Business Interruption Claims and COVID-19:

Is It "Reasonable" to Expect Any Coverage After This Disaster?

By Frederic Theodore Le Clercq and Francis J. Barry, Jr.

We have seen a shadow of this fight before. It was Katrina. Was it "reasonable" for homeowners policies to cover flood claims by recasting the meaning of that policy language? Now is the time for the wave of litigation on business interruption claims from COVID-19, like the creative one brought by New Orleans lawyer John Houghtaliang in *Cajun Conti, L.L.C. v. Certain Underwriters at Lloyd's, London, et al.*, Civil District Court, Orleans Parish, No. 2020-02558, March 16, 2020. We submit the result, though painful to policyholders, should be similar to those Katrina flood claims — that there is no coverage for business interruption claims without "physical loss." The fact that the COVID-19 virus is generally "present" at a business is also not enough to overcome a virus exclusion. Like Homer's Odysseus, and his struggle with the superficially beautiful call from the sirens, courts must resist the immense temptation of the equities and enforce the insurance contract.[1]

The COVID-19 pandemic will engender a huge number of business interruption insurance claims in Louisiana.[2] The insurance coverage issues will vary depending on the policy language, the exclusions in each policy and the circumstances and losses of each insured. There are several issues that may occur frequently, and these are discussed below.

Most business interruption insurance includes the condition that the insured premises must suffer physical damage, and many policies since 2006 contain the specific Insurance Services Office (ISO) form CP 01 40 07 06, titled "Exclusion for Loss Due to Virus or Bacteria." These two provisions should usually end the COVID-19 business interruption claims. However, the economic tragedy unfolding has spurred Louisiana lawyers to lead the effort to gut these contract provisions.

In the lawsuits filed subsequent to the pandemic closure of restaurants in the United States — a suit filed in New Orleans, *Cajun Conti, L.L.C. v. Certain Underwriters at Lloyd's, London, et al.,* Civil District Court, Orleans Parish; and *French Laundry Partners, L.P. d/b/a The French Laundry, et al v. Hartford Fire Insurance Co., et al.,* filed in Superior Court, Napa County, California — the policyholders assert that the respective governmental closure orders and the general contamination of the premises by the virus provide a basis for coverage, regardless of any limitations or exclusions in the policy language. *Cajun Conti's* treatment of "physical loss" attempts to bend beyond recognition the policy language. While understandable in the face of such economic suffering, it should be unsuccessful.[3] Likewise, lawsuits of the Chickasaw and Choctaw Nations in Oklahoma for business interruption coverage are asserted to be covered claims notwithstanding policy language to the contrary.[4] This is but the start of the wave.[5]

Most business interruption forms say they will pay for actual loss of business income due to "suspension" of "operations" while there is a "period of restoration." The "suspension" must be caused by "direct physical loss." Covered loss ends when the property is repaired or business resumed elsewhere. For instance, the policy coverage may state that there must be "direct physical loss or damage to property at a premises which are described in the Declarations."

One national law firm often representing insureds argues[6] "nothing in these often unedifying terms rules out the possibility of damage caused by the presence of microscopic organisms or requires that loss or damage be visible to the naked eye, or even visible at all." If the premises of the insured's business are flooded or damaged by fire, or building collapse, then the policy condition and definitions of "damage" would be satisfied. But what if there is no physical damage to the property of the insured, and the business interruption is caused by some type of governmental shutdown order sparked by the COVID-19 pandemic?

There is case law holding that some type of physical damage to the insured's premises must occur before business interruption coverage is triggered. In *Mama Jo's, Inc. v. Sparta Ins. Co*., No. 17-23362, 2018 WL 3412974 (S.D. Fla. 6/11/18), involving nearby roadwork which caused dust and debris contamination of the restaurant, the court held damage to the property meant that actual damage or alteration to the property requiring repairs would be needed in order to trigger the policy coverage. In *Mastellone v. Lightning Rod Mutual Insurance Co.*, 175 Ohio App. 3d 23, 40-41, 2008 Ohio 311, 884 N.E. 2d 1130 (1/31/08), the court held that mold could be removed by cleaning so it did not affect the structural integrity of the building and, therefore, did not trigger business interruption coverage. In *Source Food Tech, Inc. v. USF&G,* 465 F.3d 834 (8 Cir. 2006), applying Minnesota law, the court held that beef imports banned for mad cow disease did not amount to "physical loss or damage." In *Newman Myers Kreines Gross Harris, P.C. v. Great American Insurance Company*, 17 F. Supp. 3d 323 (S.D.N.Y. 2014), the court held that a power shutoff in advance of Super Storm Sandy approaching did not amount to physical loss or damage. In *Universal Image Products v. Chubb Corp.,* 703 F. Supp. 2d 705 (E.D. Mich. 2010), the court held that mold and bacteria in the HVAC system was not physical damage to the property that was needed to trigger the insurance coverage.

On the other hand, there is case law supporting the inventive *Cajun Conti* argument that "non-altering" physical damage is present at the insured premises if there is "contamination" at the location, even if the contamination does not physically cause property damage.

For example, in *Gregory Packaging Inc. v. Travelers Property and Casualty Co. of America,* No. 12-04418, 2014 U.S. Dist. Lexis 165232 (U.S.N.J. 11/25/14), the court held that a release of an unsafe amount of ammonia in a facility amounted to a "direct physical loss," and that property can sustain a physical loss or damage without experiencing structural alteration. In *Wakefern Food Corp. v. Liberty Mutual Fire Ins. Co.*, 406 N.J. Super. 524, 968 A. 2d 724 (2009), the court held that property can be "just temporarily unfit" and trigger coverage.

Even if governmental shutdown orders close the insured's business, traditional business interruption coverage sections on policies usually still require the trigger of a physical damage or loss.

The commentary on COVID-19 business interruption insurance coverage has focused upon the 2006 ISO Form, Virus Exclusion. ISO Form CP 01 40 07 06 is

titled "Exclusion for Loss Due to Virus or Bacteria" and provides 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 stress, illness or disease . . . ." The exclusion goes on to state that it applies to business income, and it is reportedly found in many first-party property insurance policies since 2006.

Despite such an apparently clear exclusion for business interruption due to a virus pandemic, there have been suggestions that such an exclusion may be avoided either by arguing that the governmental closure order is the cause of the damage and not the contamination by the virus or by arguing the often used "reasonable expectations" doctrine.

At least in Louisiana, however, the reasonable expectations doctrine asserted by insureds was not successful in the Hurricane Katrina litigation, and those cases may be of interest here.

In *Vanderbrook v. UniTrin Preferred Ins. Co. (In Re Katrina Canal Breaches Litig.)*, 495 F.3d. 191 (5 Cir. 2007), the U.S. 5th Circuit Court of Appeals considered the claims by numerous homeowners in the New Orleans area regarding flood damage being excluded from their homeowners policies. Counsel for the insured homeowners advanced the "reasonable expectation" doctrine, as well as the "concurrent cause" argument, and alleged ambiguities in the insurance policy flood exclusions. The 5th Circuit upheld the flood exclusions in the policies (for those claims in which the hurricane force winds did not cause damage to the properties but only for damage caused by the flooding resulting from the collapse of the levees of the drainage canal in New Orleans).

With respect to the reasonable expectations argument advanced by counsel for the insureds, the 5th Circuit stated:

> The plaintiffs finally contend that the reasonable expectations of homeowners insurance policy holders would be the damage resulting from man-made floods would be covered. "[A]scertaining how a reasonable insurance policy purchaser would construe the clause at the time the insurance contract was entered" is one way that ambiguity in an insurance clause may be resolved. *L.A. Inc. Gaur. Ass'n. v. Interstate Fire and Casualty Company,* 630 So.2d at 764 (La. 1994). But "Louisiana Law . . . precludes use of the reasonable expectations doctrine to recast policy language when such language is clear and unambiguous." *Coleman v. Sch. Bd. of Richland Parish,* 418 F.3d 511, 522 (5 Cir. 2005). As we have explained, the flood exclusions in the policies are unambiguous in the context of the specific facts of this case; thus, we need not resort to ascertaining a reasonable policyholders expectations. 495 F.3d at 219.

Graffiti mural of Louis Armstrong wearing blue gloves and a face mask on his trumpet by Louisiana artist Josh Wingerter on boarded-up shops in New Orleans during the emergency declaration. *Photo by Barbara Baldwin.*

The 5th Circuit was not swayed by the argument that the homeowners policy contained coverage for hurricanes, and that the hurricane was a concurrent cause of the levee breaches due to construction faults and engineering deficiencies.

The 5th Circuit explained the policyholders' arguments regarding efficient proximate cause and anti-concurrent causation clauses in the policies. It found that the case did not represent a combination of forces that caused damage and it was not analogous to cases from Hurricane Katrina with damage through both wind and water. Instead it affirmed the district court in finding that, in this case, the cause conflates to the flood, meaning that the alleged negligence in design, construction or maintenance of the levees and the resulting flood were not separate causes of the plaintiffs' losses.

Consequently, the court concluded that the anti-concurrent causation clauses need not be addressed because they were not applicable.

It is also possible that pollution exclusion clauses might be a basis for denial of coverage. In *Westport Ins. Corp. v. VN Hotel Group, L.L.C.*, 761 F. Supp. 2d 1337 (M.D. Fla. 2010), the court held that legionella bacteria are not pollutants and thus the policy exclusion did not apply; and in *Johnson v. Clarendon National Insurance Company,* 2009 W.L. 252619, (California Court of Appeal 2/4/09), the court held that a pollution exclusion did not apply to mold and "likely would not apply to viral infections because the Court reasoned that the language of the pollution exclusion was unclear and would be interpreted in favor of coverage."

There are cases out there to the contrary. In *First Specialty Insurance Corp. v. GRS Management, Inc.,* No. 08-81356, 2009 W.L. 254613 (S.D. Fla. 8/17/09), the court held that the virus was a pollutant. The specific ISO Form "exclusion for loss due to virus or bacteria" provides 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 ISO circular dated July 6, 2006, used as part of its filings with State Regulatory Authorities, references rotavirus, SARS, influenza (such as avian flu), legionella and anthrax.

The ISO Form CP 00 30 10 12, titled "Business Income (and Extra Expense) Coverage Form," provides that the insurer will pay for the actual loss of business income sustained due to the necessary suspension of operations during the period of restoration. The suspension must be caused by direct physical loss of or damage to property at premises which are described in the declarations and for which a business income limit of insurance is shown in the declarations. The loss or damage must be caused by or result from a covered cause of loss. The form provides "with respect to loss of or damage to personal property in the open or personal property in a vehicle, the described premises include the area within 100 feet of such premises."

ISO Form PROP 12 19 09 17, titled "Ordinance or Law Coverage," includes the provision that "coverage under this endorsement applies only if: a) the building sustains only direct physical damage that is covered under this policy and is a result of such damage, you are required to comply with the ordinance or law . . . ."

Finally, some legislatures, notably New Jersey, Louisiana, Massachusetts and South Carolina, have either considered or enacted legislation to undo the insurance contract's restrictions on COVID-19 coverage. There is a persuasive argument that these political fixes to gut the insurance contract are unconstitutional.[7] The New Jersey Legislature is considering a bill to force insurers to pay COVID-19 business interruption claims despite the ISO Form Virus Exclusion used in the policies issued to the insureds in New Jersey with businesses of less than 100 employees. The proposed legislation contains language to the effect that "notwithstanding the provision of any other law, rule, or regulation to the contrary, every policy of insurance insuring against loss or damage to property, which includes the loss or use of occupancy of business interruption enforced in this state . . . shall be construed" to include coverage for COVID-19 business interruption losses. Similar legislation may be proposed in other states, but, of course, all such litigation will be subject to constitutional challenge.

Conclusion

Courts will struggle with the equities of huge losses from business owners in the COVID-19 pandemic. There will be a siren appeal to listen to the creative and innovative arguments put forward to avoid the plain contractual meaning that blocks coverage for such claims. Courts must hold fast, like Odysseus, and not die on the rocks listening to this sweet sounding siren song.

FOOTNOTES

1. There are staggering business losses from COVID-19 shutdowns as businesses close on every block in every neighborhood. Some estimates put United States business losses for those with fewer than 100 employees at $431 billion per month. Over two months, those losses exceed the total amounts for domestic insurers reserved for every kind of risk. The Paycheck Protection Program total funding for small business forgivable loans is approximately $600 billion as of this writing. The cost of the cure, requiring unprecedented business closure leading to financial ruin and failure, may exceed the cost to have done nothing.

2. The impact of the post COVID-19 Cares Act Legislation that provides for forgivable loans to small business is not discussed in this article except to note that such loans, which turn into grants, may decrease an insured's business interruption loss to some extent but not erase it.

3. "Any effort to deny the reality that the virus causes physical damage and loss would constitute a false and potentially fraudulent misrepresentation that could endanger shareholders and the public." *Cajun Conti* Petition.

4. The Chickasaw Nation case seems to just assume physical loss: "as a result of this pandemic the nation's property sustained direct physical loss or damage . . . ." Chickasaw Nation v. Lexington Insurance Company, Case No. CV-20-35 (Oklahoma Dist. Ct., Pontotoc County) (2020).

5. The U.S. Congress is already working on what happens for business interruption claims in the next pandemic, and it may look like the risk sharing now used for terrorist insurance coverage. Those changes would not apply to the COVID-19 fights. "Insurers Oppose Pandemic Liability Plan," Wall Street Journal, B-10, May 15, 2020.

6. Jenner & Block newsletter, March 12, 2020, by David Kroeger and Elin Park, *https://jenner.com/system/assets/updates/1508/original/kroeger%20park%20March%20ILU%20March%2012%202020.pdf?1585603708*.

7. See United States Constitution, Article 1, Section 10 (No state shall pass a law impairing the obligations of contract).

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