

April 12, 2022

## **COVID-19 Insurance Coverage and Liability Update**

### **Business Interruption Coverage Decisions**

Since our last Update, the United States Court of Appeals for the Fourth Circuit issued its first decision on COVID-19 Business Interruption, ruling in favor of the Insurer. Also, the Second, Fifth, Sixth, Eighth, and Ninth Circuits, which had previously issued decisions in favor of Insurers, issued additional decisions.

With these decisions, Insurers have prevailed at every Circuit that has ruled: the Second, Fourth, 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.

There have been many additional decisions in lower courts, the vast majority of which continue to 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, only those with unusual aspects or widespread effects.

As of the date of this Update, there have been no decisions by the highest appellate court of any state. The Supreme Courts of Massachusetts and Vermont have heard oral arguments and decisions are expected.

### **New Second Circuit Decisions**

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

*Deer Mountain Inn, LLC v. Union Ins. Co.*, No. 21-1513, 2022 WL 598976 (2d Cir. Mar. 1, 2022) involved an Inn seeking recovery for business income losses resulting from the pandemic and related government restrictions. It argued that its inability to use the insured property for its intended purpose was sufficient to trigger coverage. The Court rejected the argument, saying that the prior decision of *10012 Holdings, Inc. v. Sentinel Ins. Co.*, 21 F.4th 216 (2d Cir. 2021) required actual physical loss or damage to the insured property. It noted that the Second Circuit has reached the same conclusion in two subsequent cases. This decision was a Summary Order, meaning it does not have precedential effect and can be cited only in limited circumstances.

#### **Insurer Prevails Under New York Law for Lack of Direct Physical Loss**

*SA Hospitality Group, LLC v. Hartford Fire Ins. Co.* No. 21-1523, 2022 WL 815683 (2d Cir. Mar. 18, 2022) affirmed the dismissal of claims by the owner of a group of food service establishments for business interruption coverage under an all-risk commercial property policy. It

alleged that governmental orders prevented it from using its property for the intended purpose, which amounted to a “direct physical loss of” the property. The Court held that this argument is foreclosed by its decision in *10012 Holding, Inc. v. Sentinel Ins. Co.*, 21 F.4th 216 (2d Cir. 2021). This decision was a Summary Order, meaning it does not have precedential effect and can be cited only in limited circumstances.

### **Fourth Circuit Decision**

#### **Insurer Prevails Under West Virginia Law for Lack of Physical Loss or Damage**

*Uncork And Create LLC v. The Cincinnati Ins. Co., et al.*, 27 F.4th 926 (4th Cir. Mar. 7, 2022) is the first decision from the Fourth Circuit. It involved a creative events company which closed two art studios because of governmental orders. It addressed the claim for Business Income and Extra Expense coverage. (The Insured abandoned its claim for Civil Authority coverage on appeal.) The Court examined the plain meaning of “physical loss” and “physical damage.” Relying on *Webster’s Third New Int’l Dictionary* (2002), it defined the word “physical” to mean “relating to natural or material things,” the word “loss” to mean “the state or fact of being destroyed or placed beyond recovery: destruction, ruin,” and the word “damage” to mean “injury or harm ... to property.” Applying these, it found the policy language to be plain and unambiguous, and dismissed the claims. It declined to certify the question to the West Virginia Supreme Court, because existing West Virginia law in analogous contexts was consistent with the Fourth Circuit’s interpretation here. One notable feature was the Court’s rejection of the argument that an all-risk policy “necessarily covers any type of loss for any reason unless included as a stated exclusion.”

### **New Fifth Circuit Decisions**

#### **Insurer Prevails Under Louisiana Law for Lack of Physical Loss or Damage, Lack of a Causal Connection Between Loss or Damage and Civil Authority Orders and the Inapplicability of Limited Virus Coverage Provision**

*Q Clothier New Orleans, LLC, et al. v. Twin City Fire Ins. Co.*, No. 21-30278, 2022 WL 841355 (5th Cir. Mar. 22, 2022) involved claims by an insured operating men’s clothing stores. It sought coverage under extensions for Business Income and Civil Authority, and an exception to a Virus Exclusion. The Court dismissed claims for coverage under all of these. The first two claims were straightforward. The Court found the plain and ordinary meaning of “physical loss or damage” to be “a tangible alteration to, injury to, or deprivation of property.” It thus found no coverage under the policy’s general coverage, Business Income Extension, or Limited Virus Coverage. It further found Civil Authority coverage did not apply because there was no causal connection between loss or damage to property near the Insured’s stores and the civil authority orders prohibiting access to its stores.

The novel portion of this decision is its construction of a provision for Limited Virus Coverage under Time Element Coverage. The Policy contained the Virus Exclusion for the “presence,

growth, proliferation, spread, or any activity of ‘fungi,’ wet rot, dry rot, bacteria or virus.” But that exclusion had a complex exception by virtue of a Limited Virus Coverage provision, which itself applied only if a Time Element Coverage applied. As distilled by the Court, for the Limited Coverage to apply: “a couple of things must happen. First, a loss causes a virus. That first loss does not require a suspension of operations. Second, the virus (that was caused by the first loss) causes a different loss. That second loss *does* require a suspension of operations.” The Court held that the complaint did not contain any relevant allegations that would trigger this coverage. Since the relevant Time Element Coverage was the Business Income Extension, under which there was no coverage, the Limited Virus Coverage provision would not apply in any event.

### **Insurer Prevails Under Louisiana Law for Lack of Physical Loss or Damage**

*Louisiana Bone & Joint Clinic, LLC v. Transportation Ins. Co.*, No. 21-30300, 2022 WL 910345 (5th Cir. Mar. 29, 2022) was decided by the same Fifth Circuit panel that decided *Q Clothier*, *supra*. This case involved a medical and surgical clinic. The Court cited *Q Clothier* and applied it to dismiss claims for Business Income, Extra Expense and Civil Authority coverage for the same reason. This case is most notable for its discussion about why loss of use does not constitute physical loss or damage. The Court reasoned that it would render the adjective “physical” meaningless, that it is at odds with the concept of a “period of restoration” and that the presence of the term in the consequential damages exclusion merely shows that a loss of use may cause loss or damage, although even in that provision such loss would not be covered. In the Business Income and Extra Expense provision, the adjective “physical” is present, meaning the loss must be tangible.

### **New Sixth Circuit Decisions**

### **Insurer Prevails Under Michigan Law for Lack of Direct Physical Loss or Damage**

*Brown Jug, Inc., et al. v. Cincinnati Ins. Co.*, 27 F.4th 398 (6th Cir. Feb. 23, 2022) was a consolidated appeal involving restaurants and entertainment venues seeking coverage under Business Income, Extra Expense, and Civil Authority provisions of commercial insurance policies. In addition to the usual allegations, two of the restaurants alleged they were sources of COVID-19 outbreaks, in the sense that customers and employees tested positive after being present in the restaurants. The Court applied Michigan law. Although there was no authority from the Michigan Supreme Court, the Michigan Court of Appeals recently held that “the word ‘physical’ necessarily requires the loss or damage to have some manner of tangible and measurable presence of effect in, on, or to the premises.” *Gavrillides Mgmt. Co. v. Mich. Ins. Co.*, No. 354418, 2022 WL 301555, at \*4 (Mich. Ct. App. Feb. 1, 2022). The Sixth Circuit held that none of the complaints credibly alleged that COVID-19 in any way physically and directly altered property by its mere presence. Thus, there was no Business Income or Extra Expense Coverage. Further, there was no Civil Authority coverage because none of the complaints alleged physical loss or damage to properties other than their own (except in conclusory statements). The Court distinguished cases arising from government shutdown orders issued during riots in Detroit in the summers of 1967 and 1968,

because those orders implemented a curfew closing “all places of amusement” in response to physical damage to property in Detroit.

### **Insurer Prevails Under Ohio Law for Lack of Direct Physical Loss or Damage**

*System Optics, Inc. v. Twin City Fire Ins. Co.*, No. 21-3556, 2022 WL 616968 (6th Cir. Mar. 2, 2022) involved a claim by eye-care clinics which sought coverage under Business Income, Extra Expense, and Civil Authority provisions. This was the second time the Sixth Circuit faced this question under Ohio law. The first case was *Santo’s Italian Café LLC v. Acuity Ins. Co.*, 15 F.4th 398 (6th Cir. 2021), which held that direct physical loss or damage required tangible destruction, or tangible or concrete deprivation. Mere loss of use is insufficient. Thus, the Sixth Circuit affirmed a judgment on the pleadings for the insurer. The decision was marked “[NOT RECOMMENDED FOR PUBLICATION].”

### **Insurer Prevails Under Kentucky Law for Lack of Direct Physical Loss or Damage**

*Goodwood Brewing, LLC v. United Fire Grp., et al.*, No. 21-5759, 2022 WL 620149 (6th Cir. Mar. 3, 2022) involved two Kentucky pubs seeking lost business income, extra expense, and civil authority coverage. The Sixth Circuit had previously ruled under Kentucky law that physical loss requires tangible deprivation or destruction. *Estes v. Cincinnati Ins. Co.*, 23 F.4th 695 (6th Cir. 2022). There was only one new argument presented. A provision of the policy that did not apply to the Kentucky properties at issue excluded from coverage any “loss, cost, or expense” caused by a virus, including those that result in “denial or access” to property. The Insured argued that the failure to include that provision in the part of the policy relating to Kentucky properties means that the policy must cover virus-related losses. The Court rejected the argument and applied the provisions requiring direct physical loss. Thus, it held that *Estes* applied and affirmed the district court’s grant of summary judgment. The decision is marked “[NOT RECOMMENDED FOR PUBLICATION].”

### **New Eighth Circuit Decision**

#### **Insurer Prevails Under Missouri Law for Lack of Direct Physical Loss**

*United Hebrew Congregation of St. Louis v. Selective Ins. Co. of America*, No. 21-2752, 2022 WL 1013984 (8th Cir. April 5, 2022) affirmed the dismissal of a synagogue’s claims for lost business income. It held the “argument that [a] pandemic-related closure constituted a direct physical loss of property is foreclosed by our prior precedent, *see Oral Surgeons, P.C. v. Cincinnati Insurance Co.*, 2 F. 4th 1141, 1144 (8th Cir. 2021).”

### **New Ninth Circuit Decisions**

#### **Insurer Prevails Under California Law for Lack of Direct Physical Loss or Damage, Applying the Precedent of a California Intermediate Appellate Court**

*Steven Baker, et al. v. Oregon Mut. Ins. Co.*, No. 21-15716, 2022 WL 807592 (9th Cir. Mar. 16, 2022) affirmed the dismissal of claims of restaurants for Business Income Coverage. The Court followed the California intermediate Appellate Court’s decision in *Inns by the Sea v. California Mut. Ins. Co.*, 286 Cal. Rptr. 3d (Cal. Ct. App. 2021) and held that neither the COVID-19 virus nor the related closure orders caused direct physical loss or damage within the meaning of the commercial property insurance policy at issue. The decision is marked “NOT FOR PUBLICATION” and has limited precedential value.

### **Insurer Prevails Under Nevada Law for Lack of Direct Physical Loss or Damage**

*Levy Ad Group, Inc. v. Federal Ins. Co., et al.*, No. 21-15413, 2022 WL 816927 (9th Cir. Mar. 17, 2022) affirmed the dismissal of claims under Business Income and Civil Authority provisions. Nevada law applied. Although there was no Nevada law on point, the Court cited to the numerous decisions across seven United States Courts of Appeal, agreed with them, and said that “there is no reason to think a Nevada court would interpret the contract language differently.” The decision was marked “NOT FOR PUBLICATION” and has limited precedential value.

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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