GFELLER LAURIE LLP
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COVID-19 Insurance Coverage and Liability Update

Business Interruption Coverage Decisions

Since our last Update, the United States Court of Appeals for the Ninth Circuit handed down three opinions on Business Interruption coverage. Like the Sixth, Eighth and Eleventh Circuits before it, the Ninth Circuit affirmed decisions that had favored insurers. The first opinion was based on both lack of direct physical loss or damage and a virus exclusion. The second opinion also was based on lack of direct physical loss or damage. The third opinion was based on the Virus Exclusion only, applying the laws of ten States.

There have been many additional lower court decisions, the vast majority of which continue to favor insurers on the ground that there was a lack of direct physical loss or damage, a Virus Exclusion or both. Our Updates do not address all decisions. We only address decisions with unusual aspects or widespread effects. This Update will address one lower court decision at length. It arises in the challenging context in which a court accepts the possibility that COVID-19 may result in physical loss or damage and permits expert testimony.

Ninth Circuit Opinions

Insurer Prevails Because of Lack of Direct Physical Loss or Damage and Virus Exclusion

The most comprehensive Ninth Circuit Opinion, ***Mudpie, Inc. v Travelers Cas. Ins. Co. of Am.,*** No. 20-16858, 2021 WL 4486509 (9th Cir. Oct. 1, 2021), is marked "FOR PUBLICATION." It applied California law to interpret a comprehensive commercial liability and property insurance policy issued to a children's store selling clothes, toys, books and other goods. The store suspended operations in compliance with local and State Stay-at-Home Orders and sought Business Income and Extra Expense coverages. The insured did not allege that COVID-19 was present in its storefront premises (early in the action, it abandoned its claim for Civil Authority coverage). The Policy, however, required that the suspension "be caused by direct physical loss or damage to property." The Court found this to be part of the policy's insuring clause and thus within the insured's burden of proof. The Ninth Circuit declined the insured's request to certify the coverage question to the California Supreme Court, finding sufficient interpretive authority from the State's lower courts. The Court instead applied authority to the effect that "direct physical loss contemplates an 'actual change' [and] … a 'distinct, demonstrable, physical alteration' of the property." A mere loss of use is insufficient.

The policy contained a common Virus Exclusion providing that the insurer "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 insured claimed that the losses

resulted not from the virus, but from the Stay-at-Home Orders. The Ninth Circuit reasoned that California courts broadly interpret the phrase "resulting from" in insurance contracts. Where there is more than one cause, California law applies the Efficient Proximate Cause Doctrine. That is, even if there are other, later causes that contribute more immediately to the loss, the loss is attributed to the "efficient cause," which is the one that sets the others in motion. Here, there would have been no Stay-at-Home Orders had there not been a virus. It could not plausibly be alleged that the efficient cause, *i.e.,* the one that set the others in motion, was anything other than the virus.

Insurer Prevails because of Lack of Direct Physical Loss or Damage

Selane Products, Inc. v. Continental Cas. Co., No. 21-55123, 2021 WL 4496471 (9th Cir. Oct. 1, 2021), applied ***Mudpie,*** *supra*, to affirm the denial of coverage under Business Income and Extra Expenses endorsements. It applied the rule that direct physical loss or damage to property required an insured to allege a physical alteration of insured property. The insured did not even allege that COVID-19 was present on its property and "did not plausibly allege that the stay-at-home orders caused its property to sustain any physical alteration." The Court also held that the Civil Authority endorsement did not apply because the insured failed to allege any direct physical loss or damage to adjacent property. Given the reliance on ***Mudpie***, the analysis in this case was minimal. It was marked "NOT FOR PUBLICATION."

Insurers Prevail Because of Virus Exclusions

Chattanooga Professional Baseball, LLC d/b/a Chattanooga Lookouts v. National Cas. Co., No. 20-17422, 2021 WL 4493920 (9th Cir. Oct. 1, 2021) was an action brought by the owners and operators of minor league baseball teams in ten States. All of the policies at issue contained a Virus Exclusion 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 Ninth Circuit focused on causation. It found that three of the ten relevant States have expressly adopted the efficient proximate cause test (see description in ***Mudpie,*** *supra*) and five others "have either applied or been persuaded by this analysis." Under the analysis in ***Mudpie***, the virus Exclusion was applied. The ninth State was Texas, which applies the rule that where there are concurrent perils, one covered and one excluded, the insured bears the burden to identify the portion of the loss attributable to the covered peril. The Ninth Circuit held that the causation argument failed because no argument exists that the claimed losses are susceptible to allocation. All alleged causes flowed from the virus, so the Virus Exclusion applied. The tenth State, Virginia, uses a proximate cause analysis. The Ninth Circuit held that there were no plausible allegations that other alleged causes of loss were efficient intervening causes that broke the causal chain stemming from the virus, so the Virus Exclusion applied.

The Ninth Circuit also rejected claims of regulatory estoppel. Because of the States involved, only West Virginia recognizes the doctrine and there was no allegation that the insurers themselves had advocated contrary interpretations to those earlier expressed. Claims of equitable estoppel were

denied because there were no allegations of misrepresentations or reliance. The opinion was marked "NOT FOR PUBLICATION."

Other Courts

New York Court Dismisses Claims of Medical Providers for Jails and Prisons

Wellpath Holdings, Inc. v. XL Insurance America, Inc., et al., Index No. 54589 (Sup. Ct. Westchester Co. Oct 4, 2021) is notable for the factual scenario involved. The insured provides medical and behavioral services at over 400 inpatient and residential treatment facilities, civil commitment centers and correctional facilities throughout the United States and Australia. With the onset of the pandemic, it alleged that the properties at its locations were rendered uninhabitable or unfit for its intended use. It asserts it lost income because it treated fewer patients and incurred greater costs to remain open. Although the facts were unusual, the analysis followed a familiar course. The Court found a "solid consensus" in New York that direct physical loss or damage requires physical damage to the insured's property and "actual, demonstrable physical harm of some form." It held that the mere presence of the virus in the air or on surfaces of a covered property does not qualify as damage to the property itself. The virus is a "temporary health hazard . . . [which] dissipates with the passage of time."

Federal District Court Allows Action to Proceed To Trial, Setting Up a Battle of Experts

Although the insurers have prevailed in the vast majority of cases, the insureds have prevailed in some. A particularly challenging strain of cases arises when a court accepts the possibility that the virus may have been present on the insured's property and may, in fact, cause physical loss or damage. One of the first courts to allow an insured's claim to proceed past a motion to dismiss was ***K.C. Hopps, Ltd. v. The Cincinnati Ins. Co.,*** No. 20-cv-00437, 2020 WL 6483108 (W.D. Mo. Aug. 12, 2020). There, the Court held that the insured had sufficiently pled that their properties had been physically contaminated and there was physical loss, so the action should proceed to discovery. The Western District of Missouri is in the Eighth Circuit and in July 2021, the Eighth Circuit decided ***Oral Surgeons, P.C. v. The Cincinnati Ins. Co.,*** 2 F.4th 1141 (8th Cir. 2021). That case affirmed a lower court ruling that under an identically worded policy, there was no Business Income coverage in the absence of "accidental physical loss or accidental physical damage." Notwithstanding the ***Oral Surgeons*** opinion, in September the Judge in the ***K.C. Hopps*** case issued a further opinion denying motions for summary judgment and allowing the case to proceed to trial. ***K.C. Hopps, Ltd. v. The Cincinnati Ins. Co.***, Case No. 20-cv-00437, 2021 WL 4302834 (W.D. Mo. Sept. 21, 2021.) (**"*Hopps II"***.)

The ***Hopps II*** court distinguished ***Oral Surgeons*** by stating that the Eighth Circuit only held the COVID-19 pandemic and the related government-imposed restrictions in themselves did not constitute physical loss damage, but it did not determine that the virus can never cause physical loss or damage. Unlike the insureds in ***Oral Surgeons,*** the insured in ***Hopps II*** alleged the presence

of the virus on its premises. Further, it submitted expert evidence supporting the inference that the virus is physical, contaminated its premises and made its property unsafe. The insurer submitted contrary expert evidence. The Court cited the United States Supreme Court for the proposition that "[r]esolving expert opinions is the 'near-exclusive province of the jury.'" (*citing Tyson Foods v. Bouaphakeo*, 577 U.S. 442, 459 (2016)).

The ***Hopps II*** Court noted the presence of a contamination exclusion identifying several specific contaminants, but not viruses. It reasoned that this permitted coverage for some kinds of physical contamination that render the property unsafe, which would constitute physical loss or damage without physical alteration of the property.

The insured presented evidence from two experts. The first was "an academic molecular epidemiologist." Although he never tested the insured's premises, he opined that "it is more likely than not – indeed, it is highly likely – that the virus was present on the insured's premises." He based this on the view that the virus "has a physical presence. It can exist in the air and on surfaces for indeterminate periods of time and can be transferred from the air and surfaces into human bodies." The Court found that this opinion and the fact that some of the insured's employees had been infected supported the finding of an evidentiary dispute. The insured's second expert was a "Professor Emeritus of Chemistry and Bioengineering at the Massachusetts Institute of Technology." He testified that the virus "is physical, it attaches to surfaces, and absent removal of the virus, the property is rendered unsafe." He testified the virus remains infectious for up to several days and "creates a chemical bond with the surface." The Court concluded that this supports an inference that the virus "creates an actual, tangible alteration to the property."

The insurer also presented two experts. The first was an "Assistant Professor of Family Medicine and Community Health at Duke University and Director Emeritus of the Duke University and Health System Occupational & Environmental Safety Office." In his opinion, the risk of surface transmission is low, that the virus not "modified, degraded, or altered the performance, appearance, or intended use of materials, and that the virus "is not everywhere, in every building or on every surface in every building." The second expert was a doctor "Board Certified in Internal Medicine and Infectious Diseases." This expert opined that he "fundamentally disagree[d] with [the insured's experts] assessment of the impact of SARS-CoV-2 fomites on surfaces … if the virus was present at the K.C. Hopps bars and restaurants … the presence would have been very transient, easily remediated and without question not permanent." He further stated that the virus "can be very easily remediated by simple cleaning and does not alter the object. It is simply incorrect that surfaces remain 'infectious' with time (hours to days) and/or simple cleaning with soap and water."

The Court found genuine issues of material fact, denied motions for summary judgment by both sides and allowed the action to proceed to trial. Thus, the battle of experts will continue.

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, or the Gfeller Laurie LLP attorney with whom you regularly communicate:

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Sincerely,

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