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COVID-19 Insurance Coverage and Liability Update

Since our last Update, the United States Courts of Appeals for the Second, Fifth, and Tenth Circuits all issued their first decisions in COVID-19 Business Interruption cases. In each, the Courts ruled in favor of Insurers. Also, the Sixth Circuit, which had previously issued several decisions under Ohio law, issued a Decision under Kentucky law, also ruling in favor of the Insurer. And the Eleventh Circuit handed down a decision in favor of an Insurer, construing New York law.

With these decisions, insurers have prevailed at every Circuit that has ruled: the Second, Fifth, Sixth, Seventh, Eighth, Ninth, Tenth and Eleventh Circuits. The decisions have been based on lack of direct physical loss or damage, or Virus Exclusions, or both.

Also, the State Supreme Courts of Massachusetts and Vermont became the first to hear oral argument in cases involving COVID-19 Business Interruption.

While there have been many additional decisions, the vast majority continue to hold in favor insurers, on the grounds of lack of direct physical loss or damage, a Virus Exclusion, a pollution or contamination provision, or some combination of these. Our Updates do not address all decisions. We only address decisions with unusual aspects, or widespread effects.

We also report briefly on a possible uptick in COVID-19 exposure liability lawsuits, involving alleged exposure in the workplace or in a business setting, and most recently, "take home" COVID-19 exposure to family members or friends outside the workplace/business place. A recent decision by a California Court of Appeal, rejecting a defendant employer's attempt to invoke workers' compensation law protections in that context, has commentators wondering if the gates are now cracked, if not fully, open, to a flood of such suits.

Business Interruption Coverage Decisions

Second Circuit Decisions

Insurer Prevails Under New York Law for Lack of Direct Physical Loss or Damage

10012 Holdings, Inc. v. Sentinel Ins. Co., 21 F.4th 216 (2d Cir. 2021) involved a "brick-and-mortar art gallery and dealership in New York City." The owner sought Business Income, Extra Expense, and Civil Authority coverage. It suspended business because of the Executive Orders issued by the Governor of New York. The policy required "direct physical loss" for Business Income and Civil Authority coverage. The Court relied upon a New York intermediate appellate court case, *Roundabout Theatre Co. v. Cont'l Cas. Co.,* 751 N.Y.S. 2d 4 (1st Dept. 2002), to deny Business Income and Extra Expense coverage. That was not a COVID-19 case, but in that case,

the Court denied coverage for income for lost performances when a municipal order closed a street for safety reasons following a construction accident at a building in the area. The *Roundabout Theatre* court held that the policy required direct physical damage to the Insured's property. The Second Circuit said it was aware of no contrary authority and that state and federal courts in New York have uniformly applied this case to deny coverage "under similar insurance provisions." It rejected claims that "Loss of use" should suffice, noting that the term did not appear in the Business Income and Extra Expense provisions, but was included in other unrelated policy provisions. The Second Circuit also rejected the insured's claim for Civil Authority coverage because that provision required a risk of "direct physical loss" to property in the vicinity, and "shuttering a gallery because of possible human infection does not quality as a 'risk of direct physical loss.'" Finally, the Second Circuit denied the Insured's request for Certification to New York's highest State court, the Court of Appeals.

Insurers Prevail under New York Law Because of Lack of Direct Physical Loss or Damage

Kim-Chee LLC, et al. v. Philadelphia Indem. Ins. Co., et al., No. 21-1082, 2022 WL 258569 (2d Cir. Jan. 28, 2022) involved a Tae-Kwon-Do studio seeking Business Income, Extra Expense, and Civil Authority coverage, asserting "direct physical loss or damage at" its property. The Court denied coverage, relying on *10012 Holdings, Inc., supra,* which the Court viewed as "materially identical." The decision is notable for two other points. First, it found insufficient the bare allegations that the virus is "ubiquitous, such that it is everywhere" and that the virus inflicted actual harm or damage to property. Next, the Insured argued that the absence of a virus exclusion, even though it is present in other policies, means there must be coverage in the policy at issue. The Second Circuit rejected this because the absence of an exclusion cannot create coverage and the words actually in the policy must themselves express an intention to deny coverage. This decision was a Summary Order, meaning it does not have precedential effect and can be cited only in limited circumstances.

Fifth Circuit Decisions

Insurer Prevails Under Texas Law Because There Was No Direct Physical Loss and Because a Restaurant Extension Endorsement's Causation Requirement Was Not Met

Terry Black's Barbecue, LLC v. State Auto. Mut. Ins. Co., 22 F.4th 450 (5th Cir. 2022) involved a restaurant seeking coverage under an all-risk property policy that included Business Income and Extra Expense coverage, for loss "caused by direct physical loss of or damage to property at the premises." The policy also included a Restaurant Extension endorsement providing coverage for loss "due to the order of a civil authority … resulting from the actual or alleged … exposure of the premises to a contagious or infectious disease." The suspension of operations followed an executive order from the Governor of Texas. As to Business Income and Extra Expense coverage, the Court concluded that "loss of" and "damage to" have two distinct meanings. The Insured argued only that there was a "direct physical loss of property," so the Court only analyzed that language. The Court adopted definitions from existing insurance cases and concluded the plain

meaning of "physical loss" meant there was no coverage. It joined other jurisdictions in interpreting a "physical loss" to require a tangible alteration or deprivation of property.

The Court construed the Restaurant Extension Endorsement's phrase "resulting from" as requiring causation. It held the civil authority orders did not "result from" the Insured's actual or alleged exposure to a contagious disease. In fact, "the language in the orders indicates that they were enacted to *avoid* exposure to COVID-19, not *because of* exposure to COVID-19" (emphasis in original).

Insurer Prevails Under Texas Law for Lack of Physical Loss of Property

Aggie Investments, LLC v. Cont'l Cas. Co., No. 21-40382, 2022 WL 67333 (5th Cir. Jan 6, 2022) involved the owners of a tea and spice store that suspended operations because of governmental orders. The insured sought Business Income and Extra Expense coverage. The Court rejected the argument that a loss of use was sufficient to establish "physical loss of property." Instead, it held that there must be "a tangible alteration or deprivation of property." Thus, there was no coverage.

New Sixth Circuit Decision

Insurer Prevails under Kentucky Law for Lack of Direct Physical Loss

Ryan P. Estes, D.M.D. v. Cincinnati Ins. Co., 23 F.4th 695 (6th Cir. 2022) involved a dentist's claims under provisions for Business Income, Extra Expense, Civil Authority, Ingress and Egress, and Dependent Properties coverage. The policy required that there be "direct loss" and defined "loss" as "accidental physical loss or accidental physical damage." The Court construed the language from the perspective of an "average person," concluding that the phrase "physical loss" would convey that a property owner has been tangibly deprived of the property or that the property has been tangibly destroyed. The average person would see the shutdowns of the dentist's offices as "economic" or "business" losses. The Court noted that the dentist "bought a *property* insurance policy, not a *profit* insurance policy" (emphasis in original). The Court also cited to the broad circuit consensus, saying that "every other circuit court to consider this question has read nearly identical language in the same way."

Tenth Circuit Decision

Insurer Prevails Under Oklahoma Law for Lack of Direct Physical Loss, and Because of Virus Exclusion

Goodwill Indus. of Cent. Okla., Inc. v. Phila. Indem. Ins. Co., 21 F.4th 704 (10th Cir. 2021) applied Oklahoma law to a claim by Goodwill Industries arising from government shutdown orders. Goodwill only argued that Business Income coverage applied, so the Court did not need to address extra expense or interruption by civil authority provisions. The Court construed "direct physical loss of" through word-by-word reference to two leading dictionaries and concluded that

the phrase required "an immediate and perceptible destruction or deprivation of property." The Insured had not alleged it suffered such a loss. Thus, there was no coverage.

The Policy also contained a Virus Exclusion. The Court found it was valid and enforceable, rejecting the argument that there was a lack of consideration. When the Policy was issued, the Insurer included an "advisory notice to Policyholders" explicitly alerting the Insured to the Virus Exclusion. The Insured also argued that the Insurer failed to obtain consent from the Insured to add the exclusion, and the Insured never signed the exclusion. The Court held that the exclusion was valid without the Insured's signature. The Oklahoma Administrative Code requires an insured to sign an endorsement that eliminates or restricts coverage, when issued "during the policy term." The Court held this does not apply, because the exclusion was present at the outset of the policy term, not added during it. The Court went on to hold that the plain language of the exclusion – "loss or damage caused by or resulting from any virus, bacterium, or other microorganism that induces or is capable of inducing distress, illness or disease" – would make it clear to any reasonable businessperson that the exclusion would extend to losses caused by immediate efforts to mitigate a viral outbreak. It did not require the virus to be physically present on the property. Finally, the Court concluded that the efficient proximate cause of the losses was the outbreak and spread of the virus.

Eleventh Circuit Decision

Insurer Prevails Under New York Law

Ascent Hosp. Co., LLC v. Emps. Ins. Co. of Wausau, No. 21-11924, 2022 WL 130722 (11th Cir. Jan. 14. 2022) involved a claim of a hotel and restaurant manager of 35 locations. The policy provided coverage "against all risks of direct physical loss or damage." The Eleventh Circuit had a rare opportunity to apply New York law. Like the Second Circuit in *10012 Holdings, Inc., supra,* the Eleventh Circuit looked to the intermediate appellate court case of *Roundabout Theatre Co. v. Cont'l Cas. Co.,* 751 N.Y.S.2d 4 (N.Y. App. Div. 2002). The Court denied the claim for coverage. It also denied claims under Georgia law for fraudulent representation and fraudulent suppression. The Court marked this decision "[DO NOT PUBLISH]."

Pending State High Court Cases

The highest courts in two states are primed to hand down COVID-19 decisions. On January 7, 2022, the Massachusetts Supreme Judicial Court held oral argument in *Verveine Corp., et al. v. Strathmore Ins. Co., et al.,* No. SJC-13172. On January 26, 2022, the Vermont Supreme Court heard oral argument in *Huntington Ingalls Industries Inc., et al. v. Ace American Ins. Co., et al.,* No. 2021-173.

Are The COVID-19 Exposure Liability Floodgates Officially Open?

Previously, we reported on efforts at both the state and federal levels to limit businesses' and employers' liability arising from customers' and/or employees' alleged exposure to COVID-19 in the workplace/business locations. Some states enacted limited legislation (sometimes with self-professed doubts about whether the legislation would withstand constitutional challenges).[1] However, for purposes of the discussion that follows, note that California is not one of them.

This was prior to the widespread availability of vaccines. Now, with vaccines not only available, but in some cases, mandated by employers and businesses alike, COVID-19 workplace/business place exposure claims nonetheless appear to be on the rise, in particular, in the "take home" COVID-19 context. Where the claimant is an employee, the litigation often raises the "exclusive remedy"/derivative injury defense that likely would be available to an employer in the workers' compensation litigation context. However, courts are not necessarily going to be receptive to that defense in the "take home" COVID-19 context, as one California case has illustrated recently.

Eyes are on the California case, *Matilde Ek v. See's Candies, Inc.* (Los Angeles County Super. Ct. No. 20STCV49673) in which Ms. Ek, a See's Candies worker, alleges she contracted COVID-19 while working on the packing line at a See's distribution plant in California in March 2021. She claims she later exposed her 72-year-old husband to the virus, which killed him one month later. Ms. Ek alleges the plant lacked sufficient safeguards against infection.

See's moved to strike her claims, invoking the "exclusive remedy"/derivative injury defense which, in a workers' compensation suit, would bar Ms. Ek's claims on the ground that workers' compensation benefits provide the exclusive remedy.

However, in April 2021, the trial court denied See's motion, instead allowing the case to proceed on the theory that Ms. Ek's claim was similar to an asbestos case theory that an employer has a duty to exercise reasonable care to prevent exposure to contaminants to foreseeable *third parties* – in this case, Ms. Ek's husband, who was not a See's employee.

See's appealed the trial court's decision to California's Second District Court of Appeal. A coalition of state and national employer groups submitted a "friend of the court" brief arguing that the trial court's ruling violates the workers' compensation exclusive remedy/derivative injury rule such that a "large swath of COVID-19 related claims stemming from workplace conduct would be placed outside of the workers' compensation system."

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[1] Such legislation typically requires plaintiffs making COVID-19 workplace/business exposure claims to plead and prove gross negligence by the employer/business. Nothing similar has been enacted at the federal level to date.

But on December 21, 2021, the Court of Appeal disagreed with See's, ruling that Ek's claims on her deceased husband's behalf were not "derivative" of her infection and thus, were not preempted by workers' compensation laws, thereby allowing Ek's lawsuit to proceed at the trial court level. The Court found that Ek's husband's death was dependent on Ms. Ek as a *conduit* for the virus and not, as See's had argued, dependent on her "disease" (the "derivative injury" argument typically raised in asbestos litigation). Notably, Ms. Ek still must establish at the trial court level that See's owed a duty to Ms. Ek's husband (as a "foreseeable" third party victim), which theory other courts, hearing similar suits, have rejected. Beyond that, Ms. Ek also must show that there is a link between her alleged workplace exposure and the claimed case of "take-home" COVID-19, as opposed to her husband having been exposed to COVID-19 through some other conduit.

Nonetheless, the California Second District Court of Appeal's decision has prompted commentary that the ruling could open up the proverbial "flood gates" for COVID-19 exposure liability claims. In fact, such suits are pending currently against several major employers, including Amazon, Walmart and Royal Caribbean, among others. The lawsuits generally allege negligence in adopting COVID-19 protocols, such as cramped working or living conditions or failure to screen for infected employees. The plaintiff employees claim damages on behalf of their children and spouses who became infected after being exposed to the virus, via the employee, outside the workplace/business place. Some of the suits have been dismissed or have settled.

Though some speculate that the rates of COVID-19 workplace exposure claims should *de*celerate as more workers are vaccinated, the most recent Omicron variant wave has demonstrated that "breakthrough" cases are possible even among the vaccinated. Thus, the liability shield legislation that some states have enacted will be a crucial tool in fending off not only "take home" COVID-19 suits but more broadly, workplace/business place COVID-19 exposure claims. Where the legislation specifically sets a "gross negligence" standard, employers and business owners will benefit from further development of the law on how employer and/or business owner-issued vaccine mandates and similar precautions *per se* preclude a finding of gross negligence by the employer or business owner.

As to "take home" suits such as the *Ek v. See's* matter, pending in states where no such liability shield legislation currently exists, key developments in the case law will address whether an employer or business owner owes a duty to third parties (i.e., are they "foreseeable" victims?), whether, through its protocols/precautions or lack thereof, it breached that duty and whether the claimant can demonstrate a direct causal link between the workplace/business place exposure and the alleged "take home" victim. We will continue to monitor this litigation and report on key developments periodically.

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 these topics or advice on specific questions related to coverage and/or 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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