government shutdown orders and COVID-19 *directly* impacted the way businesses used *physical* space) (emphasis added). Indeed, the spread of COVID-19 and social distancing measures (with or without the Governor's orders) caused Plaintiff, and many other businesses, to *physically* limit the use of property and the number of people that could inhabit *physical* buildings at any given time, if at all. Thus, the spread of COVID-19 did not, as Defendant contends, merely impose economic limitations. Any economic losses were secondary to the businesses' *physical* losses.

While the terms "direct" and "physical" modify the terms "loss" and "damage," this does not somehow necessarily mean that the entire phrase "direct physical loss of or damage to" property requires actual harm to Plaintiff's property in every instance. Any argument that the terms "direct" and "physical," when combined, presuppose that any request for coverage must stem from some actual impact and harm to Plaintiff's property suffers from the same flaw noted in this Court's above discussion regarding the difference between the terms "loss" and "damage:" such interpretations fail to give effect to all of the insurance contract's terms and, again, render the phrase "direct physical loss of" duplicative of the phrase "direct physical . . . damage to."

Defendant also contends that the insurance contract's Amount of Insurance provision supports the conclusion that the contract necessitates the existence of tangible damage in order for Plaintiff to be entitled to Income Protection coverage. According to Defendant, because the Amount of Insurance provision contemplates the existence of damaged or destroyed property, and the need to rebuild, repair, or replace property, Plaintiff's argument regarding loss of use in the absence of any tangible damage or destruction to property is untenable.

Although this Court agrees with Defendant on the general principle that the insurance contract's provisions must be read as a whole so that all of its parts fit together, this Court is not persuaded that the Amount of Insurance provision is inherently inconsistent with an interpretation of "direct physical loss of . . . property" that encompasses Plaintiff's loss of use of its property in the absence of tangible damage. The insurance contract provides that:

> We will pay the actual income protection loss for only such length of time as would be required to resume normal business operations. We will limit the time period to the shorter of the following periods:
>
> 1. The time period required to rebuild, repair, or replace such part of the Building or Building Personal Property that has been damaged or destroyed as a direct result of an insured peril; or
>
> 2. Twelve (12) consecutive months from the date of loss.

Omnibus Memorandum in Support of Erie's Cross-Motion for Judgment on the Pleadings and in Opposition to Plaintiff's Motion for Summary Judgment, at 64, Exhibit A. Upon review of the above language, this Court determined that the Amount of Insurance provision does not limit coverage only to instances where Plaintiff needed to rebuild, repair, or replace damaged or destroyed property. Indeed, the relevant part of the Amount of Insurance provision starts by generally stating that the insurer will pay for income protection loss for only such length of time as would be required to resume normal business operations. Thereafter, the Amount of Insurance provision further explains that this time period for coverage will be limited to either (a) the length of time needed to rebuild, repair, or replace damaged or destroyed property; *or* (b) twelve (12) months from the initial date of loss.

Although Defendant is correct to point out that the Amount of Insurance provision expressly contemplates some circumstances in which Plaintiff's property is actually damaged or destroyed, this provision does not necessitate the existence of damaged or destroyed property,

and does not require repairs, rebuilding, or replacement of damaged or destroyed property in order for Plaintiff to be entitled to coverage. The Amount of Insurance provision merely imposes a time limit on available coverage, which ends whenever any required rebuilding, repairs, or replacements are completed to any damaged or destroyed property that might exist, *or* twelve (12) months after the initial date of the loss. To put this another way, the Amount of Insurance provision provides that coverage ends when Plaintiff's business is once again operating at normal capacity after damaged or destroyed property is fixed or replaced, *or* within twelve (12) months from the initial date of loss in circumstances where it is not necessary to fix or replace damaged or destroyed property, or it is not feasible to do so within a twelve (12) month time frame. The Amount of Insurance provision does not somehow redefine or place further substantive limits on types of available coverage.

As this Court determined that it is, at the very least, reasonable to interpret the phrase "direct physical loss of . . . property" to encompass the loss of use of Plaintiff's property due to the spread of COVID-19 absent any actual damage to property, and because Plaintiff established that there are no genuine issues of material fact regarding its right to coverage under the Income Protection provision of the insurance contract, this Court grants Plaintiff's Motion for Partial Summary Judgment in relation to Plaintiff's claim for declaratory judgment and the income protection provision of the insurance contract.

Second, this Court will address whether Plaintiff is entitled to coverage under the Civil Authority provision of the insurance contract for losses Plaintiff sustained in relation to the Governor's orders, which were issued to help mitigate the spread of the COVID-19 virus. With regard to Civil Authority coverage, the insurance contract provides that:

> When a peril insured against causes damage to property other than property at the premises described in the : Declarations", we will pay for the actual loss of

> "income" and/or "rental income" you sustain and necessary "extra expense" caused by action of civil authority that prohibits access to the premises described in the "Declarations" or access to your food truck or trailer anywhere in the coverage territory provided that both of the following apply:
>
> a. Access to the area immediately surrounding the damaged property is prohibited by civil authority as a result of the damage, and the premises described in the "Declarations" or your food truck or trailer are within that area but are not more than one mile from the damaged property; and
>
> b. The action of civil authority is taken in response to dangerous physical conditions resulting from the damage or continuation of the peril insured against that caused the damage, or the action is taken to enable a civil authority to have unimpeded access to the damaged property.

Id. at 64.

With regard to Civil Authority coverage, Plaintiff must, as a threshold matter, demonstrate that COVID-19 caused damage to property other than Plaintiff's property. Unlike the Income Protection provision, under the Civil Authority provision there is no coverage for the loss of use of property other than Plaintiff's property. Accordingly, this Court's above analysis with regard Income Protection coverage and loss of use is inapplicable, as it does not address whether COVID-19 separately caused damage to property.

Again, as noted above, "damage" is defined as "loss or harm resulting from injury to person, property, or reputation . . . ."[17] Based upon this definition, this Court determined that, at the very least, in order for COVID-19 to damage property, COVID-19 must come into contact with property and cause harm. Presently, it is contested whether COVID-19 can live on the surfaces of property for some period of time. Additionally, while this might be one way by which individuals contract COVID-19, it is not the primary means by which COVID-19 spreads. *See Friends of Danny DeVito v. Wolf*, 227 A.3d 872, 892 (Pa. 2020) (holding that COVID-19

[17] Damage, Merriam Webster, https://www.merriam-webster.com/dictionary/damage.

does not spread because the virus is present on any particular surface or at any particular location, rather COVID-19 spreads because of person-to-person contact). Indeed, person-to-person transmission of COVID-19, as opposed to property damage, was the primary reason for the Governor's orders, social distancing measures, and resultant changes in the ways business utilized property. With or without COVID-19 contacting the surface of any given property in the Commonwealth, businesses throughout the Commonwealth shutdown, at least partially, and suffered the loss of use of property due to the risk of person-to-person COVID-19 transmission. Thus, in the above discussion regarding the Income Protection provision, this Court determined that there are no genuine issues of material fact as to whether Plaintiff suffered the loss use of property due to COVID-19. The same is, however, not as clear with regard to the question of whether COVID-19 caused damaged to property throughout the Commonwealth.

Even if this Court were to accept that COVID-19 could and did cause damage to property under the theory presented by Plaintiff, whether Plaintiff is entitled to coverage under the Civil Authority provision depends upon whether Plaintiff can demonstrate that COVID-19 was actually present on property other than Plaintiff's property. Additionally, Plaintiff must show that any such damaged property was within one mile of Plaintiff's property, and that the actions of civil authority (in this case the Governor's orders) were "taken in response to dangerous physical conditions resulting from the *damage* or continuation of the peril insured against that caused the *damage*, or the action is taken to enable a civil authority to have unimpeded access to the *damaged* property." Omnibus Memorandum in Support of Erie's Cross-Motion for Judgment on the Pleadings and in Opposition to Plaintiff's Motion for Summary Judgment, at 64, Exhibit A (emphasis added). At this time, genuine issues of material fact remain in dispute as to the following: [a] whether COVID-19 caused damage to property; [b] whether COVID-19

was actually present at any particular property; and [c] the extent to which the Governor's orders were issued in response to property damaged by COVID-19. Accordingly, this Court denies Plaintiff's Motion for Partial Summary Judgment in relation to its claim for declaratory judgment and the Civil Authority provision of the insurance contract without prejudice.[18]

b. Exclusions

Having determined that Plaintiff provided a reasonable interpretation demonstrating that Plaintiff is entitled to coverage under the Income Protection provision of the insurance contract, this Court turns to the question of whether Defendant demonstrated "the applicability of any exclusions or limitations on coverage." *Koppers Co.*, 98 F.3d at 1446 (applying Pennsylvania law). As discussed previously, in order to prevail, Defendant must show that the language of the insurance contract regarding an exclusion is "clear and unambiguous: otherwise, the provision will be construed in favor of the insured." *Fayette County Housing Authority*, 771 A.2d at 13.

Defendant argues that the insurance contract's exclusion regarding the enforcement of or compliance with laws and ordinances prevents coverage for income protection. The insurance contract states that the insurer will not pay for loss or damage caused "[b]y the enforcement of or compliance with any law or ordinance regulating the construction, use, or repair, of any property, or requiring the tearing down of any property, including the cost of removing its debris . . . ." Omnibus Memorandum in Support of Erie's Cross-Motion for Judgment on the Pleadings and in Opposition to Plaintiff's Motion for Summary Judgment, at 66, Exhibit A.

According to Defendant, coverage is precluded by the above exclusion because Plaintiff's alleged losses are due solely to the Governor's orders. This, however, is not the case. In its complaint, Plaintiff states that its claim for coverage is based upon losses and expenses Plaintiff

[18] As this Court is not convinced that, as a matter of law, Plaintiff cannot prevail on its damage theory, this Court also denies Defendant's Cross Motion for Judgment on the Pleadings.

suffered in relation to both "*the COVID-19 pandemic* . . . and the orders of civil authorities enacted in response to this natural disaster." Plaintiff's Complaint at 13 (emphasis added). As this Court explained earlier in this memorandum, COVID-19 and the related social distancing measures (with and without government orders) directly forced businesses everywhere to physically limit the use of property and the number of people that could inhabit physical buildings at any given time. The Governor's orders only came into consideration in the context of Plaintiff's claim for coverage under the Civil Authority provision of the contract.[19] Accordingly, Defendant failed to demonstrate that the exclusion regarding the enforcement of or compliance with laws and ordinances clearly and unambiguously prevents coverage.

VI. Conclusion

As this Court determined that [a] Plaintiff's interpretation of the Income Protection provision of the insurance contract is, at the very least, reasonable, [b] that there are no genuine issues of material fact regarding Plaintiff's loss of use, and [c] that none of the insurance contract's exclusions clearly and unambiguously prevent coverage, Plaintiff's Motion for Partial Summary Judgment as to Plaintiff's claim for declaratory judgment with regard to Income Protection coverage is GRANTED. In contrast, because this Court determined that there are genuine issues of material fact remaining as to the Civil Authority provision and whether COVID-19 caused damage to property, Plaintiff's Motion for Partial Summary Judgment as to Plaintiff's claim for declaratory judgment with regard to Civil Authority coverage is DENIED

[19] Certainly, the exclusion regarding the enforcement of or compliance with laws and ordinances could not have been intended to exclude coverage under the Civil Authority provision of the contract, as this would make any extended coverage for the actions of Civil Authority illusory. *See Heller v. Pennsylvania League of Cities and Municipalities*, 32 A.3d 1213, 1228 (Pa. 2011) (holding that where an exclusionary provision of an insurance contract operates to foreclose expected claims, such a provision is void as it renders coverage illusory).

without prejudice. Finally, Defendant's Cross Motion for Judgement on the Pleadings is DENIED.

By the Court:

Christine Ward, J.

Christine Ward, J.

Dated: 5/25/2021

IN THE COURT OF COMMON PLEAS OF ALLEGHENY COUNTY, PENNSYLVANIA

MACMILES, LLC D/B/A GRANT STREET TAVERN 310 Grant Street, Ste. 106 Pittsburgh, PA 15219-2213,	:	
Plaintiff,	:	No.: GD-20-7753
vs.	:	
ERIE INSURANCE EXCHANGE 100 Erie Insurance Place Erie, PA 16530,	:	
Defendant.	:	

ORDER OF COURT

And now, this 25 day of May, 2021 it is hereby ORDERED, ADJUDGED, and DECREED that:

1. Plaintiff's Motion for Partial Summary Judgment as to Plaintiff's claim for declaratory judgment with regard Income Protection coverage is GRANTED;
2. Plaintiff's Motion for Partial Summary Judgment as to Plaintiff's claim for declaratory judgment with regard to Civil Authority coverage is DENIED without prejudice; and
3. Defendant's Cross Motion for Judgement on the Pleadings is DENIED.

By the Court:

Christine Ward, J.

Christine Ward, J.

Dated: 5/25/2021

ADDENDUM 7

IN THE COURT OF COMMON PLEAS OF ALLEGHENY COUNTY, PENNSYLVANIA

TIMOTHY A. UNGAREAN, DMD d/b/a SMILE SAVERS DENTISTRY, PC, INDIVIDUALLY AND ON BEHALF OF A CLASS OF SIMILARLY SITUATED PERSONS,	:	CIVIL DIVISION
	:	No.: GD-20-006544
Plaintiff,	:	
v.	:	**Memorandum and Order of Court**
CNA and VALLEY FORGE INSURANCE COMPANY,	:	
Defendants.	:	

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IN THE COURT OF COMMON PLEAS OF ALLEGHENY COUNTY, PENNSYLVANIA

TIMOTHY A. UNGAREAN, DMD d/b/a SMILE SAVERS DENTISTRY, PC, INDIVIDUALLY AND ON BEHALF OF A CLASS OF SIMILARLY SITUATED PERSONS,	:	CIVIL DIVISION
	:	No.: GD-20-006544
Plaintiff,	:	
v.	:	**Memorandum and Order of Court**
CNA and VALLEY FORGE INSURANCE COMPANY,	:	
Defendants.	:	

MEMORANDUM AND ORDER OF COURT

I. The Parties

Timothy A. Ungarean, DMD, d/b/a Smile Savers Dentistry, PC is a dentist who owns and operates a dental practice with places of business located at 4701 Baptist Road, Pittsburgh, Allegheny County, Pennsylvania, 15227 and 3153 Brodhead Road, Suite A, Aliquippa, Beaver County, Pennsylvania, 15001. Timothy A. Ungarean, DMD, is hereinafter referred to as "Ungarean" or "Plaintiff."

CNA is a property and casualty insurance company with a principal place of business at 151 North Franklin Street, Floor 9, Chicago, Illinois 60606.[1] Valley Forge Insurance Company

[1] In their Cross Motions for Summary Judgment, both Valley Forge Insurance Company and CNA argue that CNA is not a proper party in this action. This Court disagrees. After Plaintiff filed its claim with Valley Forge Insurance Company, Plaintiff received a letter that Plaintiff is not entitled to coverage. Plaintiff's Complaint at 174, Exhibit C. Importantly, the letter is written by a Mark Chancellor, who identifies himself as a Claims Representative with CNA. In the letter, Mark Chancellor speaks on behalf of Valley Forge Insurance Company and specifically states that "*[w]e* have evaluated the claim under a CNA Connect Policy issued to Timothy A Ungarean by VFIC . . . Policy No. 6025183026 (the "Policy")." *Id*. at 175, Exhibit C (emphasis added). Given that the initial denial letter came from a CNA Claims Representative, this Court determined that CNA is a proper party in this declaratory judgment action. *See Shared Communications Services of 1800-80 JFK Blvd. Inc. v. Bell Atlantic Properties Inc.*, 692 A.2d 570, 573 (Pa. Super. 1997) (holding that "courts will disregard the corporate entity only in the limited

is a wholly owned subsidiary company of CNA, and also provides property and casualty insurance. Both CNA and Valley Forge Insurance Company regularly and routinely conduct business in the Commonwealth of Pennsylvania. CNA and Valley Forge Insurance Company are hereinafter collectively referred to as "Defendants."

II. Introduction

In March and April of 2020, in order to prevent and mitigate the spread of the coronavirus disease "COVID-19," Governor Tom Wolf ("Governor Wolf") issued a series of mandates restricting the operations of certain types of businesses throughout the Commonwealth of Pennsylvania (the "Governor's orders"). On March 6, 2020, Governor Wolf issued an order declaring a Proclamation of Disaster Emergency. On March 19, 2020, Governor Wolf issued an order requiring all non-life sustaining businesses in Pennsylvania to cease operations and close physical locations. On March 23, 2020, Governor Wolf issued an order directing Pennsylvania citizens in particular counties to stay at home except as needed to access life sustaining services. Then, on April 1, 2020, Governor Wolf extended the March 23, 2020 order, and directed all of Pennsylvania's citizens to stay at home. As of April 1, 2020, at least 5,805 citizens of Pennsylvania contracted COVID-19 in sixty counties across the Commonwealth, and seventy-four (74) citizens died.[2] Unfortunately, since April 1, 2020, the number of positive cases and deaths from COVID-19 has increased dramatically.[3]

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circumstances when *used to defeat public convenience*, justify wrong, protect fraud or defend a crime") (emphasis added).

[2] *See* Governor Tom Wolf, *Order of the Governor of the Commonwealth of Pennsylvania for Individuals to Stay at Home*, (April 1, 2020), https://www.governor.pa.gov/wp-content/uploads/2020/04/20200401-GOV-Statewide-Stay-at-Home-Order.pdf.

[3] As of March 21, 2021, 843,135 citizens of Pennsylvania have contracted COVID-19 and 24,788 citizens have died. *See* Pennsylvania Department of Health, COVID-19 Data for Pennsylvania, https://www.health.pa.gov/topics/disease/coronavirus/Pages/Cases.aspx.

As a result of the spread of COVID-19 and the Governor's orders, Plaintiff shutdown the majority of its business operations. For a time, Plaintiff's dental practice remained open only to perform emergency dental procedures. Not surprisingly, Plaintiff subsequently experienced a dramatic decrease in business income and furloughed some of its employees. Plaintiff thereafter submitted a claim for coverage under its business insurance policy ("the insurance contract") with Defendants. Defendants denied Plaintiff's claim.

On June 5, 2020, Plaintiff filed a complaint in the Court of Common Pleas of Allegheny County. In its complaint, Plaintiff asserted one count for declaratory judgment, by which it seeks this Court's determination as to whether Plaintiff is entitled to coverage under the insurance contract with Defendants for losses Plaintiff sustained in relation to the spread of COVID-19 and the Governor's orders. On October 5, 2020, Plaintiff filed a Motion for Summary Judgment. On December 2 and December 4, 2020, Defendants filed Cross Motions for Summary Judgment. On January 20, 2020, this Court heard oral argument on Plaintiff's Motion for Summary Judgment and Defendants' Cross Motions for Summary Judgment. For the reasons set forth herein, this Court grants Plaintiff's Motion for Summary Judgment and denies Defendants' Cross Motions for Summary Judgment.

III. The Contract Provisions

Plaintiff's and Defendants' dispute involves the following provisions regarding coverage under the insurance contract.

Business Income

a. Business Income means:
    (1) Net Income (Net profit or Loss before Income taxes) that would have been earned or incurred, including:
        a. "Rental Value;" and
        b. "Maintenance Fees," if you are a condominium association; and

(2) Continuing normal operating expenses incurred, including payroll, subject to 90 day limitation if indicated on the Declaration page.

b. We will pay for the actual loss of Business Income you sustain 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 the described premises. The loss or damage must be caused by or result from a Covered Cause of Loss.[4]

Extra Expense

a. Extra Expense means reasonable and necessary expenses you incur during the "period of restoration" that you would not have incurred if there had been no direct physical loss of or damage to property caused by or resulting from a Covered Cause of Loss.

b. We will pay Extra Expense (other than the expense to repair or replace property) to:
   (1) Avoid or minimize the "suspension" of business and to continue "operations" at the described premises or at replacement premises or temporary locations, including relocation expenses and costs to equip and operate the replacement premises or temporary locations; or
   (2) Minimize the "suspension" of business if you cannot continue "operations."

c. We will also pay Extra Expense (including Expediting Expenses) to repair or replace the property, but only to the extent it reduces the amount of loss that otherwise would have been payable under Paragraph 1. Business Income above.

Plaintiff's Complaint, at 58-59, Exhibit B (emphasis added).

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[4] The insurance contract defines "suspension" as the "partial or complete cessation of your [the insured's] business activities; or . . . that a part or all of the described premises is rendered untenantable." Plaintiff's Complaint at 55. The insurance contract defines "operations" as "the type of your [the insured's] business activities occurring at the described premises and tenantability of the described premises." Plaintiff's Complaint at 53. The insurance contract defines "period of restoration" as:

> the period of time that: [b]egins with the date of direct physical loss or damage caused by or resulting from any Covered Cause of Loss at the described premises; and . . . [e]nds on the earlier of: (1) The date when the property at the described premises should be repaired, rebuilt or replaced with reasonable speed and similar quality; or (2) The date when business is resumed at a new permanent location.

Plaintiff's Complaint at 53. The insurance contract defines Covered Cause of Loss as "RISK OF DIRECT PHYSICAL LOSS unless the loss is: a. Excluded in Section B. Exclusions; b. Limited in paragraph A.4 Limitations; or c. Limited or Excluded by other provision of this Policy. Plaintiff's Complaint at 37.

Civil Authority

1. When the Declarations show that you have coverage for Business Income and Extra Expense, you may extend that insurance to apply to the actual loss of Business Income you sustain and reasonable and necessary Extra Expense you incur caused by an action of civil authority that prohibits access to the described premises. The civil authority action must be due to direct physical loss of or damage to property at locations, other than described premises, caused by or resulting from a Covered Cause of Loss.

Id. at 84 (emphasis added).

Plaintiff's and Defendants' dispute also involves the following provisions regarding exclusions from coverage under the insurance contract:

Exclusions

We will not pay for loss or damage caused directly or indirectly by any of the following. Such loss or damage is excluded regardless of any other cause or event that contributes concurrently or in any sequence to the loss.

Ordinance or Law

(1) The enforcement of any ordinance or law:
(a) Regulating the construction, use or repair of any property; or
(b) Requiring the tearing down of any property, including the cost of removing debris.

(2) This exclusion applies whether the loss results from:
(a) An ordinance or law that is enforced even if the property has not been damaged; or
(b) The increased costs incurred to comply with an ordinance or law in the course of construction, repair, renovation, remodeling or demolition or property, or removal of its debris, following a physical loss to that property.

Contamination

Contamination by other than "pollutants."[5]

[5] The insurance contract defines "pollutants" as "any solid, liquid, gaseous or thermal irritant or contaminant, including smoke, vapor, soot, fumes, acids, alkalis, chemicals, waste, and any unhealthful or hazardous building materials (including but not limited to asbestos and lead products or materials containing lead). Waste includes materials to be recycled, reconditioned or reclaimed." Plaintiff's Complaint at 54.

Consequential Loss

Delay, loss of use or loss of market.

Acts or Decisions

Acts or Decisions, including the failure to act or decide, of any person, group, organization or governmental body.

Id. at 38-42 (emphasis added).

Fungi, Wet Rot, Dry Rot and Microbes[6]

Id. at 118-19 (emphasis added).

IV. Standard of Review

It is well-settled that, after the relevant pleadings are closed, a party may move for summary judgment, in whole or in part, as a matter of law. Pa. R.C.P. 1035.2. Summary judgment "may be entered only where the record demonstrates that there are no genuine issues of material fact, and it is apparent that the moving party is entitled to judgment as a matter of law." *City of Philadelphia v. Cumberland County Bd. of Assessment Appeals*, 81 A.3d 24, 44 (Pa. 2013). Furthermore, appellate courts will only reverse a trial court's order granting summary judgment where it is "established that the court committed an error of law or abused its discretion." *Siciliano v. Mueller*, 149 A.3d 863, 864 (Pa. Super. 2016).

The interpretation of an insurance contract is a matter of law, which may be decided by this Court on summary judgment. *Wagner. V. Erie Insurance Company*, 801 A.2d 1226, 1231

[6] "Microbe(s)" is specifically defined in the following manner:

> "Microbe(s)" means any non-fungal micro-organism or non-fungal, colony-form organism that causes infection or disease. "Microbes" includes any spores, mycotoxins, odors, or any other substances, products, or by products produced by, or arising out of the current or past presence of "microbes."

Id. at 118-19 (emphasis added).

(Pa. Super. 2002). When interpreting an insurance contract, this Court aims to effectuate the intent of the parties as manifested by the language of the written instrument. *American and Foreign Insurance Company v. Jerry's Sport Center*, 2 A.3d 526, 540 (Pa. 2010). When reviewing the language of the contract, words of common usage are read with their ordinary meaning, and this Court may utilize dictionary definitions to inform its understanding. *Wagner*, 801 A.2d at 1231; *see also AAA Mid-Atlantic Insurance Company v. Ryan*, 84 A.3d 626, 633-34 (Pa. 2014). If the terms of the contract are clear, this Court must give effect to the language. *Madison Construction Company v. Harleysville Mutual Insurance Company*, 735 A.2d 100, 106 (Pa. 1999). However, if the contractual terms are subject to more than one reasonable interpretation, this Court must find that the contract is ambiguous. *Id*. "[W]hen a provision of a[n insurance contract] is ambiguous, the [contract] provision is to be construed in favor of the [the insured] and against the insurer, as the insurer drafted the policy and selected the language which was used therein." *Kurach v. Truck Insurance Exchange*, 235 A.3d 1106, 1116 (Pa. 2020).

V. Discussion

a. Coverage Provisions

Plaintiff bears the initial burden to reasonably demonstrate that a claim falls within the policy's coverage provisions. *State Farm Cas. Co. v. Estates of Mehlman*, 589 F.3d 105, 111 (3d Cir. 2009) (applying Pennsylvania law). Then, provided that Plaintiff satisfies its initial burden, Defendants bear "the burden of proving the applicability of any exclusions or limitations on coverage." *Koppers Co. v. Aetna Cas. & Sur. Co.*, 98 F.3d 1440, 1446 (3d Cir. 1996) (applying Pennsylvania law). In order to prevail, Defendants must demonstrate that the language of the insurance contract regarding exclusions is "clear and unambiguous: otherwise, the provision will

be construed in favor of the insured." *Fayette County Housing Authority v. Housing and Redevelopment Ins. Exchange*, 771 A.2d 11, 13 (Pa. Super. 2001).

First, this Court will address whether Plaintiff is entitled to coverage under the Business Income and Extra Expense provisions of the insurance contract for losses Plaintiff sustained in relation to the public health crises and the spread of the COVID-19 virus. With regard to Business Income and Extra Expense coverage, the insurance contract provides that:

> a. Business Income means: (1) [n]et income (Net Profit or Loss before Income taxes) that would have been earned or incurred . . . and (2) [c]ontinuing normal operating expenses incurred, including payroll, subject to 90 day limitation if indicated on the Declaration page.
>
> b. [the insurer] will pay for the actual loss of Business Income you [the insured] sustain 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 the described premises. The loss or damage must be caused by or result from a Covered Cause of Loss.

Plaintiff's Complaint, at 58, Exhibit B.

* * * * *

> a. Extra Expense means reasonable and necessary expenses you [the insured] incur during the "period of restoration" that you would not have incurred if there had been no direct physical loss of or damage to property caused by or resulting from a Covered Cause of Loss.
>
> b. [the insurer] will pay Extra Expense (other than to repair or replace property) to: (1) [a]void or minimize the "suspension" of business and to continue "operations" at the described premises or at replacement premises or temporary locations, including relocation expenses and costs to equip and operate the replacement premises or temporary locations; or (2) [m]inimize the "suspension" of business if you cannot continue "operations."
>
> c. [the insurer] will also pay any Extra Expense (including Expediting Expenses) to repair or replace property, but only to the extent it reduces the amount of loss

> that otherwise would have been payable under [the above Business Income provision].

Id. at 59, Exhibit B.

The insurance contract defines "suspension" as the "partial or complete cessation of your [the insured's] business activities; or . . . that a part or all of the described premises is rendered untenantable," and "operations" means "the type of your [the insured's] business activities occurring at the described premises and tenantability of the described premises." *Id*. at 53-55, Exhibit B. The insurance contract defines "period of restoration" as:

> the period of time that: [b]egins with the date of direct physical loss or damage caused by or resulting from any Covered Cause of Loss at the described premises; and . . . [e]nds on the earlier of: (1) [t]he date when the property at the described premises should be repaired, rebuilt or replaced with reasonable speed and similar quality; or (2) [t]he date when business is resumed at a new permanent location.

Id. at 53, Exhibit B. Additionally, "Covered Cause of Loss" is defined as "RISK OF DIRECT PHYSICAL LOSS unless the loss is: a. Excluded in Section B. Exclusions; b. Limited in paragraph A.4 Limitations; or c. Limited or Excluded by other provision of this Policy." *Id*. at 37, Exhibit B.

In order to state a reasonable claim for coverage under the Business Income and Extra Expense provisions of the insurance contract, Plaintiff must show that it suffered "direct physical loss of or damage to" its property. The interpretation of the phrase "direct physical loss of or damage to property" is the key point of the parties' dispute.[7] Defendants contend that "direct

[7] The parties do not dispute whether Plaintiff's business operations were at least partially suspended or interfered with due to COVID-19 and/or the government orders. The parties mainly contend whether Plaintiff's loss of use of its property entitles Plaintiff to coverage. The dispositive question with regard to whether Plaintiff is entitled to coverage for Business Income and Extra Expense is whether Plaintiff suffered a "direct physical loss of or damage to" Plaintiff's property. To the extent the parties disagree as to the meaning of the "period of restoration," and the potential impact of this phrase on the meaning of "direct physical loss of or damage to" Plaintiff's property, this Court addresses this issue in the body of this memorandum, after this Court's discussion of the phrase "direct physical loss of or damage to property."

physical loss of or damage to property" requires some physical altercation of or demonstrable harm to Plaintiff's property. Plaintiff contends that the "direct physical loss of . . . property" is not limited to physical altercation of or damage to Plaintiff's property but includes the loss of use of Plaintiff's property. Plaintiff further asserts that, because its interpretation is reasonable, this Court must find in Plaintiff's favor.

The insurance contract does not define the phrase "direct physical loss of or damage to property." As previously noted, Pennsylvania courts construe words of common usage in their "natural, plain, and ordinary sense . . . and [Pennsylvania courts] may inform [their] understanding of these terms by considering their dictionary definitions." *Madison Construction Company,* 735 A.2d at 108. Four words in particular are germane to the determination of this threshold issue: "direct," "physical," "loss," and "damage." "Direct" is defined as "proceeding from one point to another in time or space without deviation or interruption . . . [and/or] characterized by close logical, causal, or consequential relationship . . . ."[8] "Physical" is defined as "of or relating to natural science . . . having a material existence . . . [and/or] perceptible especially through the senses and subject to the laws of nature . . . ."[9] "Loss" is defined as "DESTRUCTION, RUIN . . . [and/or] the act of losing possession [and/or] DEPRIVATION . . . ."[10] "Damage" is defined as "loss or harm resulting from injury to person, property, or reputation . . . ."[11]

Before analyzing the definitions of each of the above terms to determine whether Plaintiff's interpretation is reasonable, it is important to note that the terms, in addition to their

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[8] Direct, Merriam-Webster, https://www.merriam-webster.com/dictionary/direct.

[9] Physical, Merriam-Webster, https://www.merriam-webster.com/dictionary/physical.

[10] Loss, Merriam-Webster, https://www.merriam-webster.com/dictionary/loss.

[11] Damage, Merriam Webster, https://www.merriam-webster.com/dictionary/damage.

ordinary, dictionary definitions, must be considered in the context of the insurance contract and the specific facts of this case. *See Madison Construction Company,* 735 A.2d at 106 (clarifying that issues of contract interpretation are not resolved in a vacuum). While some courts have interpreted "direct physical loss of or damage to property" as requiring some form of physical altercation and/or harm to property in order for the insured to be entitled to coverage, this Court reasonably determined that any such interpretation improperly conflates "direct physical loss of" with "direct physical . . . damage to" and ignores the fact that these two phrases are separated in the contract by the disjunctive "or."[12] It is axiomatic that courts must "not treat the words in the [contract] as mere surplusage . . . [and] if at all possible, [this Court must] construe the [contract] in a manner that gives effect to all of the [contract's] language." *Indalex Inc. v. Nation Union Fire Ins. Co. Pittsburgh, PA*, 83 A.3d 418, 420-21 (Pa. Super. 2013). Based upon this vital principle of contract interpretation, this Court concluded that, due to the presence of the disjunctive "or," whatever "direct physical loss of" means, it must mean something different than "direct physical . . . damage to."

In order to determine what the phrase "direct physical loss of . . . property" reasonably means, this Court looked to the ordinary, dictionary definitions of the terms "direct," "physical," "loss," and "damage." This Court began its analysis with the terms "damage" and "loss," as these terms are the crux of the disputed language. As noted above, "damage" is defined as "loss or harm resulting from injury to person, property, or reputation . . . ,"[13] and "loss" is defined as

[12] *See Fayette County Housing Authority v. Housing and Redevelopment Ins. Exchange*, 771 A.2d 11, 15 (Pa. Super. 2001) (explaining that merely accepting the non-binding decisions of other courts "by the purely mechanical process of searching the nations courts for conflicting decisions" amounts to an abdication of this Court's judicial role).

[13] Damage, Merriam Webster, https://www.merriam-webster.com/dictionary/damage.

"DESTRUCTION, RUIN . . . [and/or] the act of losing possession [and/or] DEPRIVATION . . . ."[14]

Based upon the above-provided definitions, it is clear that "damage" and "loss," in certain contexts, tend to overlap. This is evident because the definition of "damage" includes the term "loss," and at least one definition of "loss" includes the terms "destruction" and "ruin," both of which indicate some form of damage. However, as noted above, in the context of this insurance contract, the concepts of "loss" and "damage" are separated by the disjunctive "or," and, therefore, the terms must mean something different from each other. Accordingly, in this instance, the most reasonable definition of "loss" is one that focuses on the act of losing possession and/or deprivation of property instead of one that encompasses various forms of damage to property, i.e., destruction and ruin. Applying this definition gives the term "loss" meaning that is different from the term "damage." Specifically, whereas the meaning of the term "damage" encompasses all forms of harm to Plaintiff's property (complete or partial), this Court concluded that the meaning of the term "loss" reasonably encompasses the act of losing possession [and/or] deprivation, which includes the loss of use of property absent any harm to property.

In reaching its conclusion, this Court also considered the meaning and impact of the terms "direct" and "physical." Ultimately, this Court determined that the ordinary, dictionary definitions of the terms "direct" and "physical" are consistent with the above interpretation of the term "loss." As noted previously, "direct" is defined as "proceeding from one point to another in time or space without deviation or interruption . . . [and/or] characterized by close logical, causal, or consequential relationship . . . ,"[15] and "physical" is defined as "of or relating to natural

[14] Loss, Merriam-Webster, https://www.merriam-webster.com/dictionary/loss.
[15] Direct, Merriam-Webster, https://www.merriam-webster.com/dictionary/direct.

science . . . having a material existence . . . [and/or] perceptible especially through the senses and subject to the laws of nature . . . ."[16] Based upon these definitions it is certainly reasonable to conclude that Plaintiff could suffer "direct" and "physical" loss of use of its property absent any harm to property.

Here, Plaintiff's loss of use of its property was both "direct" and "physical." The spread of COVID-19, and a desired limitation of the same, had a close logical, causal, and/or consequential relationship to the ways in which Plaintiff materially utilized its property and physical space. *See* February 22, 2021 Court Order of the United States District Court, N.D. Illinois, Eastern Division case *In re: Society Insurance Co. COVID-19 Business Interruption Protection Insurance Litigation*, Civil Case No. 1:20-CV-05965 at 21 (stating that government shutdown orders and COVID-19 *directly* impacted the way businesses used *physical* space) (emphasis added). Indeed, the spread of COVID-19 and social distancing measures (with or without the Governor's orders) caused Plaintiff, and many other businesses, to *physically* limit the use of property and the number of people that could inhabit *physical* buildings at any given time. Thus, thehe spread of COVID-19 did not, as Defendant's contend, merely impose economic limitations. Any economic losses were secondary to the businesses' *physical* losses.

While Defendants are of course correct to point out that the terms "direct" and "physical" modify the terms "loss" and "damage," this does not somehow necessarily mean that the entire phrase "direct physical loss of or damage to property" requires actual harm to Plaintiff's property in every instance. Any argument that the terms "direct" and "physical," when combined, presuppose that any request for coverage must stem from some actual impact and harm to Plaintiff's property suffers from the same flaw noted in this Court's above discussion regarding

[16] Physical, Merriam-Webster, https://www.merriam-webster.com/dictionary/physical.

the difference between the terms "loss" and "damage:" such interpretations fail to give effect to all of the insurance contract's terms and, again, render the phrase " direct physical loss of" duplicative of the phrase "direct physical . . . damage to."

Defendants also contend that the insurance contract's definition for "period of restoration" suggests that the contract expressly contemplates and necessitates the existence of actual tangible damage in order for Plaintiff's to be entitled to Business Income and Extra Expense coverage. The insurance contract states that the insurer "will pay for the actual loss of Business Income [the insured] sustain[s] due to the necessary "suspension" of . . . "operations" during the "period of restoration." Plaintiff's Complaint at 58, Exhibit B. The "period of restoration" begins at the time the direct physical loss of or damage to property occurs and ends on the date when the premises "should be repaired, rebuilt, or replaced with reasonable speed and similar quality . . . or . . . when the business is resumed at a new location." *Id*. at 53, Exhibit B. Specifically, Defendants argue that, without actual tangible damage, there is no period of restoration because there is no need for the property to be repaired, rebuilt, or replaced, and Plaintiff has no plans to resume the business at a new location.

Although this Court agrees with Defendants on the general principle that the insurance contract's provisions must be read as a whole so that all of its parts fit together, this Court is not persuaded that the definition for "period of restoration" is inherently inconsistent with an interpretation of "direct physical loss of . . . property" that encompasses Plaintiff's loss of use of its property in the absence of damage. Indeed, the threat of COVID-19 has necessitated many physical changes to business properties across the Commonwealth. Such changes include, but are not limited to, the installation of partitions, additional handwashing/sanitization stations, and the installations or renovation of ventilation systems. These changes would undoubtably

constitute "repairs" or "rebuilding" of property. *See* February 22, 2021 Court Order of the United States District Court, N.D. Illinois, Eastern Division case *In re: Society Insurance Co. COVID-19 Business Interruption Protection Insurance Litigation*, Civil Case No. 1:20-CV-05965 at 23 (stating that the installation of partitions and particular ventilations systems constitute "repairs" consistent with the period of restoration). Additionally, in order to "replace" or "rebuild" unused space due to social distancing protocols, businesses might choose to buildout new spaces, move to larger spaces, or rearrange existing spaces in order to increase the amount of business they can safely handle during these difficult times.

Whether or not Plaintiff in the instant matter actually undertook such changes, or resumed its business at a new location, is of no moment. The "period of restoration" does not require repairs, rebuilding, replacement, or relocation of Plaintiff's property in order for Plaintiff to be entitled to coverage. The "period of restoration" merely imposes a time limit on available coverage, which ends whenever such measures, if undertaken, would have been completed with reasonable speed and similar quality. To put this another way, the "period of restoration" ends when Plaintiff's business is once again operating at normal capacity, or reasonably could be operating at normal capacity. The "period of restoration" does not somehow redefine or place further substantive limits on types of available coverage. Defendants cannot avoid providing coverage that is otherwise available simply because the end point with regard to the "period of restoration" may be, at times, slightly more difficult to pinpoint in the context of the COVID-19 pandemic.

As this Court determined that it is, at the very least, reasonable to interpret the phrase "direct physical loss of . . . property" to encompass the loss of use of Plaintiff's property due to the spread of COVID-19 absent any actual damage to property, Plaintiff reasonably established a

right to coverage under the Business Income and Extra Expense provisions of the insurance contract.[17]

Second, this Court will address whether Plaintiff is entitled to coverage under the Civil Authority provision of the insurance contract for losses Plaintiff sustained in relation to the Governor's orders, which were issued to help mitigate the spread of the COVID-19 virus. With regard to Civil Authority coverage, the insurance contract provides that:

> 1. When the Declarations show that [the insured has] coverage for Business Income and Extra Expense, [the insured] may extend that insurance to apply to the actual loss of Business Income [the insured] sustain[s] and reasonable and necessary Extra Expense [the insured] incur[s] caused by an action of civil authority that prohibits access to the described premises. The civil authority action must be due to direct physical loss of or damage to property at locations, other than described premises, caused by or resulting from a Covered Cause of Loss.

Plaintiff's Complaint at 84, Exhibit B (emphasis added).

Thus, in order to state a reasonable claim of coverage under the Civil Authority provision of the insurance contract, Plaintiff must reasonably demonstrate both of the following: [1] there was "direct physical loss of or damage to property" other than Plaintiff's property; and [2] the

[17] This Court is aware that the insurance contract provides that any "direct physical loss of or damage to property" must be caused by a Covered Cause of Loss. However, Covered Cause of Loss is defined as "RISK OF DIRECT PHYSICAL LOSS unless the loss is: a. Excluded in Section B. Exclusions; b. Limited in paragraph A.4 Limitations; or c. Limited or Excluded by other provision of this Policy." *Id*. at 37, Exhibit B. Admittedly, this Court was somewhat perplexed by this definition. One would think that in defining Covered Causes of Loss the contract would state, either specifically or more generally, covered causes of loss, i.e. fire, tornado, hurricane, lightening, etc.. Here, the contract's language instead turns back on itself and states that "direct physical loss of or damage to property" must be caused by "RISK OF DIRECT PHYSICAL LOSS unless the loss is . . . Excluded . . . ." Given that this insurance contract is an "All Risk" insurance policy that is meant to cover any losses, damages, and expenses to the insured's premises unless specifically excluded, this Court determined it is reasonable to interpret Covered Cause of Loss in a manner that does not further limit the scope of coverage beyond any instance that amounts to a "direct physical loss of or damage to property," which is not otherwise excluded. Accordingly, this Court determined that as long as the spread of COVID-19 caused "direct physical loss of or damage to property," and does not fall within the ambit of one of the contract's exclusions, it is reasonable to interpret the contract as entitling Plaintiff to coverage. This same analysis regarding the term Covered Cause of Loss applies equally in the context of the contract's provision regarding Civil Authority coverage. Thus, this Court need not address Covered Cause of Loss again separately.

"direct physical loss of or damage to property" other than Plaintiff's property caused civil authorities to take action(s) that prohibited access to Plaintiff's property.

Defendants contend that Plaintiff is not entitled to coverage under the Civil Authority provision of the contract because the Governor's orders did not completely prohibit Plaintiff from accessing its property. According to Defendants, although the Governor's orders closed Plaintiff's property to the majority of the general public, Plaintiff is nonetheless precluded from coverage under the Civil Authority provision of the insurance contract because Plaintiff and Plaintiff's employees were still able to access Plaintiff's property in order to conduct emergency procedures. Defendants also argue, just as they did with regard to the Business Income and Extra Expense coverage provisions, that any actions taken by civil authorities in response to COVID-19 were not caused by "direct physical loss of or damage to" property at any location. In contrast, Plaintiff contends that, because the Governor's orders prohibited Plaintiff from operating its business except in cases of emergency, and because the Governor's orders directed citizens of the Commonwealth to stay at home, the Governor's orders effectively prohibited meaningful access to Plaintiff's property. Additionally, Plaintiff argues that COVID-19 caused "direct physical loss of or damage to" property across the Commonwealth just as it did with regard to Plaintiff's property.

As to whether the spread of the COVID-19 virus caused "direct physical loss of or damage to" property, the same analysis that this Court applied with regard to Plaintiff's property also applies to other property as well. Even absent any damage to property, the spread of COVID-19 has resulted in a serious public health crisis, which has directly and physically caused the loss of use of property all across the Commonwealth. Again, this is evident because COVID-19 and the related social distancing measures (with and without government orders) directly

forced businesses everywhere to physically limit the use of property and the number of people that could inhabit physical buildings at any given time in a safe and responsible manner. This Court's conclusion that other property was impacted by COVID-19 is supported by the Supreme Court of Pennsylvania. In *Friends of Danny DeVito v. Wolf*, 227 A.3d 872, 890 (Pa. 2020), our Supreme Court clarified that the COVID-19 virus qualifies as a natural disaster, and, given the nature of the manner in which COVID-19 spreads, Governor Wolf "had the authority under the Emergency Code to declare the entirety of the Commonwealth a disaster area."[18]

With regard to whether "an action of civil authority . . . prohibit[ed] access" to Plaintiff's property, this Court determined that the phrase "prohibits access" may reasonably be interpreted to encompass the instant situation. The term "prohibit" is defined as "to forbid by authority [and/or] to prevent from doing something . . . ."[19] Here, the Governor's emergency orders did exactly that. The Governor's orders directed individuals to stay home and required businesses to essentially close their doors absent emergencies and/or the need to conduct life sustaining operations. Although Plaintiff's business (a dental practice) was technically permitted to remain open to conduct certain limited emergency procedures, this does not change the fact that an action of civil authority effectively prevented, or forbade by authority, citizens of the Commonwealth from accessing Plaintiff's business in any meaningful way for normal, non-emergency procedures; procedures that likely yeild a significant portion of Plaintiff's business income.

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[18] In its opinion upholding the Governor Wolf's use of the Emergency Code to shutdown businesses throughout the Commonwealth, the Supreme Court of Pennsylvania explained that, as of April 8, 2020, confirmed cases of COVID-19 had been reported in every single county in the Commonwealth, and "*any location where two or more people can congregate is within the disaster area*." *Friends of Danny DeVito v. Wolf*, 227 A.3d 872, 889-90 (Pa. 2020) (emphasis added). The Supreme Court of Pennsylvania reached this conclusion because "[t]he virus spreads *primarily through person-to-person contact*, has an incubation period of up to fourteen days, one in four carriers are asymptomatic, and the virus can live on surfaces for up to four days." *Id*. at 889 (emphasis added).

[19] Prohibit, Merriam-Webster, https://www.merriam-webster.com/dictionary/prohibit.

This Court is not persuaded by Defendant's argument that, in order to be entitled to Civil Authority coverage, the action of civil authority must be a complete and total prohibition of all access to Plaintiff's property by any person for any reason. If this Court were to accept Defendant's cramped interpretation of the phrase "prohibits access," it would result in businesses being precluded from coverage in nearly every instance where an action of civil authority effectively closes the business to the vast majority of the general public, but does not necessarily preclude employees, or certain other individuals, from entering the premises to clean, maintain the building, obtain important documents, or to perform other similar functions, which, while important, remain secondary to the activities that actually generate business income.

Once again this Court notes the importance of reading the insurance contract's provisions as a whole so that all of its parts fit together. In so doing, this Court recognizes that the insurance contract provisions at issue are generally designed to provide business owners with coverage for lost busines *income* in the event that their business' operations are suspended. Accordingly, this Court's primary focus when interpreting the phrase "prohibits access," at least in the context of this insurance contract, is the extent to which the action of civil authority prevented the insured from accessing its premises in a manner that would normally produce actual and regular business income. Given this understanding of the insurance contract, the fact that some employees, and even some limited number of patients, were still permitted to go to Plaintiff's property for emergency procedures does not necessarily mean that Plaintiff is altogether precluded from coverage under the Civil Authority provision. The contract merely requires that "an action of civil authority . . . prohibits access to" Plaintiff's property. It does not clearly and unambiguously state that any such prohibition must completely and totally bar *all* persons from *any* form of access to Plaintiff's property whatsoever.

As this Court determined that Plaintiff provided a reasonable interpretation that: [1] there was "direct physical loss of or damage to property" other than Plaintiff's property; and [2] the "direct physical loss of or damage to property" other than Plaintiff's property caused civil authorities to take action(s) that prohibited access to Plaintiff's property, this Court concluded that Plaintiff established a right to coverage under the Civil Authority provision of the contract.

b. Exclusions

Having determined that Plaintiff provided reasonable interpretations demonstrating that there is coverage under the Business Income, Extra Expense, and Civil Authority provisions of the insurance contract, this Court turns to the question of whether Defendants demonstrated "the applicability of any exclusions or limitations on coverage." *Koppers Co.*, 98 F.3d at 1446 (applying Pennsylvania law). As discussed previously, in order to prevail, Defendants must show that the language of the insurance contract regarding exclusions is "clear and unambiguous: otherwise, the provision will be construed in favor of the insured." *Fayette County Housing Authority*, 771 A.2d at 13.

This Court starts by addressing the exclusion for Contamination. With regard to this exclusion, the insurance contract provides that "[the insurer] will not pay for loss or damage caused directly or indirectly by any of the following . . . [c]ontamination by other than "pollutants." Plaintiff's Complaint at 41, Exhibit B. Because the insurance contract does not define the term contamination, this Court looks to the word's natural, plain, and ordinary meaning, and informs its understanding of this term by considering its dictionary definition. *Madison Construction Company,* 735 A.2d at 108.

Merriam-Webster defines contamination as "the process of contaminating [and/or] the state of being contaminated."[20] Additionally, in *Raybestos-Manhattan, Inc. v. Industrial Risk Insurers*, 433 A.2d 906, 907 (Pa. Super. 1981), the Superior Court of Pennsylvania clarified that:

> Contamination connotes a condition of impurity resulting from mixture or contact with a foreign substance . . . [and] the word contaminate is defined as . . . to render unfit for use by the introduction of unwholesome or undesirable elements . . . . Contaminate implies an action by something external to an object which by entering into or coming in contact with the object destroys its purity.

This Court recognizes that the above-described common and ordinary definitions of the terms contamination and contaminate are considerably broad. However, in determining whether the contamination exclusion applies clearly and unambiguously to the loss of use of property due to social distancing measures designed to prevent the spread of COVID-19, this Court acknowledges that the question is not whether the definition of contamination is so broad that virtually anything could come within its ambit. *Madison Construction Co.*, 735 A.2d at 607. Instead, this Court is "guided by the principle that ambiguity (or the lack thereof) is to be determined by reference to a particular set of facts." *Id*.

Based upon the above dictionary definitions, the contamination exclusion only applies, in the broadest sense, when something external comes into contact with an object, i.e., property, and destroys the object's purity. Accordingly, if the specific cause of the loss of use of property was COVID-19 contacting objects, and destroying the objects' purity, then the insurance contract's contamination exclusion might prevent coverage. However, based upon the particular facts of this case, and considering the primary means by which COVID-19 spreads, the cause for the loss of use of property was *not* the contamination of property. Rather, the cause of the loss of use of property was the risk of person-to-person transmission of COVID-19, which necessitated

[20] Contamination, Merriam-Webster, https://www.merriam-webster.com/dictionary/contamination.

social distancing measures and fundamentally changed the way businesses utilized physical space (property).

The Supreme Court's recent decision in *Friends of Danny DeVito* supports the above conclusion. In rejecting the argument that actual contamination of specific property was necessary in order to justify Governor Wolf's orders restricting business operations throughout the Commonwealth, the Supreme Court of Pennsylvania elucidated that arguments regarding the dangers of COVID-19 contaminating property misunderstand the primary means by which COVID-19 spreads. *Id.* at 892. Specifically, the Supreme Court of Pennsylvania clarified that "COVID-19 does not spread because the virus is *at* a particular location . . . [i]nstead it spreads because of person-to-person contact, as it has an incubation period of up to fourteen days and that one in four carriers are asymptomatic. *Id*. (emphasis in original).

Although it is contested whether COVID-19 can live on the surfaces of property for some period of time, and while this might be one way by which individuals contract COVID-19, it is not the primary means nor is it the only means by which COVID-19 spreads. *Id*. Indeed, with or without actual COVID-19 contamination at any given property in the Commonwealth, businesses suffered the loss of use of property due to the risk of person-to-person COVID-19 transmission. Thus, the risk of person-to-person transmission of COVID-19, and the social distancing measures necessary to mitigate the spread of the COVID-19, together constitute a cause that is both *separate and distinct* from any possible or actual contamination of property.

It is important to note that, although the contamination exclusion might, at times, cover viruses when viruses actually contaminate property, the contamination exclusion does *not* altogether exclude loss of use of property caused by viruses in any manner whatsoever. If Defendants wanted to exclude coverage for any loss caused by viruses in any manner

whatsoever, Defendants could have easily included such a provision clearly and unambiguously in the contract. However, Defendants did not include a virus exclusion.

In sum, because it is reasonable to conclude that the loss of use of property due to the risk of person-to person transmission of COVID-19 is not clearly and unambiguously encompassed by the contamination exclusion, Defendants failed to show that the contamination exclusion prevents coverage in this instance.[21]

Next, this Court will address the exclusion for Fungi, Wet Rot, Dry Rot and Microbes. With regard to this exclusion, the insurance contract provides that the insurer will not pay for loss or damage caused directly or indirectly by the "[p]resence, growth, proliferation, spread or any activity of fungi, wet or dry rot, or microbes." Plaintiff's Complaint at 118, Exhibit B. The insurance contract provides the following definition for the term "Microbes:"

> "Microbe(s)" means any non-fungal micro-organism or non-fungal, colony-form organism that causes infection or disease. "Microbes" includes any spores, mycotoxins, odors, or any other substances, products, or by products produced by, or arising out of the current or past presence of "microbes."

Id. at 19, Exhibit B.

Without any elaboration and explanation, Defendants contend that COVID-19 is excluded because viruses fall within the insurance contract's definition of the term "Microbe." This Court is, however, not persuaded that Defendants' interpretation of the term "Microbe" is clear and unambiguous.

[21] While this Court's above analysis is not dependent upon whether COVID-19 was in fact at Plaintiff's premises, Defendants' Cross Motions for Summary Judgment acknowledge that "Plaintiff neither alleged nor produced evidence that the virus was present at its dental offices . . . ." Valley Forge Insurance Company 's Cross Motion for Summary Judgment at 10; *see also* CNA's Cross Motion for Summary Judgment at 10. This fact provides further support that the contamination exclusion does not prevent coverage in this instance. Defendants cannot, at the same time, contend that the virus was not present at Plaintiff's property and that the exclusion contamination exclusion applies.

Naturally, upon its initial review, the contract's use of the word "Microbe" caused this Court to pause and generally wonder what is a "Microbe," and more specifically with regard to this case, does a virus qualify as a "Microbe?" Again, this begs the question: If Defendants wanted to exclude viruses, why not simply use the word virus explicitly in the insurance contract? Regardless, even assuming that a virus could technically be considered a "Microbe" in the most general sense of the word, this Court recognizes that, in this instance, it is of course not the general sense of the term "Microbe" that is controlling. Rather, because the insurance contract provides a specific definition of the term "Microbe," it is this definition that necessarily dictates what a "Microbe" is, and whether viruses fall within the ambit of the contract's "Microbe" exclusion.

Upon reading the insurance contract's definition of the term "Microbe," this Court determined that, in order to fall within the "Microbe" exclusion, COVID-19 must qualify as a "micro-organism" and/or an "organism." Because the contract does not define the terms "micro-organism" or "organism," this Court looked to the words' natural, plain, and ordinary meaning, and informed its understanding of these terms by considering their dictionary definitions. *Madison Construction Company,* 735 A.2d at 108.

Merriam-Webster defines "microorganism" as "an organism (such as a bacterium or protozoan) of microscopic or ultramicroscopic size."[22] Merriam-Webster defines "organism" in relevant part as "an individual constituted to carry on the activities of life by means of parts or organs more or less separate in function but mutually dependent [and/or] *a living being*."[23]

[22] Microorganism, Merriam-Webster, https://www.merriam-webster.com/dictionary/microorganism.

[23] Organism, Merriam-Webster, https://www.merriam-webster.com/dictionary/organism (emphasis added).

In contrast, Merriam-Webster defines a virus as "any large group of submicroscopic infectious agents that are usually regarded as *nonliving* extremely complex molecules . . . that are capable of growth and multiplication only in living cells, and that cause various important diseases in humans, animals, and plants."[24] In fact, "outside a host viruses are dormant . . . [they] have none of the traditional trappings of life [and their] zombielike existence . . . makes them easy to catch and hard to kill."[25]

Based upon the ordinary, dictionary definitions of the terms "microorganism," "organism," and "virus," this Court concluded that: [1] the term "Microbe" generally includes things that carry on the activities of life, i.e., things that are alive; and [2] a virus is generally regarded as something that is non-living, and is capable of growth and multiplication only when it attaches to, or gets inside of, other living host cells. Accordingly, given the insurance contract's specific definition of the term "Microbe," it is reasonable to conclude that the "Microbe" exclusion does not actually encompass viruses, as viruses are generally not considered living things. Consequently, this Court determined that Defendants failed to demonstrate that the exclusion for Fungi, Wet Rot, Dry Rot and Microbes clearly and unambiguously prevents coverage.

In reaching these conclusions, this Court of law does not masquerade as an expert in the complex intricacies of science, nor does it presume to wholly realize the subtle considerations by which trained scientists define and classify things in the natural world. This Court acknowledges that, in certain contexts, the terms "microorganism" and/or "organism" might refer to things that

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[24] Virus, Merriam-Webster, https://www.merriam-webster.com/dictionary/virus (emphasis added).

[25] Sarah Kaplan et al., *The coronavirus isn't alive. That's why it's so hard to kill.*, The Washington Post, March 23, 2020 https://www.washingtonpost.com/health/2020/03/23/coronavirus-isnt-alive-thats-why-its-so-hard-kill/.

are not traditionally considered living entities.[26] This Court also understands that there are some in the scientific community who might classify viruses as a kind of semi-living, zombie-like thing.[27] However, this Court need not wade into the mire of such sophisticated considerations. The question before this Court on summary judgment is not so complicated. The question is simply whether the insurance contract provisions at issue are subject to more than one reasonable interpretation. If the contract's terms are subject to more than one reasonable interpretation, they are ambiguous, and Pennsylvania law directs this Court to find in favor of the insured. Again, this Court may inform its understanding of the contract's terms using ordinary, dictionary definitions. *See Madison Construction Company,* 735 A.2d at 108. Based upon the above definitions, this Court determined that it is reasonable to interpret the "Microbe" exclusion as applying only to *living* microscopic things such as bacterium, and *not non-living* viruses.[28]

Next, this Court will address the exclusion for Consequential Loss. With regard to this exclusion, the insurance contract provides that the insurer will not pay for loss or damage caused

---

[26] Merriam-Webster also defines "organism" in the most general sense as "a complex structure of interdependent and subordinate elements whose relations and properties are largely determined by their function in the whole." Organism , Merriam-Webster, https://www.merriam-webster.com/dictionary/organism. Merriam-Webster elaborates on this particular use of the word organism by providing the following quotation from Joseph Rossi: "the nation is not merely the sum of individual citizens at any given time, but it is a living organism, a mystical body . . . of which the individual is an ephemeral part." *Id*. Based upon this quotation, and the context in which the terms "microorganism" and "organism" appear in the insurance contract, this Court concluded that more scientific definition is most relevant to this Court's discussion.

[27] While there is some argument over whether viruses are living organisms, "[m]ost virologists consider them non-living, as they do not meet all the criteria of the generally accepted definition of life." *What are microorganisms?* Centre for Geobiology, University of Bergen, November 1, 2010 https://www.uib.no/en/geobio/56846/what-are-microorganisms.

[28] Bacterium is defined to include to following:

> any of a domain (Bacteria) . . . of chiefly round, spiral, or rod-shaped single-celled prokaryotic microorganisms that typically *live* in soil, water, organic matter, or the bodies of plants and animals, that make their own food especially from sunlight or are saprophytic or parasitic, are often motile by means of flagella, reproduce especially by binary fission, and include many important pathogens.

Bacterium, Merriam-Webster, https://www.merriam-webster.com/dictionary/bacterium (emphasis added).

directly or indirectly by "[d]elay, loss of use or loss of market." Plaintiff's Complaint at 41, Exhibit B. Defendants argue that even if Plaintiff had shown a basis for coverage under the insurance contract, this exclusion clearly and unambiguously excludes coverage.

The problem with this exclusion is not so much that it is unclear or ambiguous. Rather, the problem is that, based upon a plain reading of the Consequential Loss exclusion, this exclusion would vitiate Business Income, Extra Expense, and Civil Authority coverage in their entirety. *See* January 19, 2021 Court Order of the United States District Court, N.D. Ohio, Eastern Division case *Henderson Road Restaurant Systems, Inc. v. Zurich American Insurance Company*, Civil Case No. 1:20-cv-01239-DAP (holding that "the Loss of Use exclusion *would* vitiate the Loss of Business Income coverage"). This evident because, even if this Court accepted Defendants' more limited interpretation of the scope of coverage and the phrase "direct physical loss of or damage to property" to only include coverage in instances where Plaintiff's property was physically altered or damaged, this exclusion would effectively eliminate coverage for any kind of loss and/or damage caused by any covered peril, which closes Plaintiff's business while it is being repaired. *Id*. In other words, if this Court were to find the exclusion for Consequential Loss to be valid, this exclusion would make all Business Income, Extra Expense, and Civil Authority coverage illusory. *See Heller v. Pennsylvania League of Cities and Municipalities*, 32 A.3d 1213, 1228 (Pa. 2011) (holding that where an exclusionary provision of an insurance contract operates to foreclose the majority of expected claims, such a provision is void as it renders coverage illusory). Because this Court must read the insurance contract in its entirety, and in a manner calculated to give the agreement its intended effect, this Court concludes that the exclusion for Consequential Loss does not prevent coverage.

Finally, this Court will address the exclusions for Acts or Decisions and Ordinance or Law. With regard to the exclusion for Acts or Decisions, the insurance contract provides that the insurer will not pay for loss or damage caused directly or indirectly by "Acts or Decisions, including the failure to act or decide, of any person, group, organization or governmental body." Plaintiff's Complaint at 42, Exhibit B. With regard to the exclusion for Ordinance or Law, the insurance contract provides that the insurer will not pay for loss or damage caused directly or indirectly by the following:

> (1) The enforcement of any ordinance or law:
> (a) Regulating the construction, use or repair of any property; or
> (b) Requiring the tearing down of any property, including the cost of removing debris.
>
> (2) This exclusion applies whether the loss results from:
> (a) An ordinance or law that is enforced even if the property has not been damaged; or
> (b) The increased costs incurred to comply with an ordinance or law in the course of construction, repair, renovation, remodeling or demolition or property, or removal of its debris, following a physical loss to that property.

Defendants argue that coverage is precluded by both of the above exclusions because Plaintiff's claim for "direct physical loss of or damage to property" is solely due to the Governor's orders. This, however, is not the case. In its complaint, Plaintiff states that its claim for coverage is based upon losses and expenses Plaintiff suffered in relation to both "*the COVID-19 pandemic* and the actions of the government in response thereto." Plaintiff's Complaint at 4 (emphasis added). As this Court explained earlier in this memorandum, COVID-19 and the related social distancing measures (with and without government orders) directly forced businesses everywhere to physically limit the use of property and the number of people that could inhabit physical buildings at any given time. The Governor's orders only came into consideration in the context of Plaintiff's claim for coverage under the Civil Authority provision

of the contract.[29] Accordingly, Defendants failed to demonstrate that the exclusions for Acts or Decisions and Ordinance or Law preclude coverage.

VI. Conclusion

In Pennsylvania, "where there is doubt or uncertainty about the meaning of ambiguous language used in a policy of insurance, the policy must be construed in favor of the insured in order to not defeat the protection which [the insured] reasonably expected from the policy [the insured] purchased." *Raybestos-Manhattan, Inc.*, 433 A.2d at 483. This Court determined that Plaintiff's interpretations of the Business Income, Extra Expense, and Civil Authority provisions of the insurance contract were, at the very least, reasonable. Additionally, this Court concluded that Defendants failed to demonstrate that any of the insurance contract's exclusions clearly and unambiguously prevent coverage. Accordingly, because there are no genuine issues of material fact, Plaintiff's Motion for Summary Judgment is GRANTED, and Defendants' Cross Motions for Summary Judgement are DENIED.

By the Court:

Christine Ward, J.

Christine Ward, J.

Dated: 3/22/21

[29] Certainly, the exclusions for Acts or Decisions and Ordinance or Law could not have been intended to exclude coverage under the Civil Authority provision of the contract, as this would make any extended coverage for the actions of Civil Authority illusory. *See Heller v. Pennsylvania League of Cities and Municipalities*, 32 A.3d 1213, 1228 (Pa. 2011) (holding that where an exclusionary provision of an insurance contract operates to foreclose expected claims, such a provision is void as it renders coverage illusory).

IN THE COURT OF COMMON PLEAS OF ALLEGHENY COUNTY, PENNSYLVANIA

TIMOTHY A. UNGAREAN, DMD d/b/a SMILE SAVERS DENTISTRY, PC, INDIVIDUALLY AND ON BEHALF OF A CLASS OF SIMILARLY SITUATED PERSONS,	:	CIVIL DIVISION
	:	No.: GD-20-006544
Plaintiff,	:	
v.	:	**Order of Court**
CNA and VALLEY FORGE INSURANCE COMPANY,	:	
Defendants.	:	

ORDER OF COURT

And Now, this 22 day of March, 2021, upon consideration of Timothy A. Ungarean, DMD's Motion for Summary Judgment, Valley Forge Insurance Company's Cross Motion for Summary Judgment, and CNA's Cross Motion for Summary Judgment, and the parties' oral arguments thereto, it is hereby ORDER, ADJUDGED, and DECREED that Timothy A. Ungarean, DMD's Motion for Summary Judgment is GRANTED, and Valley Forge Insurance Company's and CNA's Cross Motions for Summary Judgment are DENIED.

By the Court:

Christine Ward, J.

Christine Ward, J.

ADDENDUM 8

SUPERIOR COURT OF CALIFORNIA,
COUNTY OF ORANGE
CIVIL COMPLEX CENTER

MINUTE ORDER

DATE: 01/28/2021 TIME: 02:00:00 PM DEPT: CX102

JUDICIAL OFFICER PRESIDING: Peter Wilson
CLERK: Virginia Harting
REPORTER/ERM: Lisa Suzanne Rouly CSR# 9524
BAILIFF/COURT ATTENDANT: Raquel Wangsness

CASE NO: **30-2020-01169032-CU-IC-CXC** CASE INIT.DATE: 11/06/2020
CASE TITLE: **Goodwill Industries of Orange County, California vs. Philadelphia Indemnity Insurance Company**
CASE CATEGORY: Civil - Unlimited CASE TYPE: Insurance Coverage

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EVENT ID/DOCUMENT ID: 73432648

EVENT TYPE: Demurrer to Complaint
MOVING PARTY: Philadelphia Indemnity Insurance Company
CAUSAL DOCUMENT/DATE FILED: Demurrer to Complaint, 12/23/2020

EVENT ID/DOCUMENT ID: 73450761

EVENT TYPE: Status Conference

APPEARANCES

Appearances noted by way of CourtCall Appearance Calendar, attached hereto and incorporated herein by reference.

Defendant Philadelphia Indemnity Insurance Company's ("Philadelphia") general demurrer to the First, Third and Fifth Causes of Action

Tentative Ruling posted on the Internet.

The Court hears oral argument and confirms the tentative ruling as follows:

Defendant Philadelphia Indemnity Insurance Company's ("Philadelphia") general demurrer to the First, Third and Fifth Causes of Action is OVERRULED. Defendant is ordered to file its answer within 10 days.

A general demurrer challenges the legal sufficiency of a complaint on the ground that it fails to state facts sufficient to constitute a cause of action. (Code Civ. Proc. § 430.10(e).) The allegations in the complaint as a whole must be reviewed to determine whether a set of alleged facts constitutes a cause of action. *(People v. Superior Court (Cahuenga's the Spot)* (2015) 234 Cal.App.4th 1360, 1376.) A complaint need only meet fact-pleading requirements, which requires a statement of facts constituting a cause of action in ordinary and concise language, and should allege ultimate facts that, as a whole, apprise defendant of the factual basis of the claim. (Code Civ. Proc. §425.10(a)(1); *Navarrete v. Meyer* (2015) 237 Cal.App.4th 1276, 1284.)

In ruling on a demurrer, the court is guided by the following long-settled rules: The court treats the demurrer as admitting all material facts properly pleaded, but not contentions, deductions or conclusions of fact or law. The court may also consider matters which may be judicially noticed. Further, the court gives the complaint a reasonable interpretation, reading it as a whole and its parts in their context. (*Blank v. Kirwan* (1985) 39 Cal.3d 311, 318.)

In a demurrer based on insurance policy language, the insurer "must establish conclusively that this language unambiguously negates beyond reasonable controversy the construction alleged in the body of the complaint." (*Columbia Casualty Co. v. Northwestern Nat. Ins. Co.* (1991) 231 Cal.App.3d 457, 468–473, 282 Cal.Rptr. 389.) To meet this burden, an insurer is required to demonstrate that the policy language supporting its position is so clear that parol evidence would be inadmissible to refute it. (*Id.* at p. 469, 282 Cal.Rptr. 389.) Absent this showing, the court must overrule the demurrer and permit the parties to litigate the issue in a context that permits the development and presentation of a factual record, e.g., summary judgment or trial." (*Palacin v. Allstate Ins. Co.* (2004) 119 Cal. App. 4th 855, 862.)

Philadelphia demurrers to the 1st, 3rd and 5th causes of action on the ground that Plaintiff has not alleged sufficient facts to show "direct physical loss" under the Business Income and Extra Expenses and Civil Authority provisions in its insurance policy because coronavirus and COVID-19 do not physically alter the structure. In response Plaintiff contends (a) that "direct physical loss" does not require physical tangible alteration of the property and that allegations of loss of use are sufficient, and (b) that if physical tangible alteration is required, Plaintiff has satisfied this requirement.

Whether Plaintiff has alleged sufficient facts to overcome Philadelphia's demurrer depends on the interpretation of "direct physical loss". The interpretation of an insurance policy is a question of law and applies the well-settled rules of contract interpretation. (*Waller v. Truck Ins. Exch.* (1995) 11 Cal. 4th 1, 18; *Vardanyan v. AMCO Ins. Co.* (2015) 243 Cal. App. 4th 779, 792.)

"The mutual intention of the parties as it existed at the time of contracting governs interpretation. (Civ. Code, § 1636.) " 'Such intent is to be inferred, if possible, solely from the written provisions of the contract. [Citation.] The "clear and explicit" meaning of these provisions, interpreted in their "ordinary and popular sense," unless "used by the parties in a technical sense or a special meaning is given to them by usage" [citation], controls judicial interpretation.' " (*Waller v. Truck Ins. Exchange, Inc.* (1995) 11 Cal.4th 1, 18, 44 Cal.Rptr.2d 370, 900 P.2d 619.) " 'Any ambiguous terms are resolved in the insureds' favor, consistent with the insureds' reasonable expectations.' " (*Safeco Ins. Co. v. Robert S.* (2001) 26 Cal.4th 758, 763, 110 Cal.Rptr.2d 844, 28 P.3d 889.) Policy exclusions are strictly construed; exceptions to exclusions are broadly construed in favor of the insured. (*E.M.M.I.*, at p. 471, 9 Cal.Rptr.3d 701, 84 P.3d 385.)

(*Vardanyan v. AMCO Ins. Co.*, *supra*, 243 Cal. App. 4th at 792.)

In *MRI Healthcare Center of Glendale v. State Farm General Ins. Co.* (2010) 187 Cal.App.4th 766 ("*MRI Healthcare*"), on cross-motions for summary judgment, the court considered whether plaintiff insured suffered "direct physical loss" to an MRI (magnetic resonance imaging) machine within the meaning of a business insurance policy. (*Id.* at 769–770, 777–778.) The *MRI Healthcare* court stated: "A direct physical loss 'contemplates **an actual change in insured property** then in a satisfactory state, occasioned by accident or other fortuitous event directly upon the property causing it to become unsatisfactory for future use or requiring that repairs be made to make it so.' [Citation.] ... **For loss to be covered, there must be a 'distinct, demonstrable, physical alteration' of the property.**" (*Id.* at 779, emphasis added.) The *MRI Healthcare* court further explained: "For there to be a 'loss' within the meaning of the policy, some **external force** must have acted upon the insured property to cause a **physical change in the condition of the property**, i.e., it must have been 'damaged' within the common understanding of that term." (*Id.* at 780, emphasis added.) Thus, the MRI machine did not suffer any "actual physical 'damage' " by virtue of the fact that it was turned off and could not be turned back

on. (*Ibid.*)

Neither party has cited to any California state cases that have resolved the question whether coronavirus or COVID-19 may cause "direct physical loss" to property.

Here, the Complaint expressly alleges the coronavirus and COVID-19 caused direct physical loss and damages to its property. The Complaint makes the following specific factual allegations: coronavirus and COVID-19 are contained in respiratory droplets called aerosols that stay on surfaces and in the air for up to a month, physically alters the air and surfaces to which it attaches and causes them to be unsafe, deadly and dangerous (Complaint, at ¶¶2, 20, 22-26); that "[r]ecognizing the ability of the coronavirus to attach onto surfaces," researchers have begun to develop technology to test for the presence of COVID-19 on the surfaces of buildings (Complaint, at ¶21); and that coronavirus and COVID-19 were present at its properties at the time of the State and County closure orders, that when Plaintiff reopened its properties, its employees tested positive, and that it was required to conduct "additional cleaning and sanitization to respond to and remove the coronavirus and COVID-19 from physical surfaces in its insured premises and properties in accordance with public health orders that require such measures to protect against the coronavirus and COVID-19 (Complaint, at ¶¶42-44).

Construing these allegations as true as the Court must on a demurrer, the Court cannot determine as a matter of law that these allegations do not show a "direct physical loss" in accordance with *MRI Healthcare*. (See *Studio 417, Inc. v. Cincinnati Insurance Company* (W.E. Mo. August 12, 2020, Case No. 20-cv-03127-SRB) ___ F. Supp.3d ___, 2020 WL 4692385, 4-5 [plaintiff adequately plead a claim for "direct physical loss" by alleging COVID-19 is a physical substance that lives on surfaces and in the air making its property unsafe and unusable and resulting in direct physical loss].)

The Court recognizes that California federal cases have interpreted *MRI Healthcare* to require a physical change in the property or permanent dispossession of the property to qualify as "direct physical loss" and have generally rejected arguments that business losses due to coronavirus and Covid-19 are covered under Business Income, Extra Expenses and Civil Authority provisions. See Amended Mem. Supp., at pp. 12 -14. However, these federal California cases are not binding on this Court and were decided under a different standard. While these cases are instructive, the allegations in those cases are largely distinguishable from those alleged here. (See e.g, *10E, LLC v. Travelers Indemnity Co. of Connecticut (C.D. Cal. September 2, 2020, Case No. 2:20-cv-04418-SVW-AS) ___ F.Supp.2d ___, 2020 WL 5359653, 1, 5 [no allegations of physical alteration]; Mudpie, Inc. v. Travelers Casualty Ins. Co. of America* (N.D. Cal. September 14, 2020) 2020 WL 5525171, *1, 4-5 [no allegations of any external physical force that induced detrimental change; *West Coast Hotel Management, LLC v. Berkshire Hathaway Guard Insurance Companies* (C.D. Cal. October 27, 2020, Case No. 2:20-cv-05663-VAP-DFMx) ___ F. Supp.3d ___, 2020 WL 6440037 *4-5 [no allegations of physical transformation or requiring that anything needed to be repaired, rebuilt or replaced]; *Pappy's Barber Shops, Inc. v. Farmers Group, Inc.* (S.D. Cal. September 11, 2020, Case No. 20-cv-907-CAB-BLM) 2020 WL 5500221, *1,5 [no factual allegations to support arguments of physical damages].)

More importantly, given the high standard that must be met to prevail on a demurrer on an insurance policy, any doubts must be resolved in favor of the Plaintiff. The Court is not satisfied that there is a sufficiently full record at this demurrer stage to make the determination as a matter of law that the coronavirus and COVID-19 have not, in some manner, caused physical damage to property.

Accordingly, the demurrer is overruled.

The Court overrules Plaintiff's objections to Exhibits B -G and grants Philadelphia's request for judicial notice.

Status Conference

Status Conference continued to April 2, 2021 at 9 AM in this department pursuant to Court's motion.

The parties are ordered to file a joint status report not later than March 26, 2021.

Moving Party is ordered to give notice.

CourtCall® Appearance Calendar

January 2021

28 Thursday

CX102Video **Judge Peter Wilson (Video Only)**

Orange County Superior Court-Santa Ana

02:00 PM PT **Dial: (855) 268-7844** **Code: 8191402#** **PIN: 0135149**

Time	Case Information	Attorney Information
	Case #: 04-2020-01169032 **Case Name:** Goodwill Industries of Orange County Cali. vs. Philadelphia Indemnity Insurance Co. **Proceeding Type:** Court Approved Video Hearing	Firm: Dentons US, LLP Phone: (213) 623-9300 ext. Contact: Ronald D. Kent For: Defendant(s), Philadelphia Indemnity Insurance Co CCID: 11061256
		Firm: Dentons US, LLP Phone: (312) 876-3156 ext. Contact: April Elkovitch For: Defendant(s), Philadelphia Indemnity Insurance Co. CCID: 11062184
		Firm: Dentons US, LLP Phone: (312) 876-3156 ext. Contact: Jeffrey Zachman For: Defendant(s), Philadelphia Indemnity Insurance Co. CCID: 11051155
		Firm: Dentons US, LLP Phone: (312) 876-3156 ext. Contact: John Kirby For: Defendant(s), Philadelphia Indemnity Insurance Co. CCID: 11062176
		Firm: Denton US, LLP - St. Louis Phone: (314) 259-5807 ext. Contact: Richard Fenton For: Defendant(s), Philadelphia Indemnity Insurance Co. CCID: 11051154
		Firm: Dentons US, LLP Phone: (949) 732-3700 ext. Contact: Justin Martin For: Defendant(s), Philadelphia Indemnity Insurance Co. CCID: 11051153

CourtCall® Appearance Calendar

January 2021 Same Day Jan 28 2021 12:22PM

28 Thursday

CX102 **Judge Peter Wilson (VC)**

Orange County Superior Court-Santa Ana

02:00 PM PT

Time	Case Information	Attorney Information

Case #: 04-2020-01169032

Case Name:

Goodwill Industries of Orange County Cali. vs. Philadelphia Indemnity Insurance Co.

Proceeding Type:

Status Conference

Firm:	Robins Kaplan LLP
Phone:	(310) 229-5405 ext.
Contact:	Sean R. O'Connor
For:	Defendant(s), Certain Underwriters at Lloyd's
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Firm:	Robins Kaplan LLP
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Contact:	Joan Li
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Firm:	Cheri Violette-Makino, CSR, Inc.
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Contact:	Lisa Rouly
For:	Court Reporter, Lisa Rouly
CCID:	11072109

ADDENDUM 9

COUCH'S "PHYSICAL ALTERATION" FALLACY: ITS ORIGINS AND CONSEQUENCES

Richard P. Lewis,* *Lorelie S. Masters*,**
*Scott D. Greenspan**** *& Chris Kozak*****

I. INTRODUCTION

Look at virtually any Covid-19 case favoring an insurer, and you will find a citation to Section 148:46 of *Couch on Insurance*.[1] It is virtually ubiquitous: courts siding with insurers cite *Couch* as restating a "widely held rule" on

1. 10A Steven Plitt, et al., Couch on Insurance 3d § 148:46. As shown below, some courts quote *Couch* itself, while others cite cases citing *Couch* and merely intone the "distinct, demonstrable, physical alteration" language without citing *Couch* itself. *Couch 1st* and *Couch 2d* were published in hardback books (with pocket parts), in 1929 and 1959 respectively. As explained below (*infra* n.5), *Couch 3d*, a looseleaf, was first published in 1995.

* *Partner, ReedSmith LLP, New York.*
** *Partner, Hunton Andrews Kurth LLP, Washington D.C.*
*** *Senior Counsel, Pillsbury Winthrop Shaw Pittman LLP, New York.*
**** *Associate, Plews Shadley Racher & Braun, LLP, Indianapolis.*

the meaning of "physical loss or damage"—words typically in the trigger for property-insurance coverage, including business-income coverage. It has been cited, ad nauseam, as evidence of a general consensus that all property-insurance claims require some "distinct, demonstrable, *physical alteration* of the property."[2] Indeed, some pro-insurer decisions substitute a citation to this section for an actual analysis of the specific language before the court.

Couch is generally recognized as a significant insurance treatise, and courts have cited it for almost a century.[3] That respect began with the first edition written by George Couch and subsequent editions written by his successors.

This particular section, however, as formulated in the third edition of *Couch*, contains an unfortunate, and serious, error. *Couch*'s apparent conclusion—that "direct physical loss" requires a "distinct, demonstrable, physical alteration"—is wrong. It was wrong when *Couch* first made it in the 1990s, and it is wrong today. As another well-respected treatise puts it, "when an insurance policy refers to *physical loss of or damage* to property, the 'loss of property' requirement can be satisfied by any 'detriment,' and a 'detriment' can be present *without there having been a physical alteration of the object*."[4]

A review of the three editions of *Couch* shows that this statement first appeared in the third edition.[5] As originally published, it supported its assertion by citing to five cases for support and two cases holding to the contrary, presenting the former as the "widely held" majority rule.[6]

But none of these cases used the "distinct, demonstrable, physical alteration" test that *Couch 3d* presents, and it was far from the majority rule. As of March 2020, there were at least *thirty-five* cases adopting a broader rule (including many binding appellate decisions and several rulings by state high courts), and significantly fewer following the *Couch* test. The "physical

2. *Id.* (emphasis added); Oral Surgeons, P.C. v. Cincinnati Ins. Co., 2 F.4th 1141, 1144 (8th Cir. 2021).

3. Girard Fire & Marine Ins. Co. v. Winfrey, 26 S.W.2d 701, 705 (Tex. Ct. App. 1930) (citing 4 George J. Couch, Cyclopedia of Insurance Law § 915).

4. 3 Allan D. Windt, Insurance Claims & Disputes § 11:41 (6th ed. 2013) (emphasis added).

5. The authors conducted searches in an effort to identify when this phrase first appeared in *Couch*. The authors ran searches on the first edition through HeinOnline and reviewed the hard copy of *Couch 2d* to see if those editions used this language. We found no language in either of the first two editions that was similar to that in section 148:46 of *Couch 3d* ("distinct, demonstrable, physical alteration"). *Couch 3d*, unlike *Couch 1st* and *Couch 2d*, was published in loose-leaf format. Without saving all versions of superseded pages in the updates published over the years, it is not possible at this point in time for us to say with certainty when language first appeared. We were able to verify that the first time that a court cited the "distinct, demonstrable" phrase in *Couch 3d* was in 1999. Columbiaknit, Inc. v. Affiliated FM Ins. Co., 1999 WL 619100, at *7–8 (D. Or. Aug. 4, 1999).

6. 10A Couch on Insurance 3d § 148:46. Couch added four cases to supplement this position following the original publication date.

alteration" test gained traction only because courts relied on *Couch*'s initial mischaracterization—inferred from a single district court opinion that was disapproved three years later by the governing court of appeals, rather than from the thirteen extant cases then holding to the contrary.

We may never know why *Couch* got the law so profoundly backwards on this key issue. But one thing is clear: courts need to stop citing it as the *sine qua non* of what "physical loss or damage" means. It is not. If the courts, and particularly the federal courts,[7] continue down this path without addressing *Couch*'s fallacy, there will be serious practical consequences. They risk overruling decades of insurance law and drastically narrowing the scope of property insurance that forms the backbone of risk protection for homeowners, businesses, and the banks that lend to them. All of those policies rest on the same terms *Couch* misconstrued. More immediately, courts will deprive American businesses of billions of dollars in coverage they paid for and need to survive the worst public health crisis in a century. Until *Couch* reckons with this error, busy trial and appellate judges cannot, and should not, trust it to give them the straight answer on this foundational question.

II. THE LAW OF "DIRECT PHYSICAL LOSS"

Modern property-insurance policies are triggered by some "direct physical loss or damage" to the property (or some variant of that term).[8] After this standard-form language was adopted, courts were quickly called upon to determine what it meant. Plainly it included injuries by fire, lightning, or tornado. But the breadth of the words—layered on the broad "all risk"[9] template—generated questions about whether a loss of use or function was sufficient to trigger these policies.

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7. There is a stark disparity between the way state and federal courts are treating these claims in the Covid-19 context. *Trial Court Rulings on the Merits in Business Interruption Cases*, *Covid Coverage Litigation Tracker*, U. Pa. L. Sch., https://cclt.law.upenn.edu/judicial-rulings (last viewed Oct. 9, 2021). As of this writing, state courts have heard fewer than 130 insurer motions to dismiss and have denied 32 of them. Federal courts have heard 484 motions, yet they have denied even fewer (25), with the balance finding, as a matter of law, that there is no claim. *Id.* Since federal courts are constitutionally bound to follow state insurance law under the *Erie* doctrine, this massive disparity simply should not exist. That it does may require corrective action from the U.S. Supreme Court. *See* Brief of *Amicus Curiae* United Policyholders, Mama Jo's, Inc. v. Sparta Ins. Co., No. 20-998 (U.S. Feb. 25, 2021) (raising similar concerns, though in a non-Covid case and without the benefit of current case data), *cert. denied*, 141 S. Ct. 1737 (Mar. 29, 2021).

8. 5 New Appleman on Insurance Law, Libr. Ed. § 42.02[3].

9. There are two general types of property insurance. The first is "all risk" insurance. As its name suggests, it is the broadest of all insurance products because it "creates a type of coverage not ordinarily present under other types of insurance, and recovery is allowed for all fortuitous losses unless the loss is excluded by a specific policy provision." 10A Couch on Insurance 3d § 148:50. The second is "named perils" insurance, which insures only for specified causes of loss.

From 1950 to 1990, courts uniformly found that such losses qualified. Over the insurance industry's objections at the point of claim, courts asked only whether the property was unsafe or unusable for its intended purpose. If the answer to either question was "yes," then there was "direct physical loss or damage" to the property. The contrary view—requiring "distinct, demonstrable, physical alteration"—emerged in the 1990s but was in the distinct minority. Despite this backdrop, *Couch* wrongly portrayed "physical alteration" as the "widely held" majority rule.

A. *The Original Meaning of "Physical Loss": 1950 to 1995*

Until the 1990s, courts uniformly gave "direct physical loss" and its variants their broad, ordinary meaning. That phrase included cases where property became unsafe or unusable for its intended purpose. Standard-form policies were triggered in such circumstances in the 1950s,[10] the 1960s,[11] the 1970s,[12] the 1980s,[13] and the 1990s.[14]

In 1995, the Third Edition of *Couch on Insurance* added a new section, titled "*Generally; 'Physical' loss or damage*."[15] The first case to cite this section

10. Am. Alliance Ins. Co. v. Keleket X-Ray Corp., 248 F.2d 920, 925 (6th Cir. 1957) (finding coverage when a release of radon dust and gas made the policyholders' building unsafe to work in and unusable for its purpose, which was calibrating medical instruments); Marshall Produce Co. v. St. Paul Fire & Marine Ins. Co., 98 N.W.2d 280, 295, 300 (Minn. 1959) (finding that egg powder, which had been exposed to smoke, was physically damaged because it suffered a loss of market value even without actual injury).

11. Hughes v. Potomac Ins. Co., 18 Cal. Rptr. 650, 655 (Ct. App. 1962) (finding "physical loss" because policyholder's home was unsafe for occupancy after a landslide deprived it of support); W. Fire Ins. Co. v. First Presbyterian Church, 437 P.2d 52, 54 (Colo. 1968) (en banc) (finding a "direct physical loss" where gasoline vapors made "use of the building highly dangerous").

12. Cyclops Corp. v. Home Ins. Co., 352 F. Supp. 931, 937 (W.D. Pa. 1973) (finding business-income coverage where vibration of motor, without apparent damage, caused it to be shut down).

13. Hampton Foods, Inc. v. Aetna Cas. & Sur. Co., 787 F.2d 349, 352 (8th Cir. 1986) (finding Business Income coverage where danger of collapse required abandonment of grocery store); Intermetal Mexicana, S.A. v. Ins. Co. of N. Am., 866 F.2d 71, 76 (3d Cir. 1989) (theft of property, depriving policyholder of possession and control, qualified as "direct physical loss"); Blaine Richards & Co. v. Marine Indem. Ins. Co., 635 F.2d 1051, 1055–56 (2d Cir. 1980) (finding policyholder could recover lost value of beans exposed to chemical not accepted in the United States but not actually harmed).

14. In chronological order: Hetrick v. Valley Mut. Ins Co., 1992 WL 524309, at *3 (Pa. Comm. Pl. May 28, 1992) (finding coverage for loss of use of a house if an outside oil spill made the house uninhabitable); Largent v. State Farm Fire & Cas. Co., 842 P.2d 445, 446 (Or. Ct. App. 1992) (noting insurance company conceded meth fumes could cause "direct physical loss"); Farmers Ins. Co. v. Trutanich, 858 P.2d 1332, 1335 (Or. Ct. App. 1993) (finding costs of meth odor covered as direct physical loss or damage); Azalea, Ltd. v. Am. States Ins. Co., 656 So. 2d 600, 602 (Fla. Ct. App. 1995) (chemicals that destroyed a bacteria colony necessary for sewage treatment plant to operate caused "direct damage to the structure").

15. 10A Couch on Insurance 2d § 148:46.

was decided in 1999.[16] The fourth paragraph in that section (as reprinted without relevant change in the June 2021 update) reads:

> The requirement that the loss be "physical," given the ordinary definition of that term, is widely held to exclude alleged losses that are intangible or incorporeal and, thereby, to preclude any claim against the property insurer when the insured merely suffers a detrimental economic impact unaccompanied by a *distinct*, *demonstrable*, *physical alteration of the property*.[17]

The origin of this matter-of-fact statement is puzzling. At the time this section first appeared, only one reported case had adopted this test in the circumstances relevant here—*Great Northern Ins. Co. v. Benjamin Franklin Federal Savings & Loan Ass'n*, decided by a federal district court in Oregon, in 1990.[18]

Benjamin Franklin involved the sudden discovery of non-friable (or intact) asbestos in a building.[19] The property insurer refused to pay for its removal, arguing there was no "direct physical loss."[20] The district court agreed, citing a 1978 Oregon Supreme Court case (*Wyoming Sawmills v. Transportation Ins. Co.*) finding that a lumber manufacturer's third-party liability-insurance policy did not cover a lawsuit seeking labor expenses for removing defective 2 × 4 studs from a building.[21] Despite the many cases actually addressing "direct physical loss" language in this context—and universally coming out the other way—the *Benjamin Franklin* court found this liability-insurance case "most helpful."[22] The court held that property insurance, like liability insurance, does not "include consequential or intangible damages such as depreciation in value, within the terms property damage."[23] Ignoring the distinction between first-party and third-party coverage, the court held that, since the building was "physically intact and undamaged," there was no "*physical* loss, direct or otherwise."[24]

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16. Columbiaknit, Inc. v. Affiliated FM Ins. Co., 1999 WL 619100, at *7–8 (D. Or. Aug. 4, 1999) (finding that policyholder could bear its burden to demonstrate that clothes contaminated with mold or mildew suffered "direct physical loss or damage" if it established "at trial a class of garments which has increased microbial counts and that will, as a result, develop either an odor or mold or mildew").

17. 10A Couch on Insurance 3d § 148:46 (emphasis added).

18. Great N. Ins. Co. v. Benjamin Franklin Fed. Sav. & Loan Ass'n, 793 F. Supp. 259, 263 (D. Or. 1990). There were other cases favoring insurers, but they involved (for example) claims that a title impairment was a "physical loss," which it obviously is not. Those cases are discussed in more detail below. *Benjamin Franklin* was the first to apply this rule in the context of physical effects on property.

19. *Id.* at 261.

20. *Id.* at 263.

21. *Id.* (citing Wyoming Sawmills v. Transp. Ins. Co., 578 P.2d 1253, 1256 (Or. 1978)).

22. *Id.*

23. *Id.* (quoting *Wyoming Sawmills*, 578 P.2d at 1256).

24. *Id.* (emphasis in original). Third-party and first-party insurance serve significantly different functions. Third-party insurance is essentially fault-based; it provides compensation for loss suffered by "third parties" that is caused by the policyholder's wrongful acts.

The "physically intact and undamaged" gloss was brand new in *Benjamin Franklin*. At that time, the major decisions predating it—*Hughes* and *First Presbyterian*—had rejected that precise logic. *Hughes* was particularly forceful:

> To accept [the insurer's] interpretation of its policy would be to conclude that a building which has been overturned or which has been placed in such a position as to overhang a steep cliff has not been "damaged" so long as its paint *remains intact and its walls still adhere to one another*. Despite the fact that a "dwelling building" might be rendered completely useless to its owners, [the insurer] *would deny that any loss or damage had occurred unless some tangible injury to the physical structure itself could be detected*. Common sense requires that a policy should not be so interpreted in the absence of a provision specifically limiting coverage in this manner.[25]

Similarly, *First Presbyterian* found that a church rendered too dangerous for occupancy because it was permeated with gasoline fumes had suffered a "loss of use" that triggered the policy.[26]

Perhaps because the "intact and undamaged" rule was invented by a single district judge, it did not stick. Three years after *Benjamin Franklin*, the Oregon Court of Appeals refused to follow it in *Farmers Ins. Co. v. Trutanich*, a case involving methamphetamine contamination.[27] *Trutanich* distinguished *Wyoming Sawmills* (the liability-insurance case *Benjamin Franklin* found "most helpful") and instead followed *First Presbyterian*.[28]

When *Couch 3d* cited *Benjamin Franklin* as evincing a "distinct, demonstrable, physical alteration" rule,[29] it ignored that *Trutanich* had rendered the "intact and undamaged" rule a dead letter three years earlier.[30] It also added the modifiers "distinct" and "demonstrable" out of thin air—we have found no pre-*Couch 3d* case where a court frames the test using those adjectives. In spite of this, *Couch 3d* crafted its own rule out of whole cloth, and

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First-party insurance, in contrast, provides coverage for loss regardless of fault. This distinction is important in understanding *Wyoming Sawmills*. Most commercial third-party policies have "business risk" exclusions—in *Wyoming Sawmills*, it was an exclusion for liability arising from damage to "your product" or "your work" (i.e., the defective 2 × 4s). The aim of such exclusions is to enforce the general third-party rule that coverage exists only for damage to *someone else*'s property, and so that liability insurance is not equated with a builder's "performance bond." Thus, *Wyoming Sawmills* is not properly read to require a "physical alteration" rule, even in the third-party context. Loss of use to a third party's property is indisputably "property damage" under standard-form general liability insurance.

25. Hughes v. Potomac Ins. Co., 18 Cal. Rptr. 650, 655 (Ct. App. 1962) (emphasis added).
26. W. Fire Ins. Co. v. First Presbyterian Church, 437 P.2d 52, 54 (Colo. 1968) (en banc).
27. Farmers Ins. Co. v. Trutanich, 858 P.2d 1332, 1335 (Or. Ct. App. 1993).
28. *Id.* at 1335–36.
29. 10A Couch on Insurance 3d § 148:46 (emphasis added).
30. *Trutanich*, 858 P.2d at 1335 n.4 (limiting *Benjamin Franklin* to asbestos that was "intact" and nonfriable).

then then included a paragraph, written in the passive voice, suggesting that there was only some case law to the contrary:

> The opposite result has been reached, allowing coverage based on physical damage despite the lack of physical alteration of the property, on the theory that the uninhabitability of the property was due to the fact that gasoline vapors from adjacent property had infiltrated and saturated the insured building, and the theory that the threatened physical damage to the insured building from a covered peril essentially triggers the insured's obligation to mitigate the impending loss by undertaking some hardship and expense to safeguard the insured premises.[31]

This lukewarm counterpoint cited only *First Presbyterian* and *Hampton Foods*—two of at least *thirteen* cases that had adopted the broader rule when the section was first drafted.[32]

B. *The One-Sided Portrayal Grows: 1995–2019*

Like any treatise updated regularly, *Couch 3d* over the years generally added citations as the law developed. However, a problem appeared on this issue as *Couch 3d* began discussing it—the third edition only added cases favorable to its made-up "majority" position.[33] Every one of these decisions cited *Couch 3d*'s "physical alteration" doctrine.[34] For example, under facts identical to *Benjamin Franklin*, the Third Circuit denied coverage by declaring (citing *Couch* and nothing else) that this was the "widely accepted definition."[35]

Yet this rule was neither "widely accepted" nor correct. *Couch 3d* did not address many of the significant decisions adopting the contrary and earlier generally accepted position. In fact, the only case supporting *Couch 3d*'s

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31. 10A Couch on Insurance 3d § 148:46.

32. The others are similar. *See* Marshall Produce Co. v. St. Paul Fire & Marine Ins. Co., 98 N.W.2d 280, 295, 300 (Minn. 1959) (unsalable goods); Hughes v. Potomac Ins. Co., 18 Cal. Rptr. 650, 655 (Ct. App. 1962) (erosion); Am. All. Ins. Co. v. Keleket X-Ray Corp., 248 F.2d 920, 925 (6th Cir. 1957) (radon contamination); Intermetal Mexicana, S.A. v. Ins. Co. of N. Am., 866 F.2d 71, 76 (3d Cir. 1989) (theft); Blaine Richards & Co. v. Marine Indem. Ins. Co., 635 F.2d 1051, 1055–56 (2d Cir. 1980) (unsalable goods); Cyclops Corp. v. Home Ins. Co., 352 F. Supp. 931, 937 (W.D. Pa. 1973) (inoperable motor); Hetrick v. Valley Mut. Ins Co., 1992 WL 524309, *3 (Pa. Comm. Pl. May 28, 1992) (oil spill); Largent v. State Farm Fire & Cas. Co., 842 P.2d 445, 446 (Or. Ct. App. 1992) (meth contamination); Farmers Ins. Co. v. Trutanich, 858 P.2d 1332, 1335 (Or. Ct. App. 1993) (same); Azalea, Ltd. v. Am. States Ins. Co., 656 So. 2d 600, 602 (Fla. Ct. App. 1995) (chemical contamination).

33. 10A Couch on Insurance 3d § 148:46 (adding Port Auth. of N.Y. & N.J. v. Affiliated FM Ins. Co., 311 F.3d 226, 236 (3d Cir. 2002); Universal Image Prods., Inc. v. Fed. Ins. Co., 475 F. App'x 569, 573 (6th Cir. 2012); Newman Myers Kreines Gross Harris, P.C. v. Great N. Ins. Co., 17 F. Supp. 3d 323, 331 (S.D.N.Y. 2014); MRI Healthcare Ctr. of Glendale, Inc. v. State Farm Gen. Ins. Co., 115 Cal. Rptr. 3d 27, 38 (Ct. App. 2010)).

34. *Port Authority*, 311 F.3d at 235; *Universal Image*, 475 F. App'x at 573–74; *Newman Meyers*, 17 F. Supp. 3d at 331; *MRI Healthcare*, 115 Cal. Rptr. at 778–79.

35. *Port Authority*, 311 F.3d at 235.

assertion was at the trial level, was not binding, and had been disapproved by the governing state's court of appeals. Beyond that, more and more cases began to recognize that the *Hughes* rule—and not the *Couch 3d* theory—was correct. There were five such cases (including two from state courts of last resort) before the turn of the twenty-first century.[36] *Couch 3d* to date has ignored all of them.

The law continued to snowball in policyholders' favor after that. In 2000,[37] 2001,[38] 2002,[39] 2003,[40] 2005,[41] courts rendered eleven decisions for policyholders on this issue without requiring "physical alteration." *Couch 3d*

36. Arbeiter v. Cambridge Mut. Fire Ins. Co., 1996 WL 1250616, at *2 (Mass. Super. Ct. Mar. 15, 1996) (finding oil fumes present in house after discovery of oil leak constituted physical damage to the house); Sentinel Mgmt. Co. v. N.H. Ins. Co., 563 N.W.2d 296, 300 (Minn. Ct. App. 1997) (asbestos); Dundee Mut. Ins. Co. v. Marifjeren, 587 N.W.2d 191 (N.D. 1998) (power outage causing potatoes to freeze); Murray v. State Farm Fire & Cas. Co., 509 S.E.2d 1, 16–17 (W. Va. 1998) (concluding that a home rendered dangerously unlivable by the presence of falling rocks had suffered a "direct physical loss to the property"); Matzner v. Seaco Ins. Co., 9 Mass. L. Rptr. 41, 1998 WL 566658, at *4 (Mass. Super. Ct., Aug. 12, 1998) (concluding that the phrase "direct physical loss or damage" was ambiguous and could mean either "only tangible damage to the structure of insured property" or "more than tangible damage to the structure of insured property," and that "carbon monoxide contamination constitutes 'direct physical loss of or damage to' property"); Bd. of Educ. v. Int'l Ins. Co., 720 N.E.2d 622, 625–26 (Ill. Ct. App. 1999) (citing liability insurance coverage cases finding that incorporation of asbestos into buildings caused "property damage," defined under liability policies to be "physical injury to or destruction of tangible property," and finding that policyholder had established that the asbestos fiber contamination constituted physical damage).

37. Sentinel Mgmt. Co. v. Aetna Cas. & Sur. Co., 615 N.W.2d 819, 825–26 (Minn. 2000) ("A principal function of any living space [is] to provide a safe environment for the occupants," and "[i]f rental property is contaminated by asbestos fibers and presents a health hazard to the tenants, its function is seriously impaired.").

38. Gen. Mills, Inc. v. Gold Medal Ins. Co., 622 N.W.2d 147, 152 (Minn. Ct. App. 2001) (oats rendered unsalable by FDA regulation suffered "direct physical loss").

39. Prudential Prop. & Cas. Ins. Co. v. Lillard-Roberts, 2002 WL 31495830, at *8–9 (D. Or. June 18, 2002) (concluding that mold damage to house could constitute "distinct and demonstrable" damage and that inability to inhabit a building may constitute "direct, physical loss"); Cooper v. Travelers Indem. Co. of Ill., 2002 WL 32775680, at *1 (N.D. Cal. Nov. 4, 2002) (coliform bacteria and E.coli); Graff v. Allstate Ins. Co., 54 P.3d 1266, 1269 (Wash. Ct. App. 2002) (methamphetamine vapors); Yale Univ. v. CIGNA Ins. Co., 224 F. Supp. 2d 402, 413 (D. Conn. 2002) (finding while the presence of asbestos and lead in buildings did not constitute "physical loss of or damage to property," contamination by such materials could, citing "the substantial body of case law" "in which a variety of contaminating conditions have been held to constitute 'physical loss or damage to property'").

40. S. Wallace Edwards & Sons, Inc. v. Cincinnati Ins. Co., 353 F.3d 367, 374–75 (4th Cir. 2003) (affirming finding that meat exposed to ammonia and thus less valuable even though not actually affected had suffered property damage).

41. Motorists Mut. Ins. Co. v. Hardinger, 131 F. App'x 823, 824, 826–27, 824–26 (3d Cir. 2005) (E. coli contamination); De Laurentis v. United Servs. Auto. Ass'n, 162 S.W.3d 714, 722–23 (Tex. Ct. App. 2005) (finding mold damage constituted "physical loss to property"); Pepsico, Inc. v. Winterthur Int'l Ins. Co., 24 A.D.3d 743, 744 (N.Y. App. Div., 2d Dep't 2005) (unmerchantable product); Schlamm Stone & Dolan LLP. v. Seneca Ins. Co., 800 N.Y.S.2d 356 (Sup. Ct. 2005) (finding that "the presence of noxious particles, both in the air and on surfaces of the plaintiff's premises, would constitute property damage under the terms of the policy").

took no notice. In 2007,[42] 2009,[43] and 2010,[44] courts decided eight more. Again, *Couch 3d* ignored them. Five more cases came in 2011,[45] 2013,[46] 2014,[47] 2015,[48] and 2016,[49] including from another state supreme court. None of these decisions were featured in *Couch 3d*, and even its June 2021 update failed to grapple with (or even cite) any of them.

Couch 3d may not have recognized these cases, but insurers did—when it served their purposes. In late 2019, Factory Mutual Insurance Company ("FM"), one of the largest and most sophisticated property insurers in the world, sued another insurer seeking to shift some of its liability for mold

42. Cook v. Allstate Ins. Co., 2007 Ind. Super. LEXIS 32, at *6–10 (Madison Cnty. Nov. 30, 2007) (finding that infestation of house with brown recluse spiders constituted "direct physical loss" to the house: "Case law demonstrates that a physical condition that renders property unsuitable for its intended use constitutes a 'direct physical loss' even where some utility remains and, in the case of a building, structural integrity remains"); Stack Metallurgical Servs., Inc. v. Travelers Indem. Co., 2007 WL 464715, at *8 (D. Or. Feb. 7, 2007) (finding "physical loss or damage" where the policyholder's heat treater for medical implants was contaminated by lead and could no longer be used); Fed. Ins. Co. v. Hartford Steam Boiler Inspection & Ins. Co., 2007 WL 1007787, at *12 (E.D. Mich. Mar. 31, 2007) (finding that food in cardboard containers exposed to ammonia was physically injured, despite the fact the food was judged fit to eat).

43. Essex v. BloomSouth Flooring Corp., 562 F.3d 399, 406 (1st Cir. 2009) (unpleasant odor in home); Wakefern Food Corp. v. Liberty Mut. Fire Ins. Co., 968 A.2d 724, 734 (N.J. Super. App. Div. 2009) ("In the context of this case, the electrical grid was 'physically damaged' because, due to a physical incident or series of incidents, the grid and its component generators and transmission lines were physically incapable of performing their essential function of providing electricity."); Manpower Inc. v. Ins. Co. of the State of Pa., 2009 WL 3738099, at *1 (E.D. Wis. Nov. 3, 2009) (finding "direct physical loss . . . or damage to" a building adjacent to a building which collapsed despite the fact that the collapse did not cause any noticeable damage to the policyholder's occupied space).

44. Travco Ins. Co. v. Ward, 715 F. Supp. 2d 699, 707–08 (E.D. Va. 2010) (finding that drywall emitting toxic gases, causing the policyholder to move out, caused a direct physical loss, despite the fact that it was "physically intact, functional and ha[d] no visible damage," noting the majority of cases nationwide find that "physical damage to the property is not necessary"); *In re* Chinese Mfr'd Drywall Prods. Liab. Litig., 759 F. Supp. 2d 822, 831 (E.D. La. 2010) (finding that "the presence of Chinese-manufactured drywall in a home constitutes a physical loss" because it "renders the [policyholders'] homes useless and/or uninhabitable").

45. Widder v. La. Citizens Prop. Ins. Corp., 82 So.3d 294 (La. Ct. App. 2011) (lead).

46. Ass'n of Apartment Owners of Imperial Plaza v. Fireman's Fund Ins. Co., 939 F. Supp. 2d 1059, 1068 (D. Haw. 2013) (finding that intrusion of arsenic into roof caused "direct physical loss or damage" to the roof).

47. Gregory Packaging, Inc. v. Travelers Prop. Cas. Co., 2014 WL 6675934, at *5–6 (D.N.J. Nov. 25, 2014) (concluding that "property can sustain physical loss or damage without experiencing structural alteration," that "the heightened ammonia levels rendered the facility unfit for occupancy until the ammonia could be dissipated," and therefore that the ammonia discharge caused direct physical loss).

48. Mellin v. N. Sec. Ins. Co., 115 A.3d 799, 806 (N.H. 2015) (rejecting "tangible alteration" rule and holding that pervasive odor of cat urine was "physical loss" to condominium).

49. Oregon Shakespeare Festival Ass'n v. Great Am. Ins. Co., 2016 WL 3267247, at *5–6 (D. Or. June 7, 2016), *vacated by joint stipulation*, 2017 WL 1034203 (Mar. 6, 2017) (smoke from wildfires, making operations hazardous to human health, caused a "direct physical loss").

and mold spore contamination at a biopharmaceuticals lab.[50] In the case, it brought a motion *in limine* contending that "physical loss or damage" to property exists when a physical substance renders property unfit for its intended use, despite that there was *no* physical alteration.[51] Citing cases like *First Presbyterian*, *Gregory Packaging*, and *Trutanich*, FM argued to the Court:

> Numerous courts have concluded that loss of functionality or reliability under similar circumstances constitutes physical loss or damage. *See*, *e.g.*, *Western Fire Insurance Co. v. First Presbyterian Church*, 437 P.2d 52 (Colo. 1968) (church building sustained physical loss or damage when it was rendered uninhabitable and dangerous due to gasoline under the building); *Gregory Packaging, Inc. v. Travelers Property and Casualty Company of America*, Civ. No. 2:12-cv-04418, 2014 U.S. Dist. LEXIS 165232, 2014 WL 6675934 (D. N.J. 2014) (unsafe levels of ammonia in the air inflicted "direct physical loss of or damage to" the juice packing facility "because the ammonia physically rendered the facility unusable for a period of time."); *Port Authority of N.Y. and N.J. v. Affiliated FM Ins. Co.*, 311 F.3d 226, 236 (3d Cir. 2002) (asbestos fibers); *Essex v. BloomSouth Flooring Corp.*, 562 F.3d 399, 406 (1st Cir. 2009) (unpleasant odor in home); *TRAVCO Ins. Co. v. Ward*, 715 F. Supp. 2d 699, 709 (E.D. Va. 2010), *aff'd*, 504 F. App'x 251 (4th Cir. 2013) ("toxic gases" released by defective drywall).[52]

Moreover, FM argued that, *at worst*, it had put forward a reasonable interpretation of the undefined phrase "physical loss or damage"—and even if Federal could propose a reasonable reading, this merely rendered the subject policy ambiguous and required the court to construe it in favor of coverage.[53]

The oddity and error in *Couch 3d*'s statement is further shown by other major insurance-coverage treatises. Allan Windt's *Insurance Claims & Disputes* (6th ed. 2013) is most explicit: "[W]hen an insurance policy refers to physical loss of or damage to property, the 'loss of property' requirement can be satisfied by *any* 'detriment,' and a 'detriment' can be present *without there having been a physical alteration of the object*."[54] Windt then proceeds to discuss the major cases that *Couch 3d* ignores, including *Murray*, *Sentinel*, and *Hardinger*.[55]

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50. Factory Mut. Ins. Co. v. Fed. Ins. Co., 1:17-cv-00760-GJF-LF, 2019 U.S. Dist. LEXIS 191769 (D.N.M. Nov. 5, 2019).

51. Motion *in Limine* No. 5 re Physical Loss or Damage at 3, *Factory Mut. Ins. Co.*, filed Nov. 19, 2019, ECF#127, https://3inbm04c0p4j2h1w132uyb5e-wpengine.netdna-ssl.com/wp-content/uploads/2021/02/fm_v._federal.pdf.

52. *Id.* at 3–4 (emphasis added).

53. *See id.* at 3 n.1.

54. 3 Allan D. Windt, Insurance Claims & Disputes § 11:41 (6th ed. 2013) (emphasis added).

55. *Id.*

Appleman's *Insurance Law and Practice*, often cited side-by-side with *Couch*, contains a similar statement of the standard in its section on "all risk" insurance.[56] After discussing *First Presbyterian*, it concluded that "[t]he courts have construed the scope of what constitutes 'physical loss or damage' liberally," while still recognizing that some losses (such as a withdrawn warranty) were not "physical."[57] At the time it was discontinued, in favor of the *New Appleman* series, the "Old" *Appleman* recognized all, or nearly all, of the seminal decisions on "physical loss" that *Couch* omitted. Those cases include dispossession of property (*Intermetal Mexicana*), "unusable or uninhabitable" property (*Murray*), and contamination (*Board of Education*).[58]

The 1999 update to another treatise by Peter J. Kalis reaches the same conclusion.[59] Explaining that "direct" and "physical" loss or damage is the coverage trigger for property insurance, the authors correctly summarized the law at the time by saying that disputes over these words "generally have

56. 5 John Alan Appleman & Jean Appleman, Insurance Law & Practice 2d § 3092 (1970 & 2012 Supp.), *reprinted in* 5f-142f Appleman on Insurance Law & Practice Archive § 3092 (LEXIS 2011). *Appleman*, like *Couch*, is a venerable treatise, used for decades by coverage practitioners including authors of this article. The "Original" *Appleman*, first published in 1929, was updated for years after the death in 1936 of the original author, John Alan Appleman. The hard copy volume of the "original" *Appleman* containing § 3092 was last copyrighted in 1970 and thereafter was updated through pocket parts. From the authors' knowledge and research on provenance of this section, the last "cumulative supplement" for this volume (volume 5) of "Old" *Appleman* was copyrighted in 2012. The "original" *Appleman* was joined by a successor, *New Appleman*, in the last two decades, which overlapped with original *Appleman* and was called first *Holmes Appleman on Insurance* and later *Appleman on Insurance 2d*. The publisher also published *New Appleman on Insurance Law*, *Law Library Edition* (Jeffrey E. Thomas & Francis J. Mootz, III, eds., Lexis-Nexis 2009 & Dec. 2020 Supp.); and most recently, *New Appleman Insurance Law Practice Guide* (Leo P. Martinez, Marc S. Mayerson & Douglas R. Richmond eds., Lexis-Nexis 2020). *Appleman on Insurance 2d*, for example, while focusing on many issues of import in insurance law, includes little analysis of the relevant policy language in consideration in this article.

57. *Id.*

58. *Id.* The *New Appleman* successor to this work, rather than carrying forward the existing research, borrowed heavily from *Couch 3d*'s misstatement of the rule—down to the cases *Couch 3d* cited and some of the descriptive words *Couch 3d* used. 5 New Appleman on Insurance Law, Libr. Ed., § 46.03[2] (offering the "generally prevailing" rule as one that "preclude[s] coverage for losses that are solely intangible or incorporeal; for example, an economic loss unaccompanied by a distinct physical alteration to property"). To the *New Appleman* authors' credit, their statements are more restrained, and (unlike *Couch 3d*) they do follow this introduction with treatments of important cases like *Trutanich*, *Sentinel*, *Hardinger*, *Pepsico*, *General Mills*, and *Wakefern*, discussed throughout this article. *Id.* § 46.03[3] ("Contamination by Vapor, Bacteria, or other Foreign Substance," "Intact Property Rendered Unfit for Intended Purpose," "Destruction or Corruption of Electronic Data," and "Deprivation of Access by Government Authorities"). Although *New Appleman*'s decision to borrow its summary from *Couch 3d* was ill-advised, the balance of the section—and the nuance it explains—illustrates the severity of *Couch 3d*'s error.

59. I Peter J. Kalis, Thomas M. Reiter & James R. Segerdahl, Policyholder's Guide to the Law of Insurance Coverage § 13.04 (Aspen L. & Bus., Supp. 1999). As the name of this treatise suggests, its authors generally represented policyholders. But unlike this section of *Couch*, the discussion is balanced and accurately represents the case law.

been resolved in favor of coverage."[60] It then proceeds to discuss *Hampton Foods*, *First Presbyterian*, *Hughes*, and *Intermetal Mexicana*, among other cases, as representing the majority rule.[61] It acknowledged *Benjamin Franklin* but noted that it was an outlier.[62] It concluded that while insurers may argue for a more stringent version of "physical loss," "[t]hese arguments have generally been unsuccessful if the loss arises out of some external event or condition changing and devaluing the property."[63] In 2013, the principal author of *Couch 3d*, Steven Plitt, published an article in an insurance industry magazine entitled "Direct Physical Loss in All-Risk Policies: The Modern Trend Does Not Require Specific Physical Damage, Alteration."[64] He discussed recent case law and concluded that the "modern trend" is that "courts are not looking for physical alteration, but for loss of use." It is unclear why the current 2021 update of *Couch 3d* does not match its principal author's stated understanding of the law.

For whatever reason, this robust body of scholarship—all contrary to *Couch 3d*—has not caught the courts' attention. That is unfortunate. Windt, Appelman, and Kalis present a far superior resource for courts interested in understanding the full scope of the law, rather than *Couch 3d*'s truncated, one-sided version.

C. Couch 3d*'s 2021 Update Has Not Remedied This Significant Error*

In 2021, *Couch 3d* updated this section. The current edition repeats the error of the previous ones.

For the proposition that its "physical alteration" rule is "widely held," *Couch 3d* currently cites seven cases—none of which were decided in 1995, when it appears that *Couch 3d* first made this statement. Moreover, nearly all of these cases *themselves cite Couch 3d* (or cases citing *Couch 3d*) for this proposition.[65] This is a remarkable feat: state *ipse dixit* you wish was true, convince courts to cite it, and then cite *those* cases as establishing that the rule is "widely held."

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60. *Id.*
61. *Id.* at 13-15 to 13-18.
62. *Id.* at 13-18 to 13-19.
63. *Id.* at 13-19.
64. Steven Plitt, *Direct Physical Loss in All-Risk Policies: The Modern Trend Does Not Require Specific Physical Damage, Alteration*, Claims J. (Apr. 15, 2013) (https://amp.claimsjournal.com/magazines/idea-exchange/2013/04/15/226666.htm) (discussing *Murray* and *Trutanich*, among other cases).
65. Port Auth. of N.Y. & N.J. v. Affiliated FM Ins. Co., 311 F.3d 226, 236 (3d Cir. 2002); Universal Image Prods., Inc. v. Fed. Ins. Co., 475 F. App'x 569, 573 (6th Cir. 2012); Newman Myers Kreines Gross Harris, P.C. v. Great N. Ins. Co., 17 F. Supp. 3d 323, 331 (S.D.N.Y. 2014); *In re* Chinese Mfd. Drywall Prods. Liab. Litig., 759 F. Supp. 2d 822, 831 (E.D. La. 2010); MRI Healthcare Ctr. of Glendale, Inc. v. State Farm Gen. Ins. Co., 115 Cal. Rptr. 3d 27, 38 (Ct. App. 2010); Welton Enters., Inc. v. Cincinnati Ins. Co., 131 F. Supp. 3d 827 (W.D. Wis. 2015); Shirley v. Allstate Ins. Co., 392 F. Supp. 3d 1185 (S.D. Cal. 2019).

For its claim that there must be a "distinct, demonstrable, physical alteration of the property," *Couch 3d* now cites five cases extant in 1995 (*Benjamin Franklin* and four others).[66] None of these pre-1995 cases cure *Couch 3d*'s original error. Nor do they offer support for the way courts are citing this section in Covid-19 cases.

For example, in the oldest case (*Cleland Simpson*) the Pennsylvania Supreme Court summarily affirmed the lower court's decision.[67] That case, however, involved a *named perils* policy for "all direct loss by fire [and] lightning."[68] The court held that an order of civil authority was not covered in the absence of fire or lightning damage.[69] In the context of a named-perils property-insurance policy, that made perfect sense: without a loss caused by an insured peril, there is no coverage. But the use of "physical loss" in an *all* risk policy is entirely different, because *all* (nonexcluded) perils are insured. *Cleland Simpson* fails to support *Couch*'s proposition at all.

In the next two cases (*Sponholz* and *HRG*) the courts held that a defect in the title to property was not a "physical loss."[70] That too, makes sense, but fails to support a "physical alteration" requirement. Title defects are *legal* injuries, not physical ones, and these cases are perfectly reconcilable with the loss-of-safe-use rule from *Hughes* and *First Presbyterian*, neither of which required "physical alteration."

The final case from this group of pre-1995 cases (*Covert*) involved products that were discarded because the manufacturer had rescinded its warranty.[71] The policyholder would not sell them without the warranty. This case comes the closest to supporting *Couch 3d*'s argument, but it still fails. As in the title-defect cases, the defect was legal or contractual (i.e., the manufacturer would not indemnify the seller from potential product defects). However, that can still be squared with the prevailing loss-of-safe-use and loss-of-function rules.[72] These cases did not support the rule *Couch 3d* derived from them.

In sum, *Couch 3d* seized on a single trial-level case with no support in the appellate law, asserted in the first instance that such a rule was "widely

66. Great N. Ins. Co. v. Benjamin Franklin Fed. Sav. & Loan Ass'n, 793 F. Supp. 259, 263 (D. Or. 1990) (asbestos), *disapproved by* Farmers Ins. Co. v. Trutanich, 858 P.2d 1332 (Or. Ct. App. 1993); Comm. Union Ins. Co. v. Sponholz, 866 F.2d 1162, 1162 (9th Cir. 1989) (title defect); HRG Dev. Co. v. Graphic Arts Mut. Ins. Co., 527 N.E.2d 1179, 1181 (Mass. Ct. App. 1988) (title defect); Cleland Simpson Co. v. Fireman's Ins. Co. of Newark, 140 A.2d 41, 44 (Pa. 1958) (named-perils coverage); Glens Falls Ins. Co. v. Covert, 526 S.W.2d 222, 223 (Tex. Ct. App. 1975) (products lacking manufacturer's warranty).

67. *Cleland Simpson*, 140 A.2d at 44.

68. Cleland Simpson Co. v. Fireman's Ins. Co., 1957 Pa. Dist. & Cnty. LEXIS 202, at *5 (Lackawanna Cnty. Jan. 11, 1957).

69. *Id.* at *8.

70. *Sponholz*, 866 F.2d at 1162; *HRG*, 527 N.E.2d at 1181.

71. *Covert*, 526 S.W.2d at 223.

72. *See supra* notes 10–13 and accompanying text.

held," did not confess error when that case was disapproved, convinced courts to cite it as authoritative, and then cited *those* cases as showing that its scantly supported test was correct. That circular process does not create sound jurisprudence, it is not persuasive, and it should not be followed any further.

D. *The Current Majority of Covid-19 Cases Adopt and Perpetuate* Couch 3d*'s Error*

To any objective observer, *Couch 3d*'s treatment of this issue is incorrect and unnerving. Despite this, a large number of courts are relying upon it to dismiss claims that the presence of SARS-CoV-2, the Covid-19 pandemic, and/or the associated orders of Civil Authority cause "physical loss or damage" to property. The result of these decisions is that many businesses—entitled to business-income coverage under the *actual* majority rule—are not receiving it.

At least twenty-eight of the early pandemic decisions ruling for insurers expressly rely on this section.[73] Another fifteen cases applied *Couch 3d*'s

73. E.g., Brunswick Panini's LLC v. Zurich Am. Ins. Co., 2021 WL 663675, at *8 (N.D. Ohio Feb. 19, 2021) (Ohio law); Kahn v. Pa. Nat'l Mut. Cas. Ins. Co., 2021 WL 422607, at *5 (M.D. Pa. Feb. 8, 2021) (Pennsylvania law); Wellness Eatery La Jolla LLC v. Hanover Ins. Grp., 2021 WL 389215, at *5 (S.D. Cal. Feb. 3, 2021) (California law); Frank Van's Auto. Tag, LLC v. Selective Ins. Co., 2021 WL 289547, at *5 (E.D. Pa. Jan. 28, 2021) (Pennsylvania law); Graspa Consulting, Inc. v. United Nat'l Ins. Co., 2021 WL 199980, at *5 (S.D. Fla. Jan. 20, 2021) (Florida law); 1 S.A.N.T., Inc. v. Berkshire Hathaway, Inc., 2021 WL 147139, at *6 (W.D. Pa. Jan. 15, 2021) (Pennsylvania law); Zagafen Bala, LLC v. Twin City Fire Ins. Co., 2021 WL 131657, at *4 (E.D. Pa. Jan. 14, 2021) (Pennsylvania law); TAQ Willow Grove, LLC v. Twin City Fire Ins., 2021 WL 131555, at *4 (E.D. Pa. Jan. 14, 2021) (Pennsylvania law); Ultimate Hearing Sols. II, LLC v. Twin City Fire Ins. Co., 2021 WL 131556, at *5 (E.D. Pa. Jan. 14, 2021) (Pennsylvania law); Moody v. Hartford Fin. Grp., Inc., 2021 WL 135897, at *4 (E.D. Pa. Jan. 14, 2021) (Pennsylvania law); ATCM Optical, Inc. v. Twin City Ins. Co., 2021 WL 131282, at *4 (E.D. Pa. Jan. 14, 2021) (Pennsylvania law); Indep. Rest. Grp. v. Certain Underwriters at Lloyd's, London, 2021 WL 131339, at *5 (E.D. Pa. Jan. 14, 2021) (Pennsylvania law); Santo's Italian Café LLC v. Acuity Ins. Co., 508 F. Supp. 3d 186, 197–98 (N.D. Ohio 2020) (Ohio law); Newchops Rest. Comcast LLC v. Admiral Indem. Co., 507 F. Supp. 3d 616, 623–24 (E.D. Pa. 2020) (Pennsylvania law); Terry Black's Barbecue, LLC v. State Auto. Mut. Ins. Co., 2020 WL 7351246, at *5 (W.D. Tex. Dec. 14, 2020) (Texas law); Richard Kirsch, DDS v. Aspen Am. Ins. Co., 507 F. Supp. 3d 835, 839 (E.D. Mich. 2020) (Michigan law); SA Palm Beach LLC v. Certain Underwriters at Lloyd's, London, 506 F. Supp. 3d 1248, 1253 (S.D. Fla. 2020) (Florida law); El Novillo Rest. v. Certain Underwriters at Lloyd's, London, 505 F. Supp. 3d 1343, 1349 (S.D. Fla. 2020) (Florida law); Hajer v. Ohio Sec. Ins. Co., 505 F. Supp. 3d 646, 650 (E.D. Tex. 2020) (Texas law); Promotional Headwear Int'l v. Cincinnati Ins. Co., 504 F. Supp. 3d 1191, 1198 n.38 (D. Kan. 2020); S. Fla. Ent. Assocs., Inc. v. Hartford Fire Ins. Co., 2020 WL 6864560, at *6 (S.D. Fla. Nov. 13, 2020) (Florida law); Dab Dental PLLC v. Main St. Am. Prot. Ins. Co., 2020 WL 7137138, at *5 (Fla. Cir. Ct. Hillsborough Cnty. Nov. 10, 2020); Hillcrest Optical, Inc. v. Cont'l Cas. Co., 497 F. Supp. 3d 1203, 1211 & n.4 (S.D. Ala. 2020) (Alabama law); Plan Check Downtown III, LLC v. AmGuard Ins. Co., 485 F. Supp. 3d 1225, 1229 (C.D. Cal. 2020) (California law); Malaube, LLC v. Greenwich Ins. Co., 2020 WL 5051581, at *5 (S.D. Fla. Aug. 26, 2020) (Florida law); Diesel Barbershop, LLC v. State Farm Lloyds, 479 F. Supp. 3d 353, 360 (W.D. Tex. 2020) (Texas law); Visconti Bus. Serv., LLC v. Utica Nat'l Ins. Grp., 71 Misc. 3d 516, 528 (N.Y. Super. Ct. 2021).

"distinct, demonstrable, physical alteration" rule without citing it directly.[74] And the first three published appellate decisions on this issue cite the section as authoritative.[75]

III. THINKING CRITICALLY ABOUT *COUCH* AND PROPERTY INSURANCE LAW

Whatever the ultimate outcome of the Covid-19 business-income-coverage litigation, the courts' treatment of this section in *Couch 3d* will have profound impacts on property-insurance coverage. The error originating from that section is poised to reshape insurance law without the rigorous intellectual analysis of a state appellate court charged with determining the law in its jurisdiction. If courts continue to blindly follow *Couch 3d* on this point, they will effectively overrule decades of property-insurance law without grappling with *stare decisis* or the usual stabilizing principles attached to precedent. Courts must dismantle *Couch 3d*'s fallacy, and the cases it has spawned, before it is too late—and, above all, stop citing *Couch 3d* on this point until the authors address the problem. We offer three general reasons for this position.

First, this section of *Couch 3d* never provides a precedent-driven or intellectual justification for its test (for it is, in reality, a test *Couch 3d* invented). Generally, when staking a position that rests at the core of a body of law, a treatise will either (a) rely on the reasoned decisions of then-extant judicial decisions to justify the rule, or (b) develop its own, independent reason that the rule is correct. *Couch 3d* does neither. This oversight is having

74. Café La Troya LLC v. Aspen Spec. Ins. Co., 2021 WL 602585, at *7 (S.D. Fla. Feb. 16, 2021) (Florida law); Vandalay Hosp. Grp. LP v. Cincinnati Ins. Co., 2021 WL 462105, at *1 (N.D. Tex. Feb. 9, 2021) (Texas law); Protégé Rest. Partners LLC v. Sentinel Ins. Co., 2021 WL 428653, at *4 (N.D. Cal. Feb. 8, 2021) (California law); Colgan v. Sentinel Ins. Co., 2021 WL 472961, at *3 (N.D. Cal. Jan. 26, 2021) (California law); Ba Lax, LLC v. Hartford Fire Ins. Co., 2021 WL 144248, at *3 (C.D. Cal. Jan. 12, 2021) (California law); O'Brien Sales & Mktg, Inc. v. Transp. Ins. Co., 2021 WL 105772, at *3–4 (N.D. Cal. Jan. 12, 2021) (California law); Humans & Resources, LLC v. Firstline Nat'l Ins. Co., 2021 WL 75775, at *5 (E.D. Pa. Jan. 8, 2021) (Pennsylvania law); Karen Trinh, DDS, Inc. v. State Farm Gen. Ins. Co., 2020 WL 7696080, at *4 (N.D. Cal. Dec. 28, 2020) (California law); Mortar & Pestle Corp. v. Atain Spec. Ins. Co., 2020 WL 7495180, at *3 (N.D. Cal. Dec. 21, 2020) (California law); Kessler Dental Assocs., P.C. v. Dentists Ins. Co., 505 F. Supp. 3d 474, 480 (E.D. Pa. 2020) (Pennsylvania law); Long Affair Carpet & Rug, Inc. v. Liberty Mut. Ins. Co., 500 F. Supp. 3d 1075, 1078 (C.D. Cal. 2020) (California law); Brian Handel D.M.D., P.C. v. Allstate Ins. Co., 499 F. Supp. 3d 95, 99 (E.D. Pa. 2020) (Pennsylvania law); Uncork & Create LLC v. Cincinnati Ins. Co., 498 F. Supp. 3d 878, 883 (S.D. W. Va. 2020) (West Virginia law); Mudpie, Inc. v. Travelers Cas. Ins. Co., 487 F. Supp. 3d 834, 839 (N.D. Cal. 2020) (California law); Pappy's Barber Shops, Inc. v. Farmers Group, Inc., 487 F. Supp. 3d 937, 944 (S.D. Cal. 2020) (California law); 10e, LLC v. Travelers Indem. Co., 483 F. Supp. 3d 828, 836 (C.D. Cal. 2020) (California law).

75. Oral Surgeons, P.C. v. Cincinnati Ins. Co., 2 F.4th 1141 (8th Cir. 2021); Mudpie, Inc. v. Travelers Cas. Ins. Co. of Am., __ F.4th __, 2021 WL 4486509 (9th Cir. Oct. 1, 2021); Santo's Italian Cafe, LLC v. Acuity Ins. Co., __ F.4th __, 2021 WL 4304607 (6th Cir. Sept. 22, 2021).

devastating consequences for businesses struggling to survive the Covid-19 pandemic, and it will have even greater consequences for the homeowners and lenders who purchase property insurance on a daily basis.

The *Couch 3d* test is largely circular. It does not flow from any substantial body of insurance law that existed (or that currently exists) outside of *Couch 3d*'s own sphere of influence. Nor is it compelling on its own. Property policies generally cover "direct physical loss or damage," which does not unmistakably communicate *Couch 3d*'s rule to an ordinary person. Perhaps insurers view "physical" as a term of art that means a "distinct, demonstrable, physical alteration." But they have not *communicated* that intent in the policy by actually defining "physical loss or damage," as courts have "begged" them to do for decades.[76]

Basic textual analysis shows why the opposite rule is correct. When property is stolen, unusable, unsafe, or nonfunctional, the policyholder has suffered a "physical loss." This comports with the distinction between "loss"[77] and "damage,"[78] two words with different meanings in the English language. If "physical" required some "distinct, demonstrable, physical alteration," then "physical loss" would be rendered meaningless.

The word "physical" simply restricts coverage to losses that are "of or relating to natural or material things, as opposed to things mental, moral, spiritual, or imaginary."[79] This draws the same line as pre-1995 decisions favoring policyholders (involving physically unsafe, physically unusable, or physically contaminated property) and pre-1995 cases favoring insurers (involving title insurance and voided warranties). An impaired title or an invalid warranty is a *legal* loss. It injures a legal right appurtenant to the

76. Cherokee Nation v. Lexington Ins. Co., 2021 WL 506271, at *3–6 (Okla. Dist., Cherokee Cnty. Jan. 28, 2021).

77. "[T]he act or fact of losing : failure to keep possession : deprivation." *Loss*, Webster's Third New Int'l Dictionary 1338 (Unabridged ed. 1966) [hereinafter Webster's]; *Loss*, I The Compact Edition of the Oxford English Dictionary 1666 (2d ed. 1986) [hereinafter Oxford's] ("**2.a.** The being deprived of, or the failure to keep (a possession, appurtenance, right . . . or the like). . . . **5.** Diminution of one's possessions or advantages; detriment or disadvantage involved in being deprived of something."); *Loss*, Merriam-Webster Online Dictionary, www.merriam-webster.com/dictionary/loss (last visited Sept. 1, 2021) ("2.a(2) the partial or complete deterioration or absence of a physical capability or function"); *Loss*, Dictionary.com, www.dictionary.com/browse/loss (last visited Sept. 1, 2021) ("1. detriment, disadvantage, or deprivation from failure to keep, have, or get").

78. "[L]oss due to injury : injury or harm to person, property, or reputation : hurt, harm." *Damage*, Webster's, *supra* note 77, at 571; *Damage*, I Oxford's, *supra* note 77, at 641 ("**2.** Injury, harm ; *esp.* physical injury to a thing."); *Damage*, Merriam-Webster Online Dictionary, *supra* note 77 ("[L]oss or harm resulting from injury to person, property, or reputation."); *Damage*, Dictionary.com, *supra* note 77 ("injury or harm that reduces value or usefulness").

79. *Physical*, Webster's, *supra* note 77, at 1706; *see Physical*, The American Heritage Dictionary of the English Language 1331 (5th ed. 2011) (same); II Oxford's, *supra* note 77, at 2161 ("Of or pertaining to material nature . . . as opposed to *psychical*, *mental*, *spiritual*"); *Physical*, Merriam-Webster Online Dictionary, *supra* note 77 ("of or relating to material things"); *Physical*, Dictionary.com, *supra* note 77 ("of or relating to that which is material").

property, and does not impair the property itself. Thus, *Couch 3d* is correct in observing that the term "physical loss" excludes losses "that are intangible or incorporeal," such as a defect in title.[80] But that statement, true as it is, does not support *Couch 3d*'s blanket "physical alteration" test. It simply illustrates one kind of "loss" that property insurance does not cover.

As the title-insurance litigation shows, the word "physical" exists in the policy for a good reason. English speakers often use the word "loss" in the mental, moral, spiritual, or imaginary sense. We speak of a "loss of reputation," a "loss of affection," or even (as John Milton wrote) a world in a state of "utter loss" and in need of divine intervention.[81] Or, in another direction, the unwitting purchaser of a house "widely reputed to be possessed by poltergeists" might have made a claim on his property insurer for a "loss," had the New York Appellate Division not excused him from the purchase by holding the seller "is estopped to deny their existence and, as a matter of law, the house is haunted."[82] In contrast to property overrun by chemicals[83] or spiders,[84] a house possessed by ghosts would seem to be the prototypical example of an "incorporeal," and thus a "nonphysical," loss.

However, this discussion of ghosts, titles, and damnation simply shows that the traditional analysis—supported by the decades of case law predating this section of *Couch 3d*—is not outlandish at all. A property perched on a cliff, inundated with gasoline, unusable due to odors or bacteria, or in danger of a rockfall is at risk due to the laws of the physical realm, not of perils legal or paranormal. *Couch 3d*'s rule erases this important distinction.

Second, the pre-*Couch* rule has a firm basis in the risk-based nature of insurance, in basic principles of insurance law, and in insurance-industry intent. Actuaries can predict the likelihood of physical phenomena that might affect property, even if those perils do not alter or structurally injure property, and even if the peril strikes the entire risk pool at the same time.[85] They can set appropriate premiums. But more difficult (or impossible) to predict, in advance, is the risk that décor will go out of style, that a house will be deemed haunted as a matter of law, or that a market meltdown will impair property values.

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80. 10A Couch on Insurance 3d § 148:46.

81. *Loss*, I Oxford's, *supra* note 77, at 1666.

82. Stambovsky v. Ackley, 169 A.D.2d 254, 255–56 (N.Y. App. Div., 1st Dep't 1991).

83. Gregory Packaging, Inc. v. Travelers Prop. Cas. Co., 2014 WL 6675934, at *5–6 (D.N.J. Nov. 25, 2014).

84. Cook v. Allstate Ins. Co., 2007 Ind. Super. LEXIS 32, at *6–10 (Madison Cnty. Nov. 30, 2007).

85. Erik S. Knutsen & Jeffrey W. Stempel, *Infected Judgment: Problematic Rush to Conventional Wisdom and Insurance Coverage Denial in a Pandemic*, 27 Conn. Ins. L.J. 185, 194–95 (2020) (explaining that pandemic losses are "insurable in theory because the timing of the pandemic itself is a fortuitous event," because "not all industries will be affected at the same time and to the same degree," and because some portions of the risk pool "may profit from the pandemic in their specific industries and may have no loss at all").

Thus, the traditional distinction between physical and nonphysical losses matches up neatly with risks that insurers can price, predict, and guard against. *Couch 3d*'s test draws the line much further upstream, leaving homeowners, businesses, and lenders exposed to large swaths of perfectly insurable risks. That fact provides ample reason to doubt *Couch 3d*'s argument that insurers drew the line there.

The more likely explanation is that "physical loss" is what the *Restatement (Second) of Contracts* calls a "deliberately obscure" term.[86] It is broad enough to let insurers charge "all risk" premiums, but ambiguous enough so the insurer can "decide at a later date what meaning to assert,"[87] i.e., a narrower, "physical alteration" rule.[88] This is illustrated by the industry's acts of playing both sides of the "physical loss" question—restrictive when it faces the policyholder, and expansive when it faces another insurer to whom it might shift liability.[89] As the *Restatement of the Law*, *Liability Insurance* points out, this is the definition of ambiguity: when "there is more than one meaning to which the language of the term is reasonably susceptible when applied to the facts of the claim."[90] If the insurance industry interprets the language both ways, surely both readings must be reasonable. But it is in these situations that both *Restatements* and every jurisdiction in the country calls for words to be construed against the drafter.[91]

Third, property insurance is one of the least negotiable types of insurance. Millions of homeowners are required, by their lenders, to maintain insurance on mortgaged property. Homeowners lack the kind of leverage that a multinational company would have to negotiate manuscript commercial-property coverage. They must have it, and due to insurers' antitrust immunity, they have no power to negotiate the terms of the policy. Yet they (and the banks that hold their mortgages) would be among the ones who suffer the most if *Couch 3d*'s rule actually becomes "widely held."

Homeowners' policies, like commercial property policies, are written on "physical loss" forms. If property insurance is construed as *Couch 3d* (incorrectly) suggests, the courts will unwittingly shift an enormous body of risks

86. Restatement (Second) of Contracts § 206, cmt. a (Am. L. Inst. 1981).

87. *Id.*

88. This is far from speculation. One writer recounts the story of an "experienced policy underwriter justifying an ambiguous draft policy as follows: 'We draft them this way so we can say later that the policy means whatever we want it to mean.'" George M. Plews & Donna C. Marron, *Survey: Environmental Law Developments: Hope and Ambiguity in Achieving the Optimum Environment*, 37 Ind. L. Rev. 1055, 1058–59 (2004).

89. *See supra* notes 50–53 and accompanying text.

90. Restatement of the Law, Liability Insurance § 4(1) (Am. L. Inst. 2019).

91. Restatement (Second) of Contracts, *supra* note 86, § 206, cmt. a. The *Restatement of the Law*, *Liability Insurance* provides for the same outcome, for the same reasons. Restatement of the Law, Liability Insurance, *supra* note 90, § 4(2), *see id.* §§ 3(3), (4), cmt. d ("The *contra proferentem* rule gives the supplier of the terms the incentive to take all reasonable steps to eliminate ambiguity in the drafting of terms.").

back on consumers and financial institutions. Homes condemned due to contamination, health hazards, or nearby natural perils could suddenly lack coverage. And if there are outstanding mortgages on those homes, the loss would be borne by the homeowner (saddled with five-or-six-figure debt or an additional mortgage payment) or the lender (unable to sell foreclosed property for anywhere near its mortgaged value). Given the long-term nature of these arrangements, blindly following *Couch* threatens to upend the law mid-stream and throw these reliance interests into disarray.

IV. CONCLUSION

The current Covid-19 coverage litigation is important in its own right. However, it is also a test of the courts' ability to be curious, thorough, and prudent in the way they resolve disputes. There is no substitute for a court's thorough review and analysis of the actual language before it and the actual law governing that language. Consulting a treatise is helpful. But they are only aids in legal analysis and can, as we have shown, be grievously wrong.

This particular section of *Couch 3d* does not aid courts whatsoever in their efforts to faithfully apply the law. Not only does it get the law wrong, but it invites courts to set dangerous precedent that could unravel decades of settled property-insurance law, on which ordinary businesses, banks, and families rely. If courts accept *Couch 3d*'s "physical alteration" fallacy, the results could be catastrophic. The ensuing legal regime could well deny policyholders the benefit of the all-risk coverage they purchased and, under the pressure of the greatest health and economic dislocation in a century, send droves of policyholders into bankruptcy. That is both bad law and bad policy.

ADDENDUM 10

Consumer Federation of America

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THE INSURANCE INDUSTRY'S INCREDIBLE DISAPPEARING WEATHER CATASTROPHE RISK:

HOW INSURERS HAVE SHIFTED RISK AND COSTS ASSOCIATED WITH WEATHER CATASTROPHES TO CONSUMERS AND TAXPAYERS

J. Robert Hunter, Director of Insurance
Consumer Federation of America

February 17, 2012

Insured losses from catastrophes around the globe totaled an estimated $108 billion in 2011, the second highest year in history. More than $30 billion of those losses occurred in the United States, likely the fifth or sixth most expensive year on record. Since 2004, storms like Katrina, Rita, Wilma and Ike, combined with other events have resulted in nearly $200 billion in catastrophe claims paid to millions of home, business and vehicle owners.

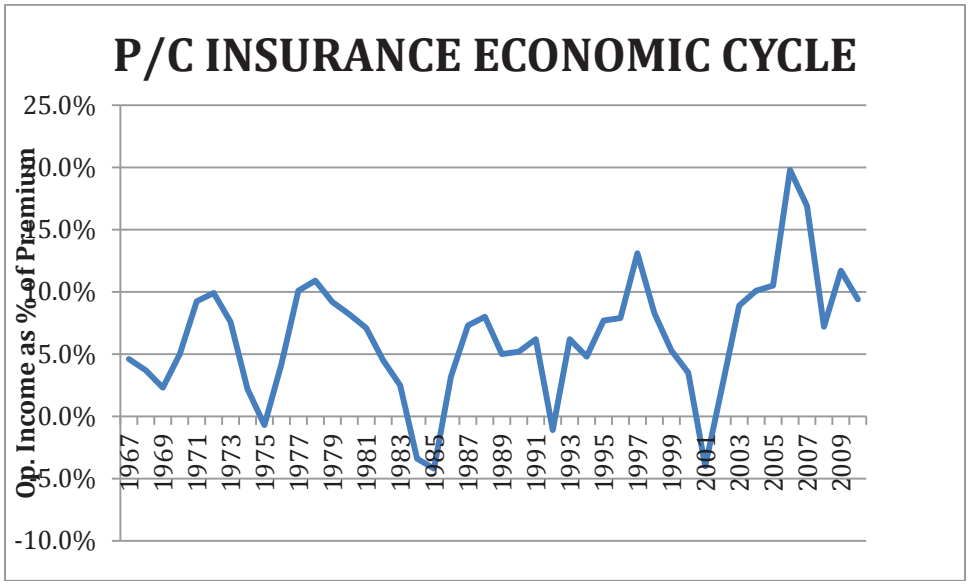
Robert Hartwig, President of the Insurance Information Institute[1]

The question of how insurers deal with weather catastrophes, especially in years in which multiple events occur, has serious policy implications for Americans. In short, how can insurers handle all this risk, and is it legitimate to shift these costs to consumers and taxpayers?

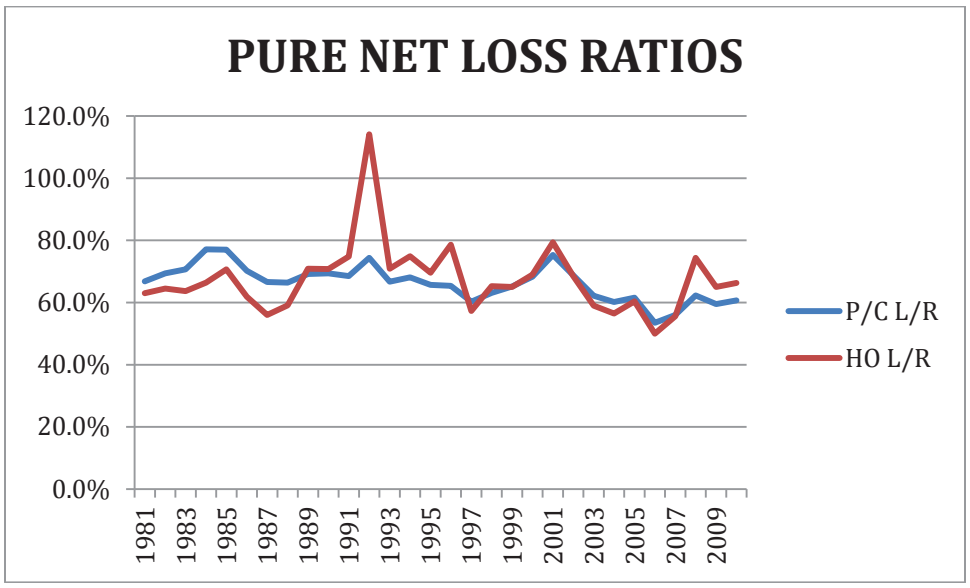
While insurance executives frequently remind the public and regulators of the frequency and severity of catastrophic events, industry data demonstrates that insurers have significantly and methodically decreased their financial responsibility for these events in recent years and shifted much of this risk to consumers and taxpayers. Some of the savings they have achieved is the result of the use of reinsurance and wise risk diversification strategies. However, most these savings have been achieved by hollowing out the coverage in homeowners insurance policies and raising rates. Insurers have also exposed taxpayers to more disaster assistance payouts and shifted high risk homes to state pools. This study investigates and analyzes the significant weather catastrophe risk-shift that has occurred in the last twenty years and offers recommendations to stop insurers from continuing to illegitimately shift costs and risks to taxpayers and consumers.

CATASTROPHES: ONCE A SERIOUS PROBLEM FOR INSURERS

The fact is that catastrophic weather events were once a serious problem for insurers. Consider the following charts:[2]



[1] "III Response to Americans for Insurance Reform Report," December 15, 2011.
[2] The data underlying these charts can be viewed at Addendum A.



"P/C L/R" is total property/casualty insurance losses divided by premium, called the "loss ratio." "HO L/R" is the loss ratio for the homeowners' insurance line of insurance.

The first chart illustrates the insurance industry economic cycle, showing operating income as a percentage of premium for the entire property-casualty insurance business over the last thirty years. There is a strong cyclical pattern to the industry's results. Periodically, insurers' profits decline to the break-even point. This is followed by what is known as a "hard market," in which coverage is hard to get and prices rise sharply. For example, a hard market began in 1975. Profits rose quickly thereafter and then, slowly, declined during the soft market until 1985, when another hard market started as profits dropped to zero and even a bit below that. A soft market began in 1987 and stayed in place until profits bottomed out again in 2001. The market is still soft as 2012 begins, but declining profits indicate that a hard market might be on the way. In fact, insurers are hoping for a hard market soon.[3]

One noteworthy aspect to the first chart is the sharp drop in overall property-casualty profits in 1992. What caused that one-year deviation from the normal cycle? The answer is that Hurricane Andrew adversely affected the insurance industry. Overall property-casualty profits fell that year by seven points as a direct result of Andrew. This is exactly what one would expect when a huge catastrophe occurs, because this is why Americans buy insurance, to cushion such occasional blows.

The impact of Hurricane Andrew can also be clearly seen in the second chart. Net loss ratios of the property-casualty industry increased by about seven points because homeowner's insurance profits were reduced by a whopping 40 points by Andrew.

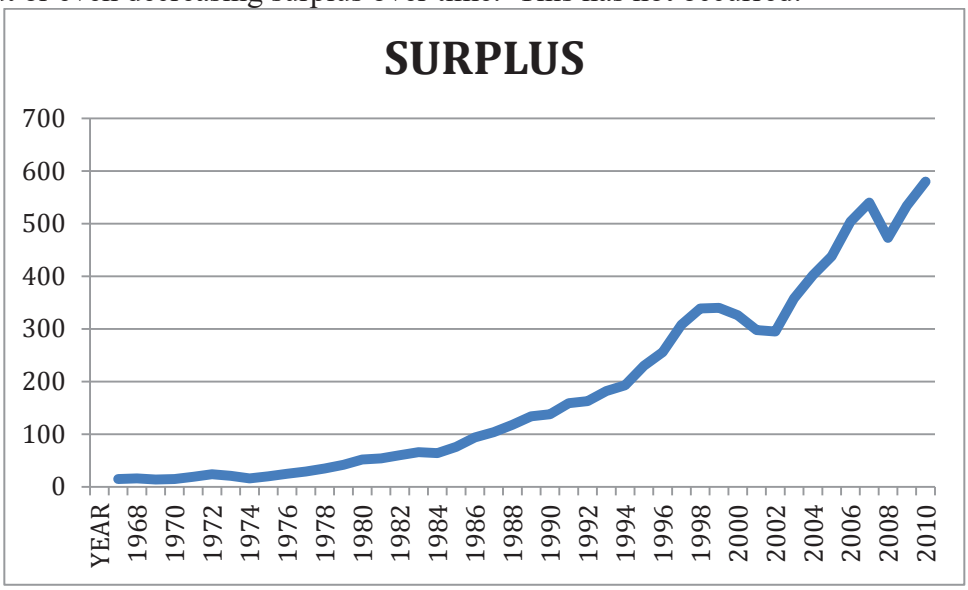
These charts demonstrate that at one time -- when hurricane Andrew hit in 1992 -- insurers bore much of the financial risk of hurricanes. This trend clearly changed in the last decade, in which seven of the most destructive ten disasters in American history occurred, according to the Insurance Information Institute.[4]. The huge hurricane damages of 2004 (four

[3] "Repeat Offenders: How the Insurance Industry Manufactures Crises and Harms America," Americans for Insurance Reform, December 2011.

[4] See http://www.iii.org/facts_statistics/catastrophes-us.html.

Florida hurricanes) and 2005 (Katrina and other hurricanes) had almost no impact on the overall property-casualty loss ratio or even the homeowners insurance loss ratio, as shown by the above chart.

One factor that illustrates the trend of large events having minimal impact on insurers is the increasing surplus that property casualty insurers have accumulated in recent years. One would expect that, in years when large hurricane events occurred, insurers losses would increase, leveling out or even decreasing surplus over time. This has not occurred.



INSURERS HAVE NOW "MASTERED" CATASTROPHIC EVENTS

When four hurricanes hit Florida in 2004 and Hurricane Katrina pummeled the Gulf Coast in 2005, there was no noticeable impact on the overall profits or loss-ratios of property-casualty insurers in either year. An examination of just the loss ratios for homeowners' insurance in those two years shows an impact from the storms that is not noticeable. According to the Insurance Information Institute,[5] Hurricane Andrew resulted in overall losses of $28 billion, of which $17 billion (64 percent) were paid out in insured losses. Hurricane Katrina resulted in overall losses of $125 billion, of which insurers paid out $62 billion (just under 50 percent). Had the payout ratio for Katrina been the same as for Andrew, insurers would have paid out $80 billion, or $18 billion more than they did. The bottom line in these comparisons is that, if insurers had not reduced policyholder coverage and increased rates after Hurricane Andrew, they would have paid out almost 30 percent more to them

How is it possible that the property-casualty industry's surplus would sharply increase as the number and severity of catastrophic weather events also increases? The primary reason is that the insurers have "mastered" hurricanes by shifting the lion's share of the risk and costs to consumers and taxpayers. In other words, property-casualty insurers have paradoxically emerged as masters of risk avoidance, rather than continuing their historic role of risk taking.

[5] See http://www.iii.org/facts_statistics/catastrophes-global.html.

HOW INSURERS REDUCED THEIR HURRICANE LOSSES AND SHIFTED RISK TO CONSUMERS AND TAXPAYERS

First, insurers have made intelligent use of reinsurance, securitization and other risk spreading techniques.[6] Some insurers now spread risk by issuing securities that couple the threat of a catastrophic event with the purchase of construction stocks that would likely increase in value if a catastrophic event occurs and the demand for construction increases. The use of this kind of creative approach to diversify risk is wise.

Second, after Hurricane Andrew, insurers changed ratemaking techniques by using computer models to project either 1,000 or 10,000 years of weather experience. While this caused huge price increases to consumers at the time, consumer leaders supported this change because insurers appeared to be genuinely surprised by the level of damage caused by Hurricane Andrew and promised that the models would bring long-term stability to prices. The model contained projections of periods of intense activity and very large hurricanes, as well as periods of little or no activity, and based rates on these estimates.

However, Risk Management Solutions (RMS) and the other risk modeling companies have recently stopped using this scientific method to project storms over a 1,000 or 10,000-year period and are now using one to five-year projections. This has caused at least a 40 percent jump in loss projections in Florida and the Gulf Coast and a 25 percent jump in the Northeast. This move reneges on promises of pricing stability made by insurers in the mid-1990s and has led to rates that are excessive. Insurance rates on the coasts have soared for property risks, homes and businesses in the last few years.

Third, insurers have sharply hollowed out the catastrophe coverage offered to consumers in recent years by placing a number of new requirements on policyholders and limits on coverage in policies:

- Deductibles of 2 to 5 percent have been imposed with little fanfare or notice. This reduction in coverage was accompanied in many cases by large rate increases.

- Caps on replacement costs and other limits on needed coverage. State Farm, for instance, caps payments for increased rebuilding costs at 20 percent. Other insurers allow no increased payments at all. A consumer who buys a $100,000 policy would receive only $100,000 to rebuild from some insurers, and $120,000 from State Farm, even if the cost of repairs skyrockets after a storm due to increased demand for materials and labor. Costs can also increase when homeowners are required to make special repairs to comply with building codes that were enacted after a home was first constructed. For example, many municipalities require such code upgrades to comply with the National Flood Insurance Program if a home is more than 50 percent damaged by a flood.

[6] This report is focused on the primary insurance market, not the reinsurance market. The worldwide reinsurance market has had rather stable catastrophe prices since 2002, with "rates on line" – defined by the reinsurer Guy Carpenter as "Premium divided by indemnity (claims paid). A British term for the rate which, when multiplied by the indemnity, would produce the premium." in a tight range since 2002. The highest rate on line observed in the data was in 1993 as Andrew severely impacted pricing. Today prices are stable because the catastrophe reinsurance sector "was overcapitalized by more than US $20 billion, or 12 percent at the beginning of 2010." This led to share buy-backs by many reinsurers. (Material in this footnote based on "World Catastrophe Reinsurance Market," Guy Carpenter, September 2010.)

Reimbursement for costs incurred to comply with building codes is now excluded from many homeowners' insurance policies. Coverage for mold mitigation is also now excluded from most policies. Given the surge in demand for home building and repair that occurs in the wake of a hurricane, and corresponding increases in prices, and new coverage exclusions, these changes significantly shift risk and costs to consumers.

- "Anti-concurrent-causation" clauses. This is the most draconian reduction in coverage that insurers have attempted to impose in recent years. It removes all coverage for wind damage if another, non-covered event (usually a flood) also occurs, regardless of the timing of the events. Under this anti-consumer measure, if a hurricane of 125-miles-per-hour rips a house apart but hours later a storm surge floods the property, the consumer would receive no reimbursement for wind losses incurred.

Given the cutbacks in coverage that have occurred in coastal areas, there is a serious question as to whether this diminished coverage is worth the higher rates that many consumers must pay. However, most consumers have no option but to purchase such coverage as it is required by lenders or the law or both. Demand for insurance is relatively inelastic.

Insurers have claimed that they are facing higher risks because of a sharp increase in the number of people and amount of construction in areas of the country vulnerable to earthquake and hurricane disasters. This claim was investigated in 2006 by the Los Angeles Times investigative reporter Peter Gosselin, who wrote that:

> …Key statistics don't support the argument….Census figures…show that the population of coastal and earthquake counties grew at an annual average rate of 1.56 percent between 1980 and last year. But they show that the U.S population grew at a reasonably close pace of 1.24 percent.

Gosselin interviewed Judith T. Kildow, director of the government-funded National Ocean Economics Program at California State University at Monterey, who said, "You simply cannot make the case from the numbers that America's coastal counties have grown at a disproportionately faster rate than the country as a whole over the last 25 years."[7]

Fourth, insurers have also shifted risk, sometimes onto taxpayers. Taxpayers are exposed by the high deductibles, anti-concurrent causation and other limits on coverage as disaster relief will fill in what insurers used to cover.

Taxpayers might also be called upon to subsidize state-run insurers-of-last resort, which were sharply populated by insurers non-renewing tens of thousands of homeowner and business properties. Allstate, the leading exemplar after Hurricane Andrew, emerged once again as the company that was most aggressive in refusing to renew homeowner's policies in the wake of Hurricane Katrina. After Hurricane Andrew, Allstate threatened to non-renew 300,000 South Floridians, leading the state of Florida to place a moratorium on such precipitous actions. After Hurricane Katrina, Allstate non-renewed thousands of homeowners, even many on Long Island, New York and Cape Cod, Massachusetts. Allstate has also announced that it will no longer offer new homeowner's policies in many states, from Connecticut to Delaware, and has refused to

[7] "The New Deal – Insurers Learn to Pinpoint Risks – and Avoid Them," Peter Gosselin, Los Angeles Times, November 28, 2006.

write new business in large portions of other states, such as Maryland and Virginia. Other insurers have also cut back coverage on the nation's coasts (See Addendum B, for more information).

Insurers have become quite adept at convincing government to use tax dollars to help them avoid risk. Consider the federal Terrorism Risk Insurance Act (TRIA), the California Earthquake Authority, Citizen's Insurance in Florida, and wind "pools" in a number of other states. The state pools have become the largest writers of insurance in some states[8]. Such an arrangement allows insurers to "cherry-pick" these states, keeping the safest risks for themselves and shifting the highest risks onto the taxpayers of the state, thereby socializing high-risk, potentially unprofitable policies and privatizing the low-risk, profitable business. This adverse result for policyholders and taxpayers is hardly surprising. It is akin to "solving" the health insurance crisis by requiring states to cover sick or terminally ill patients, while the private sector writes coverage for young and healthy consumers. Allstate has also led efforts at the federal level that failed to create a taxpayer-backed program modeled on TRIA to reinsure the private market against the perils of wind and other weather damage.

INSURERS COULD EASILY HANDLE CATASTROPHE RISK THEY ARE AVOIDING BECAUSE THEY ARE SIGNIFICANTLY OVERCAPITALIZED

In determining whether the property-casualty insurance industry is adequately capitalized, one must first examine the losses incurred for major catastrophe or terrorism events. According to the Insurance Information Institute, the top ten insured loss disasters for property were:

EVENT[9]	PRE-TAX 2010 DOLLAR LOSS	POST TAX
1. Hurricane Katrina, August 2005	$45.5 billion	$29.6
2. World Trade Center, Pentagon terrorist attacks, September 2001	22.9	14.9
3. Hurricane Andrew, August 1992	22.4	14.6
4. Northridge, California earthquake, January 1994	17.3	11.2
5. Hurricane Ike, September 2008	12.7	8.3
6. Hurricane Wilma, October 2005	11.4	7.4
7. Hurricane Charley, August 2004	8.5	5.5
8. Hurricane Ivan, September 2004	8.1	5.3
9. Hurricane Hugo, September 1989	6.7	4.4
10. Hurricane Rita, September 2005	6.2	4.0

Source: Insurance Services Office (ISO); Insurance Information Institute (See http://www.iii.org/facts_statistics/catastrophes-us.html). (Ranked on constant dollar cost to insurers)

[8] According to PIPSO – The Property Insurance Plans Service Office, the Florida FAIR Plan had 1.5 million policies, of which over 285,000 were high-risk coastal properties on May 2011. The Texas wind pool had 247,972 residential and 17,998 commercial policies in 2010. In 2010, Alabama's pool had 18,800 policies (mere than double the 7,800 of 2007z), Mississippi's Beach/Windstorm Plan had 46,546 policies and Georgia had 26,340 policies in its Pool.

[9] The catastrophes were ranked by III based on size of loss in 2005 dollars, which we do not display here. What is displayed is the actual dollars in the year of the event. We calculate the post-tax figure by deducting the corporate tax rate of 35 percent.

Considering that property-casualty insurers now have surplus in excess of $580 billion,[10] catastrophes of this size are very easy to manage.

Terrorism risk is an interesting case study. While insurers are rightly concerned about a huge event, such as a nuclear, chemical or biological attack, the actual terrorism events that have occurred so far have been easily managed by private industry. There were hundreds of terrorism events in America in the 20 years leading up to the September 11th attacks. In spite of this fact, insurers did not even bother to charge a separate price for terrorism coverage in their rating structures. September 11th changed this practice, but even that attack was a "small" insured event compared to the industry's mammoth capital and surplus, which has grown significantly since 2001. Yet, insurers convinced the federal government to provide free reinsurance that CFA estimates has represented about a ten billion taxpayer subsidy to date.

Historically, the prime test for the solidity of the property-casualty insurance industry has been the ratio of net premiums written (NPW) to surplus, discussed above. Regulators became concerned about the financial soundness of an insurer if its ratio exceeded 3 to 1. The so-called "Kenney Rule," named after financial writer Roger Kenney, held that a safe insurer should not exceed about a 2 to 1 ratio. This guideline was introduced in the 1960s and served as the standard that insurers and regulators followed for many decades. More recently, analysts have recommended lowering the acceptable ratio to about 1.5 to 1, in recognition of some more extreme risks that insurers now face, such as catastrophic hurricanes and terrorist attacks. Net premium written to surplus ratios for almost thirty years are as follows:

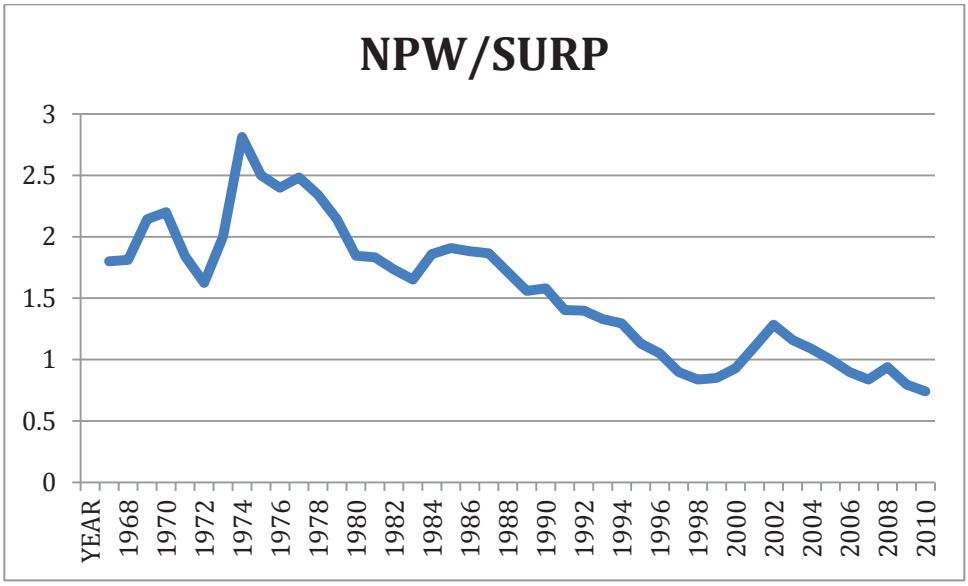
YEAR	NPW/SURP
1967	1.80
1968	1.81
1969	2.14
1970	2.20
1971	1.84
1972	1.63
1973	2.00
1974	2.81
1975	2.50
1976	2.40
1977	2.48
1978	2.34
1979	2.14
1980	1.85
1981	1.83
1982	1.73
1983	1.65
1984	1.86
1985	1.91
1986	1.88
1987	1.87
1988	1.71

[10] As of December 31, 2010, Bests Aggregates and Averages, 2011 Edition, page 366.

1989	1.56
1990	1.58
1991	1.40
1992	1.40
1993	1.33
1994	1.30
1995	1.13
1996	1.05
1997	0.90
1998	0.84
1999	0.85
2000	0.93
2001	1.10
2002	1.28
2003	1.16
2004	1.09
2005	1.00
2006	0.90
2007	0.84
2008	0.94
2009	0.80
2010	0.74

Source: Best's Aggregates and Averages, 1988-2011

Property-casualty insurers have not exceeded the recommended 1.5 to 1 ratio of NPW to surplus in almost twenty-five years. The sharp downward trend in this key leverage ratio is very clear, demonstrating that the industry is now significantly overcapitalized. Here is a graphic display of these data:



Consider this startling fact: Even if all of the top ten catastrophic events, including the September 11, 2001 attack, the Northridge Earthquake, and the top eight hurricanes, had

occurred in the last year and had been paid for last week (a total of $162 billion in 2010 dollars after tax[11]), the property-casualty industry surplus would still be at $418 billion and the leverage ratio would still be at an ultra safe ratio 1.0.[12]

WHO PAYS WHEN INSURERS DO NOT?

Consumers

Data indicates that Hurricane Katrina cost $125.0 billion, of which $62.2 billion (just under 50 percent) was paid by insurance. Hurricane Andrew cost $26.5 billion, of which $17.0 billion (64 percent) was paid by insurance.[13]

To show the difference in coverage now that the policies have been hollowed out, consider a hypothetical $100,000 home that incurred different levels of wind damage under the Hurricane Andrew compared to Hurricane Katrina. Assume the home had a $500 deductible under Andrew and a 5 percent deductible under Katrina.

	Benefit after Deductible		Katrina as a % of Andrew
Damage	Andrew	Katrina	
$10,000	$ 9,500	$ 5,000	53.6%
(Consumer pays $500 in Andrew; $5,000 in Katrina)			
$50,000	$49,500	$45,000	90.9%
(Consumer pays $500 in Andrew; $5,000 in Katrina)			

Assume further that additional work must be done when it is reconstructed to bring it up to code. If, for instance, the home required $1,000 of electrical work, the policyholder would be paid an additional $1,000 for Hurricane Andrew in both circumstances. However, under Katrina, there would the policyholder would receive no additional payment under the policy for mandated code work.

	Benefit after Deductible		Katrina as a % of Andrew
Damage	Andrew	Katrina	
$10,000	$ 9,500 + $1,000	$ 5,000	47.6%
(Consumer pays $500 in Andrew; $6,000 in Katrina)			
$50,000	$49,500 + $1,000	$45,000	89.1%
(Consumer pays $500 in Andrew; $6,000 in Katrina)			

If the home was in a flood plain and not elevated, damages that totaled 50 percent of the home's value would trigger a "non-conforming use" under the National Flood Insurance

[11] From Insurance Information Institute at http://www.iii.org/facts_statistics/catastrophes-us.html.

[12] $430 million in premium divided by ($580 million in surplus less $162 million in assumed after-tax loss) Data on Net Premiums Written and Surplus for all insurers is from A. M. Best Aggregates and Averages, 2011 Edition, Page 369.

[13] See http://www.iii.org/facts_statistics/hurricanes.html.

Program and the home would have to be upgraded to withstand a "100-year" flood. If such an improvement costs $10,000, the damage situation with $50,000 in losses would be:

Damage	Benefit after Deductible Andrew	Katrina	Katrina as a % of Andrew
$10,000 (Consumer pays $500 in Andrew; $6,000 in Katrina))	$ 9,500 + $1,000 + $10,000	$ 5,000	24.4%
$50,000 (Consumer pays $500 in Andrew; $16,000 in Katrina)	$49,500 + $1,000 + $10,000	$45,000	74.4%

It could get even worse if the home is destroyed and a demand surge of 50 percent raised the rebuilding cost for the $100,000 home to $150,000. If there was any additional flood damage to the home, even minor damage, (such as $5,000) the insurer might invoke the anti-concurrent causation clause of the policy and pay nothing. If the damage is caused only by wind, but the severe damage in the area causes rebuilding costs to rise by 50 percent, the benefit situation would be:

ANDREW: $150,000[14] less $5,000 for flood damage plus $10,000 flood elevation less $500 deductible = $154,500. Consumer pays $5,500.

KATRINA: Insurance pays nothing. Consumer pays $160,000.

It is very clear that much of the cost that used to be paid by private insurers has been shifted to consumers, ranging from a small amount to 100 percent of what used to be paid. Much of this will be shifted again, to taxpayers, in the form of increased disaster relief payouts as discussed now.

Taxpayers

Taxpayers are also bearing more risk. The National Flood Insurance Program is almost $20 billion in debt because the program is poorly administered by the Federal Emergency Management Agency (FEMA) and is poorly designed. FEMA has allowed flood risk maps to become antiquated, which has resulted in inadequate premiums that encourage unwise construction. The "Write Your Own" program which requires taxpayers to shoulder all financial risk, but allows insurers to service the NFIP, has also allowed insurers to collect excessive fees. The program will surely go deeper in debt in coming years due to these among other hidden subsidies, such as "grandfathering" in low, inadequate rates when new maps are issued. Congress should require the private sector to take a small, but growing, percentage of the risk over time. This will reduce taxpayer exposure in two ways: (1) The private sector will pay for flood losses incurred on their own accounts and (2) once the private sector has financial responsibility for some flood losses, it will police against hidden subsidies, such as FEMA's unauthorized (by Congress) grandfathering of low rates on supposedly actuarially-rated homes when a new map raises flood elevations.

[14] Some companies, such as State Farm, would pay an additional 20% or $30,000 more in this example.

The subsidy to taxpayers under TRIA has amounted to roughly $10 billion. Although there is no need for the federal government to back terrorism risk (except for exotic risks like nuclear and biological attacks), insurers are enjoying what amounts to free reinsurance, making TRIA another example of a wasteful corporate subsidy.

When private insurance payouts decline during catastrophic weather events, it stands to reason that government disaster relief costs will increase. Hurricane Andrew generated public disaster relief payments of $7 billion in 2009 dollars, whereas Hurricane Katrina generated $51 billion.[15] Insurance payments were twice as high for Katrina as for Andrew but disaster relief payments were over seven times higher. In 2008, with Hurricanes Gustav and Ike, among others, federal disaster relief was $13 billion (2009 dollars). When storms like these eclipse Andrew in the amount of government disaster relief that is paid out, it is hard not to conclude that a major cause of this increased taxpayer burden is the reduction in risk carried by insurers. The total cost of disaster relief from 1990 to 1999 was $40 billion; from 2000 to 2010 it was more than double, at $94 billion (all in 2009 dollars).

Because private insurers have fled America's coasts, many homes are insured through state pools. In Florida, Florida Citizens' Property Insurance Corporation (CPIC), the state pool, covers 1.5 million homes. If a storm or series of storms depletes Citizens' rather healthy reserves, assessments may be placed on other property-casualty companies in the state to address the shortfall. The state has the authority, since assessments are limited, to finance loss payments via tax-exempt bonds. State taxpayers could be at some risk if Citizens' or the CAT Fund (also backed by the state) ever ran out of money, even though this possibility has become less likely as the state has built up reserves. In California, earthquake risk is mostly written through the California Earthquake Authority, an entity similar to Florida Citizens, where state taxpayers may be exposed in extreme events.

RECOMMENDATIONS

There are many conclusions to be drawn from the reduced losses that insurers have experienced in recent years. The prime conclusion is that the insurance industry has moved from its historic role as a calculated risk-taker to one of a risk-avoider, exposing consumers and taxpayers to much higher costs. Not only have insurers insulated themselves from their historic share of hurricane risk, they have made no serious effort to write flood risk and terrorism risk, which are entirely backed by federal taxpayers.

Although insurers have become adept at shifting the cost of catastrophe losses to others, they still use catastrophic weather events to advocate for measures that would shift risk even more, such as higher rates, or putting more policyholders in pools or created taxpayer-supported entities. Thus, many consumers exposed to catastrophe weather risk are also vulnerable to insurer attempts to unjustifiably increase rates or hollow out coverage.

Recommendations for the States

CFA recommends that the states carefully examine national data on limited catastrophe losses and excessive surplus before approving any insurer requested rate increases. State

[15] Database maintained by Congressional Research Service based upon US Budget documents and appropriation statutes, Table 1 of "Disaster Relief Funding and Emergency Supplemental Appropriations, CRS, May 24, 2010.

insurance commissioners should be on guard against unwarranted attempts by insurers to use catastrophe losses as part of their rationale for jacking up rates.

We recommend that states carefully review the reasons why insurers are dumping risks into state pools and to take action to stop insurers from unjustifiably refusing to cover qualified homeowners. It is unnecessary for any more dumping to occur since insurers have now twice purged their portfolios of risk, once after Hurricane Andrew and again after Hurricane Katrina. States should also look at the high prices being charged to homeowners in their states in light of the fact that, in the aftermath of Andrew, insurers made major adjustments to pricing, dumped risk, reduced coverages and significantly reduced their hurricane risk exposure. Repeating these adjustments in the wake of 2004/5 storms was really more about gouging than correction. Rates requested by insurers in non-competitive markets after hurricanes can easily be excessive, violating sound actuarial principles. The coastal states must revisit hurricane pricing in recognition of the fact that the industry has mastered hurricanes on a national basis as evidenced by the almost negligible impact of Hurricane Katrina on their national results, a vast change compared to results during Hurricane Andrew, a smaller event. States should ban the use of non-scientific pricing models, such as short-term catastrophe models.

States should ban use of anti-concurrent causation clauses and any other attempt by insurers to build a "trap-door" hidden in the policy, through which coverage can unexpectedly fall when policyholders most need help.

States should not allow hurricane deductibles to apply unless a storm is classified as a hurricane throughout its journey through the state, from entry to exit. It is impossible to tell where a hurricane exactly becomes a tropical storm within a state so this ambiguity must be decided to the benefit of the consumers who have bought the coverage, not insurers who are compensated for being risk-takers.

States should adopt the California approach to consumer participation in regulatory proceedings, where consumers can receive reimbursement from the filing insurer to hire experts (like actuaries, lawyers and economists) if they make a "substantial contribution" to a case. They receive no compensation if they do not make a substantial contribution, so consumer groups in California study filings prior to risking an intervention very carefully. Costs paid by the insurers for such intervention would be allowed to be included as part of the rate filing.

States should make sure that they have all the data they need to monitor the home insurance market, including data by census track on who is writing and where, non-renewal patterns, etc. This will allow regulators to make informed decisions about whether markets in their states are truly competitive.

Coastal states should join together to form an interstate compact to deal with common issues stemming from their shared hurricane risk. A pool of states with common policies could allow states to spread risk and lower costs by developing common pools and provide consumers and insurers with consistent requirements. A common approach would also better position states – especially small ones – to resist coercive efforts by insurers to weaken regulatory protections for consumers. For example, after the hurricanes of 2004/5, several smaller states (AL, MS and LA) were pressured by insurers with threats of withdrawal to take actions that would harm consumers in those states.

One action a consortium of coastal states could take is to create a regulatory model for calculating hurricane risk to test the reliability of insurer-proposed catastrophe premiums in rates.

Using the model, states could create a stand-by reinsurance mechanism that would sell reinsurance to insurers at 50 percent more than actuarial rates developed by the model, which would keep premiums in check during the non-competitive phase of the insurer cycle or after hurricane events when reinsurers often gouge. When private reinsurance is reasonably priced at or near the actuarial level, the state back-up would not kick in. Florida successfully did sell reinsurance to the industry after the 2004/5 storms and now has, through premium accumulation and bonding, no real risk for its reinsurance. At the same time, policyholders saved about 15 percent of premiums because Florida requires insurers to use their reinsurance (or at least adopt the cost of that state reinsurance or less in home insurance ratemaking). This system temporarily replaced private reinsurance in Florida, which was priced at four to five times the actuarial rate in the non-competitive reinsurance market after 2004 and 2005 storms.

States should also develop model language that would be required in every minimum insurance policy sold in the region. Among other things, this language should remove the anti-concurrent causation clauses from use and clarify exceptions and exclusions in coverage. Coverage above the minimum would be allowed to be sold to consumers with pricing for such enhancements made clear to the policyholder.

Recommendations for the Federal Government

The fact that insurers do not take financial risk for either flood or terrorism insurance is a huge policy error. With the NFIP, it tempts unscrupulous insurers to illegitimately shift wind risk to the flood program. With both programs, taxpayers are required to pick up huge risks that private insurers are more than capable of identifying and backing. Taxpayers deserve to have at least some of this risk removed from them, particularly at this time of economic stress, and a search for ways to cut federal spending. We recommend that Congress limit the exposure of taxpayers to terrorism risk to only extreme events such as nuclear, chemical or biological events exceeding a 100 billion threshold. TRIA should be amended to only cover losses caused by nuclear, biological or chemical attacks that exceed $100 billion.

We recommend that the National Flood Insurance Program bills currently under consideration be amended to require a study on how to involve the private sector in sharing the risk from the first dollar of loss, perhaps starting with a low, but increasing, percentage of the risk for insurers wishing to participate in the NFIP as "Write Your Own" companies.[16] FEMA should also lower the excessive WYO servicing fees that create a windfall for the WYO companies at taxpayer expense. Recommendations for private reinsurers to cover losses only above the federal insurance coverage that is offered should be rejected, as they will only add the cost of reinsurers' overhead and profit to the program over time. It does not make sense to have the relatively tiny reinsurance industry backing up the federal government, at the same time as insurers are pushing for a federal backstop for their wind exposure. Logically, a smaller entity should not be backing up a bigger one, which argues for a private NFIP role at the low end of flood loss spectrum, not at the high end. If the program were privately reinsured, it would most

[16] See June 23, 2011 Testimony given by Travis Plunkett to the US Senate Banking Committee on the "Authorization of the National Flood Insurance Program" for detailed comments on CFA's recommendations.

likely add the unnecessary cost of the overhead and profit the reinsurers receive to the cost of the program, requiring more taxpayer expenditures over time. Further, if significant events occur, reinsurers are likely to either retrench or severely raise prices, just when reinsurance is most needed, as they do with wind coverage.

Data on home insurance in a format similar to what is required of banks under the Home Mortgage Disclosure Act (HMDA) should be collected by the Federal Insurance Office (FIO) and made available to the states and to the public. This would allow detailed analysis of why certain markets are stressed, which insurers are doing their best to serve markets in stressed areas and which are causing problems. This would enable policyholders to craft solutions based on solid statistical evidence. It would also allow analysis of markets to see if low- and moderate-income areas are being properly served.

We recommend that the federal government assist the states in forming an interstate compact to regulate hurricane insurance by authorizing such a combined effort and by taking action to assist the states in several ways, including:

- Offering the expertise of the federal government (entities like FEMA, NOAA, etc.) to the group of coastal states. These experts could help develop the regulatory hurricane model for states to use in regulating insurance and in developing stand-by reinsurance pricing.

- Offering bridge loans at low-interest when stand-by reinsurance is used, if such use suffers losses due to timing risk (such as a large storm in the early years of the development of reserves.) These loans would be required to be fully repaid over reasonable time periods.

ADDENDUM A

DATA UNDERLYING THE CHARTS FOUND IN THE BODY OF THIS REPORT

COLUMN 1 YEAR	COLUMN 2 Total P/C Op Inc/Prem	COL 3 YEAR	COLUMN 4 P/C L/R	COL 5 HO L/R	
1967	4.6%				
1968	3.7%				
1969	2.3%				
1970	5.0%				
1971	9.3%				
1972	9.9%				
1973	7.6%				
1974	2.2%				
1975	-0.7%				
1976	4.2%				
1977	10.1%				
1978	10.9%				
1979	9.2%				
1980	8.2%				
1981	7.1%	1981	66.8%	63.0%	
1982	4.5%	1982	69.4%	64.5%	
1983	2.5%	1983	70.7%	63.7%	
1984	-3.4%	1984	77.1%	66.4%	
1985	-4.2%	1985	77.0%	70.7%	
1986	3.2%	1986	70.2%	61.9%	
1987	7.3%	1987	66.6%	56.0%	
1988	8.0%	1988	66.4%	59.1%	
1989	5.0%	1989	69.2%	70.9%	
1990	5.2%	1990	69.4%	70.8%	
1991	6.2%	1991	68.5%	74.8%	
1992	-1.1%	1992	74.4%	114.1%	HURRICANE ANDREW
1993	6.2%	1993	66.7%	70.9%	
1994	4.8%	1994	68.1%	74.9%	
1995	7.7%	1995	65.7%	69.6%	
1996	7.9%	1996	65.4%	78.6%	
1997	13.1%	1997	60.3%	57.3%	
1998	8.3%	1998	63.1%	65.3%	
1999	5.3%	1999	65.2%	65.0%	
2000	3.5%	2000	68.3%	69.0%	
2001	-4.0%	2001	75.3%	79.4%	
2002	2.4%	2002	68.8%	68.5%	
2003	8.9%	2003	62.2%	59.0%	
2004	10.1%	2004	60.2%	56.5%	4 FLORIDA HURRICANES
2005	10.5%	2005	61.6%	60.4%	HURRICANE KATRINA
2006	19.8%	2006	53.5%	50.0%	
2007	16.9%	2007	56.0%	55.6%	
2008	7.2%	2008	62.3%	74.4%	

2009	11.7%	2009	59.5%	65.0%
2010	9.4%	2010	60.7%	66.3%

Source: All data from Best's Aggregates and Averages, various years.

Columns 1 and 2 were used to create the chart showing the Property-casualty Insurance Industry's Economic Cycle over more than four decades.
Columns 3, 4 and 5 were used to create the chart showing the loss ratios for both the overall Property-casualty Insurance Industry and for homeowners insurance over a thirty-year period.

Addendum B: Reprinted from The Los Angeles Times, November 28, 2006

Insurance company cutbacks have left more than 1 million coastal residents scrambling to land new insurers or learning to live with weakened policies. As insurers retreat, states and homeowners are left to bear the biggest risks.

Massachusetts

During the last two years, six insurers have stopped selling or renewing policies along the coast, especially on Cape Cod, leaving 45,000 homeowners to look for coverage elsewhere. Most have turned to the state-created insurer of last resort. The Massachusetts FAIR Plan, now the state's largest homeowners insurer, recently received permission to raise rates 12.4 percent.

Connecticut

Atty. Gen. Richard Blumenthal has subpoenaed nine insurance companies to explain why they are requiring thousands of policyholders whose houses are near any water —coast, river or lake —to install storm shutters within 45 days or have their coverage cut or canceled.

New York

Allstate has refused to renew 30,000 policies in New York City and Long Island, and suggested it may make further cuts. Other insurers, including Nationwide and MetLife, have raised to as much as 5 percent of a home's value the amount policyholders must pay before insurance kicks in, or say they will write no new policies in coastal areas.

South Carolina

Agents say most insurers have stopped selling hurricane coverage along the coast. Those that still do have raised their rates by as much as 100 percent. The state-created fallback insurer is expected to more than double its business from 21,000 policies last year to more than 50,000.

Florida

Allstate has offloaded 120,000 homeowners to a start-up insurer and has said it will drop more as policies come up for renewal. State-created Citizens Property, now the state's largest homeowners insurer with 1.2 million policies, was forced to use tax dollars and issue bonds to plug a $1.6- billion financial hole due to hurricane claims. The second-largest, Poe Financial Group, went bankrupt this summer, leaving 300,000 to find coverage elsewhere. The state also has separate funds to sell insurers below-market reinsurance and cover businesses. Controversy over insurance was a major issue in this fall's election campaign, causing fissures in the dominant GOP.

Louisiana

The state's largest residential insurer, State Farm, will no longer offer wind and hail coverage as part of homeowners policies in southern Louisiana. In areas where it still covers these dangers, it

will require homeowners to pay up to 5 percent of losses themselves before insurance kicks in. In a move state regulators call illegal and are fighting, Allstate is seeking to transfer wind and hail coverage for 30,000 of its existing customers to the state created Citizens Insurance.

Texas

Allstate and five smaller insurers have canceled hurricane coverage for about 100,000 homeowners and have said they will write no new policies in coastal areas. Texas' largest insurer, State Farm, is seeking to raise its rates by more than 50 percent along the coast and 20 percent statewide.

California

The state has bucked the trend toward higher homeowners insurance rates with three major insurers, State Farm, Hartford and USAA, seeking rate reductions of 11 percent to 22 percent. Regulators have begun to question whether insurers are making excessive profits after finding that major companies spent only 41 cents of every premium dollar paying claims and related expenses. Alone among major firms, Allstate is seeking a 12.2 percent rate hike.

Washington

Allstate has dropped earthquake coverage for about 40,000 customers and will have its agents offer the quake insurance of another company when selling homeowners policies in the state. Nationally, the company has canceled quake coverage for more than 400,000.

Sources: Risk Management Solutions (map); interviews with state insurance regulators

ADDENDUM 11

STATE OF INDIANA)		IN THE MADISON SUPERIOR COURT
) SS:		
COUNTY OF MADISON)		
CHAD E. COOK,	)	
	)	
Plaintiff	)	CAUSE NO. 48D02-0611-PL-01156
	)	
vs.	)	
	)	
ALLSTATE INSURANCE COMPANY,	)	
	)	
Defendant	)	

ORDER GRANTING PARTIAL SUMMARY JUDGMENT TO PLAINTIFF AND DENYING PARTIAL SUMMARY JUDGMENT TO DEFENDANT

Plaintiff Chad E. Cook ("Cook") and Defendant Allstate Insurance Company ("Allstate") cross moved for partial summary judgment and for summary judgment, as to the availability of coverage under Allstate's Deluxe Homeowners Policy for an infestation of Brown Recluse Spiders at Cook's house located at 906 Whitmore Street, Anderson, Indiana 46012 (the "Home"). The parties have exhaustively briefed the issues. The Court heard oral argument on November 12, 2007. Based on the papers filed, the evidence presented and the arguments heard, the Court ORDERS that Cook's motion for partial summary judgment is GRANTED and Allstate's motion for summary judgment is DENIED.

I. FINDINGS OF FACT

Cook and Allstate agree on the governing facts. Cook bought the Home and moved his pregnant wife, three year old and one year old into the Home in April, 2005. Cook observed spiders he assumed were ordinary household spiders when he inspected the house. In August, 2005, Cook became aware that the spiders in the Home might be Brown Recluse Spiders. In September, 2005, Purdue University confirmed that the spiders were Brown Recluse Spiders and

advised Cook to immediately move his family out of the Home. Cook contacted his local Allstate office in September, 2005 and requested coverage. Cook renewed the request by telephone and in person during the following eight months. Cook had the Home treated by pest control professionals. He moved his family back in December, 2005, observed spiders, and moved his family back out again after approximately one week. Although Cook hired various professionals to treat his Home (which continues to date), Brown Recluse Spiders can still be found in living spaces within the Home.

On June 23, 2006, Allstate sent a letter denying coverage based on Allstate's exclusion for losses "consisting of or caused by ... insects, rodents, birds or domestic animals." The letter did not reserve Allstate's right to assert other coverage defenses. On August 11, 2006, Allstate sent a letter denying coverage for failure to "take all reasonable steps to save and preserve property when the property is endangered by a loss we cover" and because of a "substantial change or increase in hazard, if changed or increased by any means within the control or knowledge of an insured person." The letter stated that Allstate had "completed" its investigation and did not reserve Allstate's right to assert other coverage defenses. Seven months after Cook filed suit, Allstate asserted a third coverage defense -- that there had been no "sudden and accidental direct physical loss" to covered property. Allstate failed to assert this coverage defense in its Answers to the initial Complaint and the Amended Complaint.

The applicable coverage limit for dwelling coverage under Allstate's policy is $187,000 and Cook claims alternative living costs at $940 per months for two twelve month coverage periods.

II. CONCLUSIONS OF LAW

A. Indiana's Rules of Insurance Policy Construction.

Indiana appellate decisions apply special rules of construction in insurance coverage disputes. "An insurance policy should be so construed as to effectuate indemnification . . . rather than defeat it." *Masonic Acc. Co. v. Jackson*, 164 N.E. 628, 631 (Ind. 1929); *Tate v. Secura Ins.*, 587 N.E.2d 665, 668 (Ind. 1992). Policy terms not defined in the policy are interpreted from the perspective of an ordinary policyholder of average intelligence. *Travelers Indem. Co. v. Summit Corp. of America*, 715 N.E.2d 926, 936 (Ind. Ct. App. 1999).

If any ambiguity exists in a policy term, and particularly in an exclusion, the term must be interpreted in favor of the policyholder and in favor of coverage: *Eli Lilly and Co. v. Home Ins.*, 482 N.E.2d 467, 470 (Ind. 1985). A term is ambiguous if there is more than one reasonable interpretation of the term. *See Lilly*, 482 N.E.2d at 470-471: ("An insurance policy is ambiguous if reasonable persons may honestly differ as to the meaning of the policy language."). If *any* reasonable construction of a term supports coverage, that construction governs as a matter of law. *Lilly*, 482 N.E.2d at 471. Indiana courts apply these coverage-enhancing rules of construction because "the insurer drafts the policy and foists its terms on the potential customer." *Summit*, 715 N.E.2d at 936.

B. Allstate's "Insect" Exclusion.

Cook and Allstate cross moved for partial summary judgment as to whether Allstate's exclusion for losses "consisting of or caused by ... insects, rodents, birds or domestic animals" applies to Cook's Brown Recluse Spider insurance claim. At the summary judgment hearing, Allstate identified this issue -- whether spiders are insects -- as the essence of this case.

Allstate's opening brief cites a Merriam Webster dictionary's definition of "insects" as "any of numerous small invertebrate animals (as spiders and centipedes) that are more or less obviously segmented." Allstate's brief indicates that this same dictionary's second definition of "insect" is "any of a class (Insecta) of arthropods (as bugs or bees) with well-defined head, thorax, and abdomen, only three pairs of legs, and typically one or two pairs of wings."

Cook cites a children's encyclopedia, an adult encyclopedia, and a scientific article establishing spiders are not insects. All of these materials -- elementary to advanced -- distinguish spiders from insects. For example, spiders have eight legs; insects have six. Spiders have two body parts; insects have three. Cook also cites a Merriam Webster dictionary definition of "spiders" as "a group of arachnids somewhat resembling true insects, but readily distinguishable from them by the four (instead of three) pairs of walking legs . . . ."

Cook is entitled to partial summary judgment if any reasonable policyholder could possibly conclude that a spider is not an insect. *Lilly*, 482 N.E.2d at 471; *Summit*, 715 N.E.2d at 936. The Court finds that as a matter of common and scientific fact, spiders are not insects. The Court further finds that at a minimum, the distinction between spiders and insects raises an ambiguity in Allstate's policy language that must be resolved in favor of coverage.

Thus, Cook is entitled to partial summary judgment that Allstate's "insect" exclusion does not bar coverage for Cook's claim arising from the Brown Recluse Spider infestation at the Home. Allstate is not entitled to summary judgment that its "insect" exclusion applies to Cook's insurance claim.

C. Protection of Property Endangered by a Covered Cause of Loss.

It is undisputed that Cook has had the Home treated by pest control professionals, causing a decline in the Brown Recluse Spider population, even though Cook and his family were unable to live there and Allstate refused to pay any alternative living expenses.

Cook moved for partial summary judgment that Cook did not forfeit coverage by any failure to protect the Home from a covered loss. Allstate made no argument in its briefs or at oral argument regarding the coverage denial reasons state in its August 11, 2006 letter, which claimed that coverage was forfeited because Cook did not "take all reasonable steps to save and preserve property when the property is endangered by a loss we cover" and because of a "substantial change or increase in hazard, if changed or increased by any means within the control or knowledge of an insured person." The Court finds that Cook took the appropriate steps of hiring multiple pest control specialists to treat his Home, which actually decreased the Brown Recluse Spider infestation. Moreover, Allstate failed to designate any evidence to the contrary.

For these reasons, Cook is entitled to partial summary judgment on these two issues.

D. Sudden and Accidental Direct Physical Loss.

Cook and Allstate cross moved for partial summary judgment as to whether the infestation of the Home by Brown Recluse Spiders is a "sudden and accidental direct physical loss" that Allstate's policy covers. Allstate did not raise this coverage defense in its June 23, 2006 and August 11, letters denying coverage. Neither letter reserved Allstate's right to assert further coverage defenses. Allstate stated in its August 11, 2006 letter that it had "completed" its investigation. It also failed to raise this coverage defense in its answers to Cook's complaint or

to his amended complaint. Allstate first raised the new coverage defense seven months after coverage litigation commenced.

The Court finds that the "mend the hold" doctrine, named after a nineteenth century wrestling term, applies. This doctrine "forbids a contract party, particularly when it is an insurance company, to change its position on the meaning of the contract in the middle of litigation over it." *Utica Mut. Ins. Co. v. Vigo Coal Co., Inc.*, 393 F.3d 707, 716 (7th Cir. 2004). In *Walter Powe d/b/a Progressive Cleaning v. American State Ins. Co.*, Cause No. 49D03-0312-CT-2143 (Marion County Superior Court, January 10, 2005), "mend the hold" barred the insurer from raising a new coverage defense after litigation had commenced. Other Indiana decisions (*Brightpoint v. Zurich American Ins. Co.*, 2006 WL 693377 (S.D. Ind. 2006) and *National Casualty Co. v. Floyd County Bd. Of Commissioners*, 2002 WL 31045373 (S.D. Ind. 2002)) declined to apply "mend the hold" where the insurer had reserved its rights to add new coverage defenses. The Court finds these cases persuasive. Allstate did not reserve its rights and waited too long, under the "mend the hold" doctrine, to claim there was no "sudden and accidental direct physical loss."[1]

The Court also finds that the undisputed evidence demonstrates a "sudden and accidental direct physical loss" as a matter of law. The term "sudden" in an insurance policy means unexpected or unintended under Indiana coverage law. *Am States Ins. Co. v. Kiger*, 662 N.E.2d 945, 948 (Ind. 1996). The determination of whether a loss was expected for insurance coverage purposes turns on an examination of the actual subjective mental state of the policyholder rather than an analysis of whether the policyholder should have expected the harm that took place. *PSI*

[1] In the alternative, the Court finds that Allstate has waived this claim. *Protective Insurance Company v. Coca-Cola Bottling Company Indianapolis Inc.*, 423 N.E.2d 656, 662 (Ind. Ct. App. 1981). Cook has been prejudiced by not being able to properly investigate this assertion.

Energy, Inc. v. Home Insurance Company, 801 N.E.2d 705, 728 (Ind. Ct. App. 2004). Expectation or intent is inferred only when "the evidence is so overwhelming as to mandate the court to conclude that, from the very nature of an insured's actions, harm must have been intended." *Auto Owners Ins. Co. v. Harvey*, 842 N.E.2d 1279, 1289 (Ind. 2006).

Cook designated evidence that he did not subjectively expect or intend the Brown Recluse Spider infestation. This evidence controls. The only counter-evidence is that Cook saw spiders in the Home before he bought it and did not have the Home inspected. This does not demonstrate subjective expectation or intent, does not raise an inference that Cook subjectively expected or intended the Brown Recluse Spider problem and does not raise a disputed issue of material fact.

Case law demonstrates that a physical condition that renders property unsuitable for its intended use constitutes a "direct physical loss" even where some utility remains and, in the case of a building, structural integrity remains. In *Matzner v. Seaco Ins. Co.*, 1998 WL 566658 (Mass. Sup. Ct. August 12, 1998), cited by Allstate, a building with unsafe levels of carbon monoxide from a chimney blockage by an old galvanized pipe sustained a "direct physical loss." In *Western Fire Ins. Co. v. First Presbyterian Church*, 437 P.2d 52, 55 (1968), also cited by Allstate, a church with fumes and vapors caused by gasoline contamination of the underlying soil sustained a "direct physical loss." *See also Gen. Mills, Inc. v. Gold Medal Ins. Co.*, 622 N.W.2d 147, 150–152 (Minn. Ct. App. 2001) (raw oats that could not be incorporated into a product because they had been treated with an unapproved pesticide sustained a "direct physical loss"); *Murray v. State Farm Fire & Cas. Co.*, 509 S.E.2d 1, 17 (W. Va. 1998) (home subject to a risk of falling rocks sustained a "direct physical loss.")

Brown Recluse Spiders living, breeding and hunting on and within surfaces of the Home

are a physical condition that renders the Home unsuitable for its intended use. The undisputed evidence is that the Brown Recluse Spiders make it unsafe for Cook and his very young children to live in the home and also that Cook has not been able to sell the Home, even at a loss.

Thus, Cook is entitled to partial summary judgment that there has been a "sudden and accidental direct physical loss" that triggers coverage. Allstate is not entitled to summary judgment that there has been no "sudden and accidental direct physical loss."

E. Damages.

Cook designated evidence that the dwelling coverage limit under the homeowners policy he purchased from Allstate to cover the Home is $187,000. Cook designated evidence that his alternative living expenses for two twelve month policy periods at $940 per month amount to $22,500.

III. ORDER

The Court, having found in favor of Cook and against Allstate, now enters partial summary judgment in favor of Cook and against Allstate as to the availability of coverage. Allstate's motion for summary judgment is denied. The Court directs that the issue of damages shall be considered at trial.

Dated: November 30, 2007

HON. JACK L. BRINKMAN, JUDGE
MADISON SUPERIOR COURT, DIVISION II

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