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COVID-19 Insurance Coverage Litigation Update

In early July, a court handed down a substantive, on-the-merits ruling on business interruption coverage under a property policy following government orders. The Court ruled for the insurer. There have been many additional complaints filed of a similar nature, most with the standard allegations. But one complaint has presented a new theory not previously described in our Updates: regulatory estoppel. A few others raised unusual allegations. Also, a large provider of hospital and health care facilities initiated an action under a Healthcare Premises Pollution Liability Policy for losses in connection with COVID-19.

In this Update, we review those cases and we also present a preview of the disputes likely to arise under reinsurance contracts due to COVID-19.

Case Activity of Special Interest

Gavrilides Mgmt. Co., et al. v. Michigan Insurance Co., Case No. 20-258-CB-C30 (Cir. Ct. Ingham County MI) (Judge Dragabchuk), decision rendered July 1, 2020. This is believed to be the first substantive, on-the-merits ruling on business income coverage under a property policy. The court ruled in favor of the insurer, from the bench, following an argument conducted via Zoom. Plaintiffs alleged that stay-at-home Executive Orders from the Governor had the effect of denying physical access to their restaurants, resulting in a loss of *use* of the property. However, the policy did not insure against loss of use. Instead, it required that for business income coverage, there be "direct physical loss of or damage to the [insured's] property." The court held that direct physical loss of or damage to property must be something with *material existence,* something that is *tangible*, something that alters the *physical integrity* of the property and found that the complaint before it did not contain allegations to that effect. Importantly, the insured did allege that at no time had COVID-19 entered the restaurants through an employee or patron, which allegation the court held foreclosed any possibility that the plaintiff could remedy the problem of failure to allege direct physical loss of or damage to property by amending its complaint. The court also applied the policy's Virus Exclusion, holding that even if direct physical loss of or damage to property had been alleged, the Virus Exclusion applied to bar coverage. The Zoom hearing can be viewed here.

1 S.A.N.T., Inc. v. Berkshire Hathaway Inc., et al., Case No 2:05-mc-02025 (U.S.D.C., W.D. PA), filed June 11, 2020. Plaintiff is a restaurant, tavern and banquet hall seeking business income coverage under an all-risk Commercial Property Coverage policy with a Virus Exclusion. The Defendants are Berkshire Hathaway, Inc. and its risk-bearing subsidiary National Fire & Marine Insurance Company (collectively, "Berkshire"). Plaintiff seeks certification as a class action, making the usual arguments that its covered property suffered "direct physical loss or damage" due to state and local governmental

shut down orders and that apart from the orders, the COVID-19 pandemic and ubiquitous nature of the virus caused direct physical loss of or damage to covered property.

Plaintiff makes an additional, novel argument: that Berkshire should be estopped from enforcing the Virus Exclusion on principles of regulatory estoppel. It alleges misrepresentations were made in 2006 by two insurance trade groups, Insurance Services Offices, Inc. and the American Association of Insurance Services, while seeking approval from state insurance regulators. It argues that the trade groups were acting on behalf of hundreds of insurers, including Berkshire, implicitly arguing that the conduct of the trade associations should be attributed to Berkshire.

Specifically, Plaintiff alleges that in their filings, the trade groups "represented that the adoption of the Virus Exclusion was only meant to 'clarify' that coverage for 'disease-causing agents' has never been in effect, and was never intended to be included, in the property policies." Plaintiff alleges this was false because by 2006, "[c]ourts had repeatedly found that property insurance policies covered claims involving disease-causing agents, and had held on numerous occasions that any condition making it impossible to use property for its intended use constituted 'physical loss or damage to such property.'" Plaintiff alleges that by misrepresenting that the Virus Exclusion would not change the scope of coverage, "the insurance industry effectively narrowed the scope of the insuring agreement without a commensurate reduction in premium charged."

Berkshire Hathaway moved to dismiss for lack of personal jurisdiction and failure to state a claim against it. National Fire provided the substantive arguments, referring to the regulatory estoppel argument as a "Hail Mary." Regulatory estoppel only operates if, in the litigation, the insurer takes a position opposite to the one presented to the regulators. National Fire argues that it did not change its position and stands by the statements of the trade groups. Further, National Fire argues that Plaintiffs have made no allegations of bad faith and that there is "zero controlling authority" holding that regulatory estoppel has any relation to original statements made during the approval process.

National Fire further specifies that plaintiff is trying to alter the doctrine of regulatory estoppel. Under existing law, a purportedly false original statement is irrelevant under that doctrine. The relevant element is a change in position. A court can readily determine on the face of the pleadings whether a party has changed its position, but it cannot determine on the face of the pleadings whether an allegedly false statement is, in fact, false. National Fire's position is that if regulatory estoppel were to be based on a purportedly false statement, discovery and, potentially, trial, would be necessary to make a ruling and consequently, the Virus Exclusion could not be enforced on a motion to dismiss.

Dime Fitness, LLC v. Markel Insurance Co. (Thirteenth Judicial Circuit, Hillsborough Co. FL), filed July 6, 2020 and ***The Rivers Edge Enterprises, LLC v. Scottsdale Insurance Co.*** (Thirteenth Judicial Circuit, Hillsborough Co. FL), filed July 7, 2020. These complaints allege that the Virus Exclusion does not apply because it "was only meant to exclude the cost of damages to either the insured location or the insured's products when a virus specifically infected the insured location" and there "is no allegation that the insured property was specifically affected by the COVID-19 virus." The attempt to avoid the Virus Exclusion on a theory like this may have been the reason the plaintiff in ***Gavrilides***

made similar allegations, but by doing so, it fatally undermined its position in that case concerning "loss of or damage to property," as discussed above.

Northwell Health, Inc. v. Illinois Union Ins. Co., (Sup. Ct, N.Y. Co.), filed July 24, 2020. The insured is the leading provider of hospitals and outpatient facilities in the New York City metropolitan area and a leading provider of healthcare services to COVID-19 patients. It sued one of the companies in the Chubb group for coverage under a Healthcare Premises Pollution Liability Policy. The Policy provides coverage for "emergency response costs" and "decontamination costs" arising out of "facility-borne illness events" and for "remediation costs" and "emergency response costs" arising out of "pollution condition." It also provides coverage for business interruption loss that is directly attributable to a "covered pollution condition." The complaint is vague on specific expenses, noting generally that the insured transformed its facilities and operations to respond to COVID-19 needs. It mentions a few items, including the costs of additional beds, personal protective equipment and around-the-clock staffing. The complaint alleges "the most significant drivers of the losses have been the forced cessation of elective surgeries, the closing of physician's practices, and fewer hospital admissions and visits to or uses of Northwell's other medical facilities due to the pandemic." The complaint does not tie these general categories into insured costs.

"Facility-borne illness event" is defined in the policy as "the presence of a facility-borne infectious virus … provided that such facility borne virus is not … solely or exclusively the result of communicability through human-to-human contact." The complaint alleges Chubb denied coverage because a facility-borne illness event is generated by the facility itself and COVID-19 is communicable through human-to-human contact. The insured responded by providing scientific studies showing COVID-19 could spread after contact with infected objects and a wide range of surfaces. The insured alleges that each facility is "a building in which coronavirus comes walking in the door every single day and it must be assumed is present in the air and on surfaces at all times." If there were coverage under the section, the insured could recover expenses for certain first-party emergency response costs and decontamination costs.

"Pollution condition" does not expressly include viruses. The insured alleges the definition of pollution conditions encompasses the presence of hazardous substances or materials and waste materials including infectious wastes. Chubb denies this on the ground that "COVID-19 is an infectious communicable disease caused by a virus, not pollution."

Anticipating COVID-19 Reinsurance Issues

If coverage were found to exist under some direct insurance policies, the one reinsurance issue certain to arise is aggregation. Aggregation always fascinates, because it can affect both deductibles and limits, so the position an insurer or reinsurer ultimately takes will depend entirely on the unique factual matrix.

Like other reinsurance issues, if a dispute is being resolved by arbitration in the United States under a contract containing an "honorable engagement" clause, the panel is not bound to follow the "strict

rules of law." Thus, the outcome will depend on the contract language, the presentation at the hearing and the preparation of that presentation with respect to the treatment of losses.

As always, the most important factor is the contract language. Aggregation clauses allow two or more separate losses to be treated as a single loss, triggering a single deductible or a single limit. Broadly, there are two kinds of clauses. The first and most common are *occurrence or event-based*. The second are *cause or originating cause-based*.

A typical *occurrence or event-based* clause would define "loss occurrence" as "all individual losses directly occasioned by any one disaster, accident or loss or series of disasters, accidents or losses arising out of one event," or words to that effect. Even in U.S. arbitrations, English case law is sometimes cited as persuasive authority. It generally applies a "unities test" to these *occurrence or event-based* clauses, which requires the losses to be connected by a measure of unity of cause, locality, and time. This is an inherently subjective test.

A typical *cause or originating cause-based* clause would allow for the aggregation of "each and every loss arising out of one cause/originating cause," or words to that effect. Under English law, a "cause" is less restricted than an "event." Generally, it permits aggregation of a wider range of losses. For example, a cause can be a continuing state of affairs, or the absence of something happening.

Under United States law, there are many cases dealing with aggregation in the insurance context. The majority of courts tend to apply causation-based approaches. There is, however, one leading case addressing aggregation under a reinsurance contract, *Travelers Casualty & Surety Co. v. Certain Underwriters at Lloyd's of London*, 96 N.Y.2d 583 (2001). Construing *occurrence or event-based* language, it held that pollution-related damages at several sites over several decades, having no "spatial or temporal relationship," could not be aggregated into a single loss.

With respect to COVID-19 losses, there are several options for possible aggregation. A company could argue, for example, that:

- a global pandemic is a single cause or originating cause, wherever and however it spreads;
- the governmental orders to restrict commerce and enforce lockdowns constitute a series of losses arising out of one event; or
- more narrowly, the governmental orders within a single state or region have a sufficient spatial or temporal relationship to qualify as a single loss.

Virtually every problem eventually becomes an insurance problem and ultimately, a reinsurance problem. COVID-19 is no different.

For more information, please contact the Gfeller Laurie LLP attorney with whom you regularly communicate, or one of our COVID-19 Coordinators:

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Sincerely,

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