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The Pandemic Vs. The Policyholder: COVID-19 And Business Interruption Coverage Claims

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Early 2020 will likely be remembered for the flurry of announcements about the coronavirus – from the World Health Organization declaring COVID-19 a Global Health Emergency on January 31 to California's move to become the first state to force businesses deemed "non-essential" to close on March 19.

As a result of these orders, millions of businesses across the country chose or were forced to close their doors to the clientele that kept their businesses operational. Restaurants and bars, hair and nail salons, and spas, daycare centers, and health clubs were hit hardest, as many state and local governments deemed them "non-essential," forcing their doors closed for longer periods of time, without the promise of regular income.

For many, insurance coverage was a means to preserve their business throughout the ensuing pandemic and to keep doors open and staff employed. Facing coverage denials from their insurers, many policyholders took to the courts, often with the survival of their businesses hanging in the balance.

As of August 24, 2021, hundreds of lawsuits had been filed by policyholders, seeking breach of contract damages, arguing that their insurance policies provided coverage for business interruption losses and other extra expenses associated with a COVID-19 outbreak on the premises (and related sanitation costs) for which their insurers wrongfully denied coverage. Approximately 500

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of these lawsuits have been decided in nearly every state across the country. Unfortunately for policyholders, the trend courts have endorsed – and particularly so in federal courts – is that the insurers' interpretation of their policies are generally correct.

Of the nearly 500 cases to date, only nine had outcomes on the side of the policyholder where policyholders have won coverage on a motion for summary judgment. Policyholders have fared better at defeating insurers at the motion to dismiss phase, where the insurers generally argue that the policyholder failed to state a claim upon which relief can be granted on the basis that the policy at issue unambiguously excludes the coverage the policyholder seeks. On motions to dismiss, policyholders have succeeded in defeating insurers' arguments for unambiguous non-coverage of COVID-19-related claims 23 times where the policy has contained a virus exclusion and 30 times where the policy at issue did not contain a virus exclusion.

Predictably, the courts that have decided against the policyholder most often have done so where the policy contained a virus exclusion purporting to exclude from coverage loss or damage caused by "any virus, bacterium or other microorganism that induces or is capable of inducing physical distress, illness or disease" or otherwise containing similar language. These exclusions generally apply to both direct and indirect causes of loss, making them appear, at first blush, very broad. However, as discussed further below, if you as a policyholder are still waging this battle in court, all is not lost, even if your policy contains a virus exclusion.

Coverage for COVID-19-related losses typically arises from coverages for "direct physical loss of or damage to property" in the form of business interruption coverage, most often provided in commercial property policies. These provisions generally contain language providing coverage for "actual loss of 'business income' you sustain due to the necessary 'suspension' of your 'operations' during the 'period of restoration.'" Such suspension of business operations generally "must be caused by direct physical loss of or damage to" covered property.

Alongside business interruption coverage comes "Civil Authority" coverage, which generally covers loss of business income, for example, as a result of "necessary 'suspension' or delay in the start of your 'operations' if the 'suspension' or delay is caused by order of civil authority that prohibits access to the 'premises'" or similar language. Such "order of civil authority" generally must be due to a civil authority's response to "direct physical loss of or damage to property" located within a certain radius of the covered property. Civil Authority coverage often has a "waiting period" deductible and a reduced sublimit for losses sustained.

Policyholders across the country have generally argued that one or both, depending on whether a policy provides coverage for both, apply to provide coverage for their COVID-19-related losses stemming from closure due to COVID-19 government shutdown orders or, conversely, closure due to a COVID-19 outbreak and the requirements of social distancing.

In general, these policyholders have argued that they "lost" the physical space in which their businesses operate due to government orders mandating closure or closure due to a COVID-19 outbreak on the premises, thus entitling them to coverage for business interruption expenses and/or civil authority coverage stemming from "loss of" their property. These arguments have met with some success in response to insurers' motions to dismiss and policyholders' motions for summary judgment. The courts that have accepted

these arguments generally have done so on the basis of insurance policy interpretative principles: namely, that different words in a policy must have distinct meanings. Courts have recognized that where insurers offer coverage for “loss of or damage to property,” “loss of” property may be ambiguous, as “loss of” property must have a different meaning than “damage to” property.

As noted above, one of the larger pitfalls to coverage arguments is the virus or “pollutant” exclusion. Generally, insurers have argued, and courts have accepted, that any losses – whether business interruption, civil authority, or cleanup and sanitation costs – stemming from the COVID-19 pandemic are excluded under such provisions. However, policyholders have had success arguing against the application of these provisions in two primary ways. First, insureds have made causation arguments, arguing that closure due to government orders is not closure because of the virus itself, but rather the government mandate. In other words, the business would have stayed open in the face of the global pandemic, but for the state or local government’s requirement otherwise. Second, policyholders have argued that, where closure was not a direct result of a COVID-19 outbreak within the business, the virus exclusion should not apply, as such exclusions are designed to exclude coverage for costs associated with clean up and sanitation after a viral or bacterial outbreak on a business’ premises.

Some federal courts, rather than deciding these important – and novel – issues of policy interpretation have instead certified questions to state supreme courts for the highest state authority to determine definitively whether coverage may exist for COVID-19-related claims. Many states have such questions currently pending for decision.

As the COVID-19 pandemic begins to wane in the face of mass vaccination and herd immunity across the United States, there is light at the end of the tunnel for businesses who have fought and succeeded in remaining open despite over a year of turmoil. However, for those still battling in the courts for insurance coverage, a final coverage determination may not be available for years to come, as the surviving policyholders make their way to trials and further motions practice in support of their breach of contract claims.

Yet there is hope. Although most courts have decided against the policyholder, there remain those that have decided in the policyholder’s favor. As these lawsuits work their way through appeals, the unfavorable decisions may be overturned. For now, these policyholders must simply hang on and continue to fight, in hopes that the tides may turn in their favor.

This article was originally published in the 2021 edition of Corporate Policyholder Magazine.

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[1] https://www.ajmc.com/view/a-timeline-of-covid19-developments-in-2020

[2] https://cclt.law.upenn.edu/judicial-rulings/

[3] See, e.g., Henderson Road Restaurant Systems Inc. v. Zurich American Insurance Co., Case No. 1:20-cv-01239 (N.D. Ohio January 19, 2021).

[4] https://cclt.law.upenn.edu/judicial-rulings/

[5] See, e.g., Ceres Enterprises, LLC v. Travelers Insurance Co., Case No. 1:20-cv-01925, at 5 (N.D. Ohio February 18, 2021).

[6] See, e.g., id.; Neuro-Communication Services v. Cincinnati Insurance Co., et al., Case No. 4:20-cv-01275 (N.D. Ohio January 19, 2021); Cherokee

Nation; Cherokee nation Businesses, LLC; Cherokee Nation Entertainment, LLC v. Lexington Insurance Co. et al., Case No. CV-2020-00150 (Okla. Dist. Ct., Cherokee Cnty. January 14, 2021); and Goodwill Industries of Orange Cnty, Cal. vs. Philadelphia Indemnity Ins. Co., Case No. 30-2020-01169032-CU-IC-CXC (Supr. Ct. Cal., Orange Cnty. January 28, 2021).

[7] See, e.g., Henderson Road, Case No. 1:20-cv-01239.

[8] See, e.g., Neuro-Communication, Case No. 4:20-cv-01275.