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COVID-19 Insurance Coverage Litigation

There have been many recent decisions on motions to dismiss or for summary judgment on coverage claims for business income losses due to COVID-19 shutdown orders. By a large margin, most have continued to rule in favor of the insurers. The decisions are based on the absence of direct physical loss or analogous coverage terms, or on the presence of Virus Exclusions, or both. However, there is one important exception in which a North Carolina State court granted summary judgment for an insured, finding that loss of access to restaurants constituted direct physical loss.

We also report in this update on a recent Multidistrict Litigation Panel decision ordering consolidation and transfer of a group of cases against one insurer, Society Insurance Co., and on a new wave of cases claiming failure to protect assets during the COVID-19 era financial market downturn.

Finally, there reportedly will be tennis balls flying at Wimbledon next year!

Decisions Granting Motions to Dismiss Based on Lack of Direct Physical Loss or Damage

Infinity Exhibits, Inc. v. Certain Underwriters at Lloyds' London Known as Syndicate PEM 4000, et al., Case No. 8:20-cv-1605-T-30AEP, 2020 WL 5791583 (M.D. Fla. Sept. 28, 2020). The contingent business income loss claim of a designer and fabricator of trade show displays was dismissed. State executive orders resulted in cancelled trade shows. The Court construed the phrase "direct physical loss or damage" and held that "Florida law and the plain language of the policies reflect that actual, concrete damage is necessary." There were no allegations that the insured's property suffered any actual physical loss or damage. The Court found that any amendment would be futile and dismissed the case with prejudice.

Oral Surgeons, P.C. v. The Cincinnati Ins. Co., Case No. 4-20-CV-222-CRW-SBJ, 2020 WL 5820552 (S.D. Iowa Sept. 29, 2020). The claims of dentists were dismissed because there was no "direct 'loss' to property," and "loss" was defined to mean "accidental physical loss or accidental physical damage." There were no allegations of "physical" or "accidental" loss, and the case was dismissed with prejudice at the insured's cost.

Henry's Louisiana Grill, Inc., et al., v. Allied Ins. Co. of America, Case No. 1:20-CV-2939-TWT, 2020 WL 5938755 (N.D. Ga. Oct. 6, 2020). The claims of a restaurant and affiliated party space were dismissed. The Court construed the phrase "direct physical loss of or damage to" the covered property. It found that an executive order did not have a "direct" effect on the insured under Georgia law. Also, plaintiff alleged that unless the phrase "loss of" was construed to mean "physical spatial loss of their dining rooms," the use of two phrases, "loss of" and "damage to," would be surplusage. The Court examined common dictionary definitions and concluded the two

terms could be reconciled by the understanding that "loss of" means total destruction and "damage to" means some lesser amount of harm or injury. The Court denied Civil Authority Coverage, holding that the applicable executive order did not prohibit access to the premises, nor were there any allegations that that areas immediately surrounding the properties were blocked. The decision did not specify whether the dismissal was with prejudice. However, the Policy also had a Virus or Bacteria Exclusion which the Court stated it did not need to analyze.

Hillcrest Optical, Inc. v. Continental Cas. Co., Case 1:20-cv-00275-JB-B, 2020 WL 6163142 (S.D. Ala. Oct. 21, 2020). The claim for business income losses of an optometrist who shut down operations in compliance with an executive order was dismissed with prejudice. The insured conceded the Civil Authority Endorsement provided no coverage, and there was no Virus Exclusion. That left the claim for Business Income and Extra Expense. The Court denied the insured's request for certification to the Alabama Supreme Court and described the issue as "whether a temporary inability to use property due to governmental intervention constituted a direct physical loss of property." It held that direct physical loss requires a tangible alteration of property, so there was no coverage. The insured also argued that the presence of a "period of restoration" in the policy contemplates that the inability to use property constitutes a direct physical loss. The Court rejected this, holding that the period of restoration "expressly assumes repair, rebuild or replacement of property."

Decisions Granting Motions to Dismiss Based on Lack of Direct Physical Loss or Damage and a Virus Exclusion

It's Nice, Inc. v. State Farm Fire and Cas. Co., Case No. 2020L000457 (Cir. Ct., 18th Jud. Ct. Ill. Sept 29, 2020). Ruling from the bench in a videoconference hearing on a case involving a restaurant, the Court granted a motion to dismiss with prejudice. The Court ruled that direct physical loss "unambiguously requires some form of actual physical damage to the insured's premises" and that alleged intangible or incorporeal losses are not covered. Alternatively, the Virus Exclusion would bar coverage.

Mark's Engine Company No. 28 Restaurant, LLC v. The Travelers Indemn. Co. of Connecticut, Case No. 2:20-cv-04423-AB-SK, 2020 WL 4283958 (C.D. Cal. Oct. 2, 2020). The claims of a restaurant were dismissed with prejudice because the Court found that "direct physical loss of or damage to property" does not include loss of use but rather requires a "distinct, demonstrable physical alteration." The Court relied heavily on, and quoted extensively from, *10E, LLC v. Travelers Ind. Co. of Connecticut, et al.*, 2020 WL 5359653 (C.D. Cal. Sept. 2, 2020). Alternatively, there was no "direct physical loss" because the insured always had complete access to its premises.

The Policy also contained a Virus Exclusion stating that "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." The Court concluded the exclusion "applies here and precludes all coverage."

Kenneth Seifert d/b/a The Hair Place, et al., v. IMT Ins. Co., Civil No. 20-1102 (JRT/DTS), 2020 WL 6120002 (D. Minn. Oct. 16, 2020). The claims of a hair salon and barbershop were dismissed. The Court held that under Minnesota law, "mere loss of use of function" does not constitute "direct physical loss or damage" but rather that "actual physical contamination of the insured property is still required." The insured made no such allegations. There was no Civil Authority coverage because there were no allegations of contamination of neighboring businesses, nor a prohibition of entering the insured's business.

There was a Virus Exclusion with the same language as *Mark's Engine Company, supra.* Although not identified or analyzed in *Marks's Engine Company*, the provision begins with anti-concurrent cause language. The Court held that the Virus Exclusion would extend to "all losses where a virus is part of the causal chain," as it was here, so the Exclusion applied. However, the Court took pains to say that "it is possible that [the insured's] claims [for lost business income] may survive if properly alleged" and granted leave to amend. It is not clear why this was done in view of the definitive ruling on the Virus Exclusion.

Travelers Cas. Ins. Co. of America v. Geragos and Geragos, Case No. 2:20-cv-03619-PSG-E, 2020 WL 6156584 (C.D. Cal. Oct. 19, 2020). A law firm's counterclaims were dismissed. The Court found no Civil Authority Coverage because COVID-19 was the "primary root cause" for the closing and thus was precluded by the Virus Exclusion (with the same language as in *Mark's Engine Company, supra*). The Court went on to hold that loss of use does not constitute direct physical loss or damage. Like *Mark's Engine Company*, it relied on and quoted extensively from *10E, LLC v. Travelers Ind. Co. of Connecticut, et al.*, 2020 WL 5359653 (C.D. Cal. Sept. 2, 2020). Concluding that amendment would be futile, the Court denied leave to amend.

Case Voluntarily Dismissed After Tentative Ruling Based on Lack of Physical Loss or Damage

Plan Check Downtown III, LLC v. AmGuard Ins. Co., et al., Case No. 2:20-cv-06954-GW-SK, 2020 WL 5742713 (C.D. Cal. Sept. 16, 2020). A restaurant accepted dismissal with prejudice following a Tentative Ruling. Construing the phrase "direct physical loss of or damage to," the Court held that "loss" and "damage" "are the default, catch-all terms for referring to what the insured is protected against," and that "the weight of California law also appears to require some tangible alteration, no matter whether the trigger language uses 'loss' or 'damage.'" Finally, it also relied on the recent California case of *10E, LLC v. Travelers Ind. Co. of Connecticut, et al.*, 2020 WL 5359653 (C.D. Cal. Sept. 2, 2020). The Policy also contained a Virus Exclusion which the Court did not address.

Decision Granting Motion to Dismiss Based on Virus Exclusion

Rhonda Hill Wilson, et al. v. Hartford Cas. Co., et al., Case No. 2:20-cv-03384-ER, 2020 WL 5820800 (E.D. Pa. Sept. 30, 2020). An attorney's claim was dismissed because of a Virus Exclusion. The version at issue provides that the insurer "will not pay for loss or damage caused directly or indirectly by … [p]resence, growth, proliferation, spread or any activity of 'fungi', wet rot, dry rot, bacteria or virus." It also contains anti-concurrent cause language. There is an exemption when the virus is the result of "(1) A 'specified cause of loss' other than fire or lightning" or "(2) Equipment Breakdown Accident." The Court did not apply the exemption, simply stating that "[P]laintiffs do not attempt to plead any factual allegations that would allow the Court to reasonably infer that the virus is a result of a 'specified cause of loss' or equipment breakdown." Leave to amend was denied because amendment "would be futile."

Boxed Foods Company, LLC, et al., v. California Capital Ins. Co., Case No. 20-cv-04571-CRB, 2020 WL 6271021 (N.D. Cal. Oct. 26, 2020). Two restaurants commenced a putative class action seeking Business Income, Extra Expense and Civil Authority Coverage. Their claims were dismissed without prejudice. The Court relied solely on the "Virus Exclusion" (the actual name of the exclusion was "Pathogenic Organisms Exclusion") which provided that "[W]e do not insure for loss or damage caused by, resulting from, contributing to or made worse by the actual, alleged or threatened presence of any pathogenic organism, all whether direct or indirect, proximate or remote, or in whole or in part caused by, contributed to or aggravated by any physical damage insured by this policy …." The Court held that this excludes viruses as a Covered Cause of Loss. It rejected arguments that the Exclusion only applied to property damage, whereas the Civil Authority provision applies to business income and extra expenses. The Court found that no such limitation appeared in the Virus Exclusion even though other (non-applicable) exclusions stated they did not apply to certain provisions. The Court also concluded that the COVID-19 virus was the "efficient proximate cause" of the losses.

The insureds argued that the Virus Exclusion was ambiguous because it did not specifically use the word "pandemic." The Court stated that "the word 'pandemic' describes the disease's geographic prevalence, but it does not replace disease as the harm-causing agent." It held that "the Virus Exclusion is only subject to one reasonable interpretation: that coverage does not extend to any claim premised on virus-induced damage, regardless of the virus's magnitude." Also, the Court declined to apply the reasonable expectations doctrine because "the policy's language is clear and unambiguous." Further, in an extended discussion, the Court rejected the claim that evidence of ISO's intent would be relevant to this dispute and could be attributed to the insurer. The Court reached its decision despite starting it by expressing its sympathies to the small businesses affected or destroyed by the pandemic. In its final footnote, it took pains to say that "[T]he Court's holding should not be construed to necessarily apply to all virus exclusions. The Virus Exclusion [at issue here] casts an exceptionally wide net relative to other virus exclusions because it lacks relevant limitations and ambiguous language."

Vizza Wash, LP d/b/a The Wash Tub v. Nationwide Mut. Ins. Co., et al., Case No. 5:20-cv-00680-OLG (U.S.D.C., W.D. Tex. Oct. 26, 2020). The claims of car washes for business income and civil authority coverage were dismissed. The Court faced a threshold motion to remand because the insured had named its broker and both were residents of Texas. The Court denied the motion, holding that the broker was improperly joined because of "inability of a plaintiff to establish a cause of action against the non-diverse party in state court." The Court found there were no specific allegations of misrepresentations, that Texas law does not require an agent to explain all coverage limitations or terms in a policy and no damages followed any post-loss misrepresentations. Thus, no valid claims had been stated against the broker.

The Court briefly addressed but did not resolve any questions of "direct physical loss" or civil authority coverage. It relied entirely on the Virus or Bacteria Exclusion, which applied to "[A]ny virus, bacterium or other microorganism that induces or is capable of inducing physical distress, illness or disease." There was also an anti-concurrent causation provision. The Court held that the Exclusion was unambiguous, and "plainly excludes 'loss or damage' caused *even indirectly* by a virus." (Emphasis by the Court.) It also rejected the insured's argument that the Exclusion could have been more specific because that does not render ambiguous the language actually used. The Court also rejected extra-contractual statutory and bad faith claims. Finally, it rejected a civil conspiracy claim against the insured and the broker because conspiracy is a derivative tort, and there was no underlying tort. Leave to amend was denied because it would be futile, so the dismissal was with prejudice.

Decision Dismissing Contingent Business Interruption Claim on Specific Policy Language

Harvest Moon Distributors, LLC v. Southern-Owners Ins. Co., Case No. 6:20-cv-1026-Orl-40DCI, 2020 WL 6018918 (M.D. Fla. Oct. 9, 2020). The insured supplies beer to Walt Disney Parks and Resorts. When Disney voluntarily closed due to the pandemic, it refused to accept or compensate the insured for beer already purchased by the insured. The beer subsequently spoiled. The threshold question was thus whether spoilation of the beer constitutes "direct physical loss or damage." The Court concluded that a plausible claim had been stated under federal pleading standards. However, the Court found there were insufficient allegations to support the claim for lost business income and extra expense. Specifically, there were no allegations regarding suspension of the *insured's* operations as opposed to *Disney's* operations. The insured also sought coverage under an Accounts Receivable Endorsement but the Court found that it only applied to the physical loss of the actual Accounts Receivable records themselves. The Court went on to hold that there was no Covered Cause of Loss because of two exclusions. The first provided that the Policy does not cover loss or damages caused by "[d]elay, loss of use, or loss of market." The second provided that the "[a]cts or decisions … of any person, group, organization or governmental body" are not a Covered Cause of Loss. The Court dismissed without prejudice, and granted leave to file an Amended Complaint if the insured "believes it can do so in accordance with Rule 11."

Miscellaneous Decision Allowing Re-Pleading

Vandelay Hospitality Group LP d/b/a Hudson House v. The Cincinnati Ins. Co., Civil Action No. 3:20-CV-1348-D, 2020 WL 5946863 (N.D. Tex. Oct. 7, 2020). In an action originally filed by restaurants in State court and remanded to Federal court, where an amended petition had been filed under Texas pleading rules, the restaurants were given leave to replead under federal pleading standards.

Decision Granting Summary Judgment in Favor of Insured by Finding of Direct Physical Loss

North State Deli, LLC, et al. v. The Cincinnati Ins. Co., et al. (Case No. 20-CVS-02569 (Super. Ct., Durham Co. N.C. Oct. 9, 2020). This is the most unusual case to date, providing a clean win on summary judgment for sixteen insured restaurants under an all-risk policy. The insureds' primary contention was that Government Orders forced them to lose the physical use of and access to their property and premises which constitutes "direct physical loss." With no definitions in the policy, the Court looked to dictionary definitions of "direct," "physical" and "loss." It concluded that "[A]pplying these definitions reveals that the ordinary meaning of the phrase 'direct physical loss' includes the inability to utilize or possess something in the real, material, or bodily world, resulting from a given cause without the intervention of other conditions. In the context of the Policies, therefore, 'direct physical loss' describes the scenario where businessowners and their employees, customers, vendors, suppliers and others lose the full range of rights and advantages of using or accessing their business property. This is precisely the loss caused by the Government Orders."

The insurer argued for the common interpretation of "direct physical loss" in business interruption coverage cases – that there must be some form of physical alteration to property. The Court ruled that "[e]ven if Cincinnati's proffered ordinary meaning is reasonable, the ordinary meaning [identified by the Court] is also reasonable, rendering the Policies at least ambiguous." It construed the ambiguity against the insurer.

The Court saw a necessary distinction between the terms "physical loss" and "physical damage," both of which are used in the Policies. "The term 'physical damage' reasonably requires alteration to property... If 'physical loss' also requires structural alteration to property, then the term 'physical damage' would be rendered meaningless."

There was no Virus Exclusion. The Court rejected, without explanation, the exclusions for "Ordinance or Law, "Acts or Decisions" and "Delay or Loss of Use."

The insurer has indicated that the decision will be appealed.

Miscellaneous Decision Overruling Preliminary Objections to Pleading

Ridley Park Fitness, LLC v. Philadelphia Ind. Ins. Co., Case No. 01903 (First Judicial Dist., Civil Trial Division Pa. Aug 31, 2020). This case is included solely for completeness even though it is of little analytical value. It overruled preliminary objections to a pleading, without prejudice. The totality of the explanation is set forth in the footnote of the order. It said in relevant part: "Defendant alleges in the instant preliminary objections that plaintiff's failure to attach the insurance agreement in total constitutes a failure to plead, which defendant has cured by attaching the agreement in full, that certain clauses including a Virus Exclusion and 'direct physical loss' bar coverage, and finally that plaintiff is not entitled to a declaratory judgment. At this very early stage, it would be premature for this Court to resolve the factual determinations put forth by defendants to dismiss plaintiff's claims. Taking the factual allegations made in plaintiff's complaint as true, as this Court must at this time, plaintiff has successfully pled to survive at this stage of the proceedings."

Multidistrict Litigation Will Proceed Against Society Insurance Co.

In an October 2, 2020 Transfer Order, the U.S. Judicial Panel on Multidistrict Litigation ("MDL") agreed to consolidate suits for insurance coverage for lost business income due to COVID-19 executive orders filed against Society Insurance Company, but refused to do so against several other insurers saying it would be inefficient. *See In re: Society Insurance Co. COVID-19 Business Interruption Protection Insurance Litigation* MDL No. 2964, 2020 WL 5887444 (October 2, 2020).

As we previously reported in its July 2020 hearing session, the MDL Panel considered two motions seeking centralization of litigation involving claims for coverage for COVID-19-related business income losses due to government orders suspending or curtailing operations of non-essential businesses. The Panel denied the motions on the ground that the differences among the many insurers would overwhelm any common factual questions and hinder the presiding court's ability to efficiently manage the litigation. *See In re COVID-19 Bus. Interruption Prot. Ins. Litig.*, MDL No. 2942, 2020 WL 4670700, __ F. Supp. 3d __ (J.P.M.L. Aug. 12, 2020).

In the briefing on those motions, several parties proposed that insurer-specific MDLs be created. The Panel concluded that it needed a better understanding of the factual commonalities and differences among those actions and the relative efficiencies/inefficiencies involved in the proposed centralization. Accordingly, it issued "show cause" orders directing the parties to certain actions involving a common insurer or group of insurers to demonstrate why those actions should *not* be centralized.

In its ruling in *In re: Society Insurance Co. COVID-19 Business Interruption Protection Insurance Litigation*, the Court concluded that centralizing the litigation as to Society Insurance would "serve the convenience of the parties and witnesses and further the just and efficient conduct of this litigation." The Panel noted that Society Insurance is a regional insurer operating in six states —

Illinois, Indiana, Iowa, Minnesota, Tennessee and Wisconsin — and that the lawsuits filed against it "share common factual allegations" that Society Insurance wrongfully denied policy holders' claims for business income losses due to COVID-19 shutdown orders. The plaintiffs assert in their suits that Society Insurance preemptively denied their claims under policies that include all or some of the following coverages: (1) business income coverage, (2) civil authority coverage, (3) extra expense coverage, (4) contamination coverage, and (5) sue and labor coverage. The Panel noted that the insurance policies appeared to use standard forms drafted by the Insurance Services Office (ISO) and thus, adjudication of the plaintiffs' claims "will involve the interpretation of common policy language" and "an assessment of whether COVID-19 caused any direct physical loss of or to property, and whether any of Society's policy exclusions apply to preclude plaintiffs' claims." The Panel further concluded that to the extent discovery is necessary as to the drafting and interpretation of Society Insurance's policies, that discovery would be common to all of the actions.

Of note, in concluding that the cases present common factual and legal questions that support centralization and that such centralization will promote "the just and efficient conduct of the actions," the Panel specifically explained, "This litigation demands efficiency. . . time is of the essence. . . many plaintiffs are on the brink of bankruptcy as a result of business lost due to the COVID-19 pandemic and the government closure orders."

The consolidated litigation was transferred to Judge Edmond E. Chang of the U.S. District Court in Chicago, a district the Panel concluded "is the obvious center of gravity of this litigation against Society, with 22 of the total 34 pending cases filed there."

A New Wave of COVID-19 Claims?
Failure to Protect Assets From COVID-19-Era Financial Market Losses

Pension funds for truckers, teachers and subway workers have filed suits in the U.S. Southern District of New York against Germany's Allianz SE, an asset manager, for allegedly failing to safeguard their investments during the COVID-19-induced financial market downturn. Allianz reportedly had to close two private hedge funds after severe losses, prompting this wave of litigation.

The latest claims include one from the pension fund for the Metropolitan Transportation Authority. Similar suits have been filed against Allianz by pension funds for the Teamster labor union, Blue Cross and Blue Shield, and Arkansas teachers.
The cases are a second front of litigation for Allianz, already facing suits for denying coverage for losses business closures due to COVID-19-related government shutdown orders.

And Finally, The Show (Tennis Tournament) Must Go On!

In our April 2020 COVID-19 alert, we reported that Wimbledon was one of the notable exceptions as a business that actually purchased pandemic insurance and successfully made a claim under that coverage for its COVID-19-related business income losses.

Wimbledon recently declared that it is "set to go ahead next year even if the tournament has to be staged behind closed doors." Wimbledon reportedly has been "closely watching" the recent U.S. Open, played behind closed doors, and the French Open, where 1,000 fans a day were eventually admitted. Both tournaments were "deemed overall successes, with very few positive COVID-19-19 cases and broad player support."

Beyond drawing off these examples of successful tennis events in the U.S., a clearly motivating factor for Wimbledon to press forward itself next year is its admission that it will now be "unable to secure pandemic insurance."

The guidance provided in this Update is a basic overview, with high-level advice, and it should not be applied in the drafting of documentation without further consideration of the specific state laws and factual circumstances involved therewith. For more information on this topic or advice on specific questions related to managing risk for your business in the pandemic, please contact one of our COVID-19 Coordinators, identified below. 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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