

March 16, 2020

COVID-19

Coverage Considerations for Property and Liability Insurance

The extraordinary challenges arising from the COVID-19 virus will affect every aspect of our society. Within the insurance industry, insurers are bracing for a surge of claims across multiple policy lines. The first wave has already begun, and the focus is on property and general liability coverage. This brief memorandum will highlight some of the issues and provide a framework for analyzing coverage questions as they initially arise.

Property Insurance

There will be claims for loss of property and loss of income under business interruption coverage. COVID-19 has caused widespread economic disruption, and countless cases of disrupted or delayed business operations. The New York Department of Financial Services has already issued a notice to carriers requiring an explanation as to available coverage under policies issued in New York and legislators in New Jersey are considering legislation that would effectively negate certain policy exclusions.

Clearly, an intense focus in the coming months and beyond will be on the availability of business interruption and contingent business interruption coverage, where applicable. The specific facts, the specific policy language, and the governing law all need to be analyzed and evaluated, but here are some of the key points.

Direct Physical Loss. Most property policies require that the loss be caused by a “direct physical loss” or “physical damage” to insured property. Generally, this does not include the threat of a communicable disease. Shuttering a business merely due to fears of the coronavirus, where a building remains habitable, will likely not meet the direct physical loss requirement.

Even if there is no “physical damage,” there may be arguments that the “loss of use” of property that is unusable because of contamination constitutes “physical loss.” For example, where an infected person has been inside of a property and physically contaminated it (including the HVAC system), that may be used to support the argument that there is direct physical loss under the policy. Analyzing these arguments is intensely fact-specific.

Some policies or provisions may specifically extend to an insured’s supply chain. For example, a business which relies on services, parts, equipment, or completed products

from China, Italy, or other affected countries may lose income. Also, damage to customers may affect business income. Coverage for losses relating to suppliers or customers is referred to most often as “Contingent Business Interruption” coverage. It, too, typically requires direct physical loss or damage to property of a “direct” supplier or customer, at times within designated geographic areas. Some policies limit coverage to specifically-identified suppliers and customers.

Governmental or Civil Authority Order. Policies may have provisions or extensions providing coverage when a governmental authority prohibits or impairs access to a building or property. Typically, these require physical damage to one of the insured’s covered locations. In some policies, coverage might extend to loss when a governmental authority restricts access to an insured’s location because of physical damage to adjacent property. The waiting period for these coverages is often relatively short, *e.g.*, 72 hours.

Policies with Supply Chain or Contingent Business Interruption coverage may also be implicated when the loss is related to the authority’s establishment of quarantine zones, or suspending services, travel or transport. Until recently, these would be connected most often to China or Italy, and could be especially present in, for example, the textile and apparel industries. However, several states have required all bars and restaurants to close their doors, with more closures certain to follow suit. Again, whether these governmental orders and the resulting loss of business trigger coverage will depend on policy language, the language of the civil order and the status of the law in that particular jurisdiction. Clearly, this is a rapidly evolving threat.

Ingress/Egress Extension. These could afford coverage without a governmental or civil authority order, but still typically would require physical damage to property that hinders access to the insured’s property.

Communicable Disease Exclusions. After the SARS outbreak in 2003, some insurers began to add exclusions covering bacteria, viruses, and infectious diseases. However, there is no standardized clause. Some apply only to bacteria, so would not extend to COVID-19, which is a virus. But other exclusions expressly extend to viruses. In 2006, ISO introduced, and regulators approved, an “Exclusion for Loss Due to Virus Or Bacteria.” It is directed toward first-party property insurance and expressly applies to loss of business income. The American Association of Insurance Services has a similar exclusion. Also, some policies issued in 2020 have express Coronavirus exclusions. As discussed below, New Jersey is considering legislation that would attempt to render these exclusions inapplicable.

Infectious Disease Extensions. Conversely, some policies affirmatively extend coverage when an order of a competent public authority is made as the result of “an

infectious or human contagious disease.” Sometimes, however, the clause requires that the infectious disease be present at the insured’s covered location. Others use the wording that coverage requires “the actual not suspected presence of a communicable disease.”

Extraordinary Regulatory Requirements in New York. On March 10, 2020, the New York Department of Financial Services (“DFS”) issued a letter to All Authorized Property/Casualty Insurers entitled “Call for Special Report Pursuant to Section 308, New York Insurance Law: Business Interruption and Related Coverage Written in New York.” It requires a report on the insurers’ commercial property insurance, defined to consist of business owner policies, commercial multiple peril policies, specialized multiple peril policies, and “substantially similar” insurance. It also requires information and an explanation of coverage of in-force policies providing business interruption coverage, civil authority coverage, contingent business interruption coverage, and supply chain coverage. Insurers are directed to examine these policies and “explain the coverage each policy offers in regard to COVID-19 -- *both presently and as the situation could develop* to change the policyholder’s status (i.e., *is there any potential for coverage* as a result of COVID-19).” (Emphasis added.) The insurers are also to send such explanation to each policyholder.

The DFS requires, in essence, that both the report to DFS, and the explanation to policyholders, make blind and premature coverage evaluations. For example, it asks whether contamination related to a pandemic may constitute “physical damage or loss.” It asks “what type of damage or loss is sufficient for coverage” under the various categories. It is truly extraordinary. And the letter, once again dated March 10, 2020, *directs a response by March 18, 2020.*

Legislative Initiative in New Jersey. The New Jersey Legislature is currently considering a proposed law with unique scope and effect. In its current form, it would require business interruption coverage for COVID-19 losses even if the policy contains a virus exclusion, including those approved by the regulators. It applies to policies in force on March 9, 2020, issued to insureds with fewer than 100 full-time employees in New Jersey, who work 25 or more hours a week. It would extend coverage “for the duration of the declared State of Emergency,” even though business interruption coverage is never open-ended. The only limit would be the policy limit. The draft would allow some recoupment of the forced payments from an “additional special purpose apportionment” on carriers insuring risks in New Jersey.

It is unclear how a statute such as this would interact with the other requirements for business interruption coverage, notably the requirement of direct physical loss or damage.

The legislature is probably assuming that requirement would be overridden, which would be an even more remarkable extension of coverage.

There may be substantial grounds to challenge many variations of this statute under the New Jersey and United States Constitutions.

Similar legislation is likely to be introduced in other states.

General Liability Insurance

Coverage A. Any business open to the public faces exposure to claims that it did not take adequate measures to prevent the transmission of the virus. Claims could be based on failures in security, cleaning, maintaining adequate filtration systems, or on simply remaining open for business. They could arise from attempts to link claimants' infections directly to employees' infections. For example, plaintiffs have already commenced a lawsuit against Princess Cruise Lines Ltd. for gross negligence for failing to take precautions to clean a ship and prevent an outbreak after two passengers on a prior cruise had symptoms.

There could also be claims for third-party property damage, as well. If an insured's action or inaction negatively affects another business, the latter could claim it experienced the "loss of use" of its property.

Coverage B. There could be claims that forced quarantines fell within the scope of wrongful detention or imprisonment.

Each claim will require analysis of the specific facts and the specific policy language, against the background of the controlling state law. Potentially important provisions are described below.

Is there an Occurrence or Accident? The basic grant of liability coverage often extends to bodily injury caused by an "occurrence," often defined as "an accident, including continuous or repeated exposure to substantially the same general harmful conditions." Does failure to prevent exposure to COVID-19 fit into this definition? Given the inherent flexibility of the words and the variations in interpretation of "occurrence" and "accident" across the states, it seems inevitable that this will be a widely litigated issue.

Mold Exclusions. These should be parsed closely. Many encompass far more than mold, and extend to fungi or bacteria. But typically, they do not extend to viruses, so in some cases would not exclude COVID-19.

Communicable Disease Exclusions. Although not common in liability policies, some liability policies contain exclusions for bodily injuries arising from the “transmission of a communicable disease, virus, or syndrome.”

Conclusion

COVID-19 presents a supremely challenging claims matrix in all respects. The policy provisions and related coverage issues outlined herein provide an overview, rather than an exhaustive list, of those potentially in play as this situation develops further. We anticipate that, as with recent post-natural disaster scenarios, individual states’ insurance regulators may, at least initially, take varying approaches to securing this coverage for insureds within their jurisdictions, but over time, there will be intense focus on leveraging these coverages for broad swaths of insured business sectors.

Gfeller Laurie LLP’s coverage attorneys have extensive experience in such first- and third-party coverage claims and regulators’ involvement under similar circumstances, including but not limited to the issues outlined in this alert. We have direct experience handling such claims and related client counseling as to insurance department relations throughout New England, New York, New Jersey, Georgia, South Carolina and North Carolina.

If we can be of further assistance, please contact the Gfeller Laurie LLP attorney with whom you regularly communicate, or one of our COVID-19 Coordinators, Elizabeth Ahlstrand (eahlstrand@gllawgroup.com, 860-760-8420), Vince Vitkowsky (vvitkowsky@gllawgroup.com, 212-653-8870), or Melicent Thompson (mthompson@gllawgroup.com, 860-760-8446).

Sincerely,

[Gfeller Laurie LLP](#)

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