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COVID-19 Insurance Update: More Court Decisions on Insureds' Claims Against Their Property Insurance Policies for Coverage of Their COVID-19 Losses

by Patrick Frye

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A great deal of money is at stake between property insurers and the businesses they insure in those insureds' lawsuits over whether business-interruption or civil-authority insurance covers the businesses' substantial and widespread loss of revenue resulting from their closures during the COVID-19 pandemic. We reported in a prior alert that the first five judicial decisions on these disputes went 4 to 1 in the insurers' favor, summarily rejecting even the possibility of insurance coverage for these losses. The next twenty-six decisions have largely gone the insurers' way, 19 to 7. The 8 total decisions won by an insured mean that these insureds will have the opportunity to prove their case, which they may succeed in accomplishing in the end – but perhaps they will not.

Decisions in favor of the insurers

The decisions in favor of the insurers provide examples of several significant arguments against coverage prevailing. First, insurers argue that the alleged presence of the virus or of people sick from the virus are not "direct physical loss of or damage to" property that the insured must show to make a recovery under the insurance policy's business-interruption or civil-authority coverages. For that reason, *Pappy's Barber Shops v. Farmers Group* (S.D. Cal. Oct. 1, 2020) refused to allow the plaintiff to re-plead its complaint to add those allegations. *Oral Surgeons v. Cincinnati Insurance Co.* (S.D. Iowa Sept. 29, 2020) likewise found no allegation of "accidental physical loss" in a plaintiff dentist's complaint that he closed his office because of the virus (and government orders).

Second, insurers argue that the insured business's closure in compliance with government stay-at-home orders is not "direct physical loss of or damage to" property either. *Malaube LLC v. Greenwich Insurance Co.* (S.D. Fla. Aug. 26, 2020) reasoned that the government orders were not based on any tangible loss of or damage to the insured restaurant's property and although they forced the restaurant to close, there was no physical problem with the property.

10E LLC v. Travelers Indemnity Co. (C.D. Cal. Sept. 2, 2020) similarly found no physical alteration or loss from a government order – the insured restaurant remained in possession of its property, which was intact, using reasoning adopted by *Mark's Engine Co. No. 29 Restaurant v. Travelers Indemnity Co.* (C.D. Cal. Oct. 2, 2020) in dismissing a similar complaint brought by another restaurant. Citing *Malaube* and *10E* on these points, *Pappy's Barber Shops v. Farmers Group* (S.D. Cal. Sept. 11, 2020) arrived at the same result. *Sandy Point Dental v. Cincinnati Insurance Co.* (N.D. Ill. Sept. 21, 2020) agreed, characterizing the claims as seeking recovery for financial losses following closure orders, with the property entirely unaltered by the virus itself. Literally repeating that reasoning, *It's Nice v. State Farm Fire & Casualty Co.* (Ill. Cir. Ct. Sept. 29, 2020) added while dismissing another complaint that the plaintiff restaurant did not allege loss resulting from an inability to access its own property or from the actual presence of the virus on any surface at the insured property. *Infinity Exhibits v. Certain Underwriters at Llyod's* (M.D. Fla. Sept. 28, 2020) likewise found that the economic loss resulting from government orders did not result from any actual physical damage to property.

Henry's Louisiana Grill v. Allied Insurance Co. (N.D. Ga. Oct. 6, 2020) offered this summary of another restaurant's argument: "Under the Plaintiffs' logic, a minute before the Governor issued the Order, the dining rooms existed in one state. A minute later, the Governor issued the Order, and the restaurant underwent a direct physical change that left the dining rooms in a different state." *Henry's* disagreed with that logic and dismissed the insured's complaint.

Relatedly, insurers dispute the contention that physical loss is shown by the insureds' inability to use their property for their business functions. *Turek Enterprises v. State Farm Automobile Mutual Insurance Co.* (E.D. Mich. Sept. 3, 2020) – which considered the phrase "direct physical loss to property" – rejected the insured chiropractor's functionality argument because this arguable physical loss was not one to property. *Mudpie Inc. v. Travelers Casualty Insurance Co.* (N.D. Cal. Sept. 14, 2020) drew the same conclusion against a children's store but for a different reason: loss of a property's function could count as physical loss only if that loss resulted from a physical force (e.g., the compromised structural integrity of the building containing the insured property, which was not damaged itself), which the government orders themselves are not. *Plan Check Downtown III v. AmGuard Insurance Co.* (C.D. Cal. Sept. 16, 2020) also rejected the functionality argument, this time for want of tangible alteration to the insured's restaurants. It concluded that the phrase "loss ***of*** … property" was not meaningfully distinct from "loss to property," which was decided in prior cases to require physical damage. "Ultimately, the Court finds that [insured] Plan Check's interpretation is not a reasonable one because it would be a sweeping expansion of insurance coverage without any manageable bounds," in that insurance recoveries could be had for changes in municipal ordinances or zoning and other events that limit the use of otherwise physically available and ready property. *Henry's* similarly noted that this theory of an insurer's liability may create coverage should the government lower a restaurant's maximum occupancy.

Vandelay Hospitality Group v. Cincinnati Insurance Co. (N.D. Tex. Oct. 7, 2020) dismissed a restaurant group's complaint as too conclusory to amount to an adequate pleading of direct physical loss or damage. It, however, left open the possibility that the insured may later plead a legally plausible claim. *The Inns by the Sea v. California Mutual Insurance Co.* (Cal. Super. Ct. Aug. 4, 2020) did not, apparently concluding that plaintiff's claim had no possible merit.

Third, insurers argue that those government orders do not prohibit access to the insured's property so as to bring a claim within the policy's civil-authority coverage. *Pappy's* held that government orders forbidding the operation of businesses did not prohibit access to the property that housed those businesses. It further ruled that the government order did not result from any physical loss of or damage to any other property. *10E* also decided that the government order was not based on physical damage at other property by virtue of the virus's presence there, because the virus's general spread to various physical surfaces presented a "mere possibility" instead of actual direct physical damage. *Mudpie* similarly noted that rather than react to arguable physical damage at any location, the government orders were preventative means to stop the virus from spreading. In addition to noting the lack of any physical damage to any property, *Sandy Point* decided that access was not prohibited to the insured dental office, given that the closure order allowed dentists to perform emergency and non-elective procedures.

Some state governments did not limit access to businesses. *Henry's* found no government-ordered closure because although the Georgia governor advised people to stay home, his order did not limit access to any business. *Harvest Moon Distributors v. Southern-Owners Insurance Co.* (M.D. Fla. Oct. 9, 2020) addressed the complaint of a distributor that sued over its beer that spoiled after Walt Disney Parks refused to accept shipment because Disney voluntarily closed due to the pandemic. While the spoiled beer was adequately pled as damaged property, the complaint was dismissed because the policy excluded damages caused either by delay, loss of use, or loss or market or by the acts or decisions of any person, organization, or government. The beer spoiled not because of the pandemic, but because Disney's decision to close cost the distributor its customer.

Fourth, insurers argue that the virus exclusion prohibits coverage of loss regardless of whether it is due to COVID-19 or instead to government orders. *Martinez v. Allied Insurance Co.* (M.D. Fla. Sept. 2, 2020) dismissed a dentist's claims for the cost of decontaminating his office and the income he lost when the governor restricted dental services during the COVID-19 pandemic to emergency procedures only. Because these losses resulted from COVID-19, which is "clearly a virus," his policy covered none of them. *Turek* applied the exclusion because the government order that closed the chiropractor practice expressly stated that it was issued to suppress the spread of COVID-19. Even though the order rather than the virus was the more proximate cause of the insured's losses, the policy's anti-concurrent causation clause made clear that the exclusion reaches causes that are not the most immediate. *It's Nice* decided the same, explaining that the actual spread or presence of the virus was unnecessary to the application of the exclusion. *Turek* also rejected the argument that the virus exclusion was only meant to apply to contamination by disease-causing viruses, because the exclusion does not state any such limitation on its scope. *Wilson v. Hartford Casualty Co.* (E.D. Pa. Sept. 30, 2020) and *Mark's Engine* also dismissed a lawsuit under the virus exclusion.

Franklin EWC v. Hartford Financial Services Group (N.D. Cal. Sept. 22, 2020) found the exclusion to apply to the insured wax center's claim for civil-authority coverage. For the insured to recover this type of coverage, access to the property had to be prohibited by a civil-authority order issued "as the direct result of a Covered Cause of Loss," and the wax center alleged that the closure orders were issued because "the COVID-19 virus [was] spreading." The wax center claimed that the closure orders themselves were the Covered Cause of Loss, but this judge refused to count those orders not only as the orders resulting from the Covered Cause of Loss but also as the Covered Cause of Loss that resulted in the orders. To quote this judge: "Nonsense."

Decisions in favor of the insureds

The insurers' same arguments against coverage failed in the equally remarkable decisions rendered in favor of the insureds. *Optical Services USA v. Franklin Mutual Insurance Co.* (N.J. Super. Ct. Aug. 13, 2020) considered the claim of opticians who closed their business because of government stay-at-home orders issued to tamp down the risk of transmission of the virus that causes COVID-19. Seeking civil-authority coverage, the opticians contended that they suffered physical loss from the loss of the "functionality" of their premises and that access to those premises was prohibited by the stay-at-home orders. Rather than categorically rule out the possibility that this coverage was available for the insureds' "novel theory of insurance coverage," the court allowed their claim to proceed so that a decision on the merits may be made later based on the evidence of the factual circumstances surrounding this particular claim.

In *Blue Springs Dental Care v. Owners Insurance Co.* (W.D. Mo. Sept. 21, 2020), the insured dentists alleged COVID-19 and stay-at-home orders forced them to suspend most of their operations and deprived them of the use of their clinics. This court ruled that the dentists alleged direct physical loss by contending that their customers and employees "likely" were infected with the virus that allegedly physically attached to their clinics. The court further ruled that that the facts surrounding the dentists' claim to civil-authority coverage needed to be investigated and developed because their coverage may trigger upon the restriction of "any" (as opposed to "all") access to the premises, and it was unclear whether the government orders permitted them to provide their non-essential services while continuing to offer their "essential" services. *KC Hopps Ltd. v. Cincinnati Insurance Co.* (W.D. Mo. Aug. Aug. 12, 2020) perfunctorily reached the same conclusions, for the same reasons the same judge had refused (on the same day) to dismiss the complaint filed in *Studio 417 v. Cincinnati Insurance Co.* (W.D. Mo. Aug. Aug. 12, 2020), which we reported in an earlier alert. The judge who decided these two cases also decided Blue Springs.

Urogynecology Specialist of Florida v. Sentinel Insurance Co. (M.D. Fla. Sept. 24, 2020) decided not to apply the policy's virus exclusion to bar the claims of gynecologists who shut their practice after the governor declared an emergency. The court reasoned that COVID-19 losses do "not logically align" with the losses within the scope of the virus exclusion, i.e., those losses stemming from "fungi, wet rot, dry rot, bacteria or virus." Describing the pandemic's effect on society as "unique," the court distinguished the gynecologists' claims from prior claims that courts decided were barred under the virus exclusion because the insured was accused of transmitting a virus or the claim otherwise resulted from illness or disease.

Insureds also prevailed in several state court decisions that declared the insureds' complaints adequately pled without further explanation: *Best Rest Motel v. Sequoia Insurance Co.* (Cal. Super. Ct. Sept. 30, 2020); *Johnston Jewelers v. Jewelers Mutual Insurance Co.* (Fla. Cir. Ct. Sept. 22, 2020); *Ridley Park Fitness v. Phila. Indemnity Insurance Co.* (Pa. Ct. Com. Pl. Aug. 31, 2020).

Inconsistent and not yet definitive decisions

The United States does not have nationwide uniform law on contracts. Instead, each individual state determines how contracts are treated under its laws. Variety among so many states helps explain why diametrically opposite decisions were issued by courts considering essentially the same issues raised under the same alleged facts and policy language. But interstate differences do not explain it all. Two Florida judges, sitting in the same federal district, issued contradictory decisions because the judges had completely different understandings of the virus exclusion. These are the decisions of trial courts, which may later be affirmed or reversed by courts of appeal that make the authoritative law that should be uniform at least across the state where they sit. Indeed, every decision discussed in this alert may later be altered by an appellate court.

While consistent patterns may be emerging in some states' case law resolving insurance claims for COVID-19 losses, those decisions do not dictate the development of the same case law in other states and themselves may yet be undone by a later court.

If you have any questions, contact Patrick Frye or visit Freeborn's COVID-19 webpage.

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