

Business Interruption Insurance in the COVID-19 Environment

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What we'll cover:

- ▶ What is Business Interruption Insurance?
- ▶ How to determine if you have this coverage
- ▶ Will it cover COVID-19-related business interruption?
 - ▶ Is it a “covered loss?”
 - ▶ Virus/Bacteria exclusion
 - ▶ Civil authority coverage
- ▶ How do you challenge a claim denial if you want to pursue a claim against your insurer?

What is Business Interruption Insurance?

- ▶ About 30% of US businesses have this coverage.
- ▶ Provides coverage for business income lost as the result of a “covered loss.”
 - ▶ Traditionally triggered by a disaster (E.g., a fire destroys the business premises, and income is lost while the business rebuilds) - key is in the wording of the policy
 - ▶ Likely also applies if government actions require the business to close temporarily due to harm at the premises
- ▶ Not sold as a stand alone policy - can be added to a property/casualty policy.
- ▶ May be part of the a “comprehensive” commercial policy as a “rider.”
- ▶ This is important because you have to read the coverage forms together to determine what triggers business interruption coverage (and what type of losses are excluded from coverage).
- ▶ Some BII will cover a partial interruption in business in addition to total interruption.

“All Risk” v. “Named Peril”

- ▶ Property policies come in two flavors
 - ▶ All risk = covers all “direct physical loss or damage” not specifically excluded or limited by the policy
 - ▶ Named peril = coverage only for loss caused by the perils specifically named in the policy (e.g., fire policy - covers only loss caused by a fire)
- ▶ Type of policy influences analysis of whether BII could be triggered by COVID-19-related loss

Most policies made up of series of standard coverage “forms” designed for risks in business’ industry

- ▶ Standard Forms created by insurance industry organizations
 - ▶ ISO (Insurance Services Office, Inc.)
 - ▶ AAIS (American Association of Insurance Services)
- ▶ The forms are presented to regulators in each state, and may be approved as written, or modified by the regulator
 - ▶ E.g., you may see a “NH Endorsement” in your policy that changes one of the standard forms
 - ▶ This becomes important when considering if there is a challenge to enforceability of any of these forms.

To determine if BII applies, you need to analyze policy as a whole to see if risk covered:

- ▶ First step: Is type of risk generally covered in the policy you bought?
- ▶ Second step: Are there any exclusions to coverage? (e.g. Virus exclusion)
- ▶ Third step: Are there any “buybacks” in coverage or exceptions to exclusions? (e.g, civil authority coverage)

If BII is triggered, how much does it cover?

- ▶ Policy will state if there is a particular limit to the amount of coverage it will provide per claim
- ▶ Generally amount payable is based on past financial records of the business. Typical categories of business loss covered:
 - ▶ Profits
 - ▶ Fixed Costs
 - ▶ Temporary Location - some policies will cover costs of setting up the business in a temporary location
 - ▶ Training costs - if need to retrain staff upon resumption of business or while in a temporary location
 - ▶ Extra expense - reasonable expenses (in addition to fixed costs) that allow business to resume
 - ▶ Civil authority ingress/egress - may cover government-mandated closures (e.g., curfew imposed by civil authority that affects business hours of operation)
 - ▶ Employee wages
 - ▶ Taxes
 - ▶ Loan Payments

How long of an interruption will BII cover ?

- ▶ Depends on policy limits - typically, up to a year but can be extended (higher premium)
 - ▶ Insured needs to make diligent efforts to restore business operation
 - ▶ Once business resumes operations, coverage terminates even if limit has not been reached

So what about COVID-19? Does my BII cover my business interruption losses due to the business shutdowns?

This is where it gets interesting:

- ▶ Insurance industry is steadfastly maintaining that BII does not apply
 - ▶ No covered “direct physical loss” that triggers the BII coverage
 - ▶ Virus exclusions
 - ▶ Civil authority coverage doesn’t apply
- ▶ A few test cases have just been filed in last month challenging this policy interpretation primarily by business with a lot at stake (e.g. Oceana Grill in New Orleans and French Laundry in Napa Valley have filed lawsuits seeking coverage under business interruption policies)

Does Pandemic Create a “Covered Loss”?

Start analysis by asking if the type of risk is covered (even if we have to also consider exclusions)

Coverage triggered by “Direct Physical Loss”

- ▶ Includes risks of destruction of or harm to premises - like a fire, or tree falling on roof
- ▶ NH Supreme Court has never examined whether viral pandemic can create “direct physical loss”
 - ▶ Has determined that noxious smell (cat urine odor) permeating building to be “direct physical loss”
- ▶ Other courts have determined “direct physical loss” to include:
 - ▶ Ammonia smell in facility
 - ▶ Gasoline vapors permeating a church
 - ▶ Pervasive odor from “meth” lab that infiltrated a house
 - ▶ Lead dust in building

What if property has actual COVID-19 contamination?

- ▶ Insurers argue that since virus can be cleaned off surfaces there is no direct physical loss to the property

BUT

- ▶ Some courts have determined that contamination is sufficient to satisfy “direct physical loss” requirement - mixed results around country
- ▶ E.g., PA case holding that bacterial contamination of a well is “direct physical loss” if building is not useable as a result

But is a “fear” of COVID-19 contamination enough? Would you have to prove actual contamination to have any hope of coverage?

Policyholders taking view that business closure orders are based on presumption of contamination

- ▶ CDC has stated that person can get COVID-19 “by touching a surface or object that has the virus on it and then touching their own mouth, nose, or possibly their eyes.”
- ▶ So even though surfaces can be cleaned, the pervasiveness of the virus in the community means that the surfaces must be presumed to be contaminated until the virus is eradicated in the community.

Case Analysis: Assume a NH restaurant is permitted to do takeout only...

- ▶ Can there be a “direct physical loss” if restaurant is able to serve patrons through takeout - must be sanitary enough, right?
- ▶ Isn't closure of dining room just an order of a civil authority not based on direct physical loss?(we'll take a look at that in a few minutes)
 - ▶ If purely a government-ordered closure, and no actual contamination, then seems unlikely to constitute “direct physical loss”
- ▶ But what about the “cat odor” case? - there was no structural harm to the building...

Even if “direct physical loss”
established, is coverage excluded by
Virus and Bacteria Exclusions?

SARS Epidemic in early 2000s caused the insurance industry to develop coverage exclusions...

Virus or Bacteria Exclusion - 2006 AAIS form

virus exclusion.pdf - Adobe Acrobat Pro DC
File Edit View Window Help iManage
Home Tools virus exclusion.pdf x

Page 1 of 1 -- PLEASE READ THIS CAREFULLY --

VIRUS OR BACTERIA EXCLUSION

DEFINITIONS

Definitions Amended --

When "fungus" is a defined "term", the definition of "fungus" is amended to delete reference to a bacterium.

When "fungus or related perils" is a defined "term", the definition of "fungus or related perils" is amended to delete reference to a bacterium.

PERILS EXCLUDED

The additional exclusion set forth below applies to all coverages, coverage extensions, supplemental coverages, optional coverages, and endorsements that are provided by the policy to which this endorsement is attached, including, but not limited to, those that provide coverage for property, earnings, extra expense, or interruption by civil authority.

- The following exclusion is added under Perils Excluded, item 1.:

Virus or Bacteria --

"We" do not pay for loss, cost, or expense caused by, resulting from, or relating to any virus, bacterium, or other microorganism that causes disease, illness, or physical distress or that is capable of causing disease, illness, or physical distress.

This exclusion applies to, but is not limited to, any loss, cost, or expense as a result of:

- any contamination by any virus, bacterium, or other microorganism; or
- any denial of access to property because of any virus, bacterium, or other microorganism.

2. **Superseded Exclusions --** The Virus or Bacteria exclusion set forth by this endorsement supersedes the "terms" of any other exclusions referring to "pollutants" or to contamination with respect to any loss, cost, or expense caused by, resulting from, or relating to any virus, bacterium, or other microorganism that causes disease, illness, or physical distress or that is capable of causing disease, illness, or physical distress.

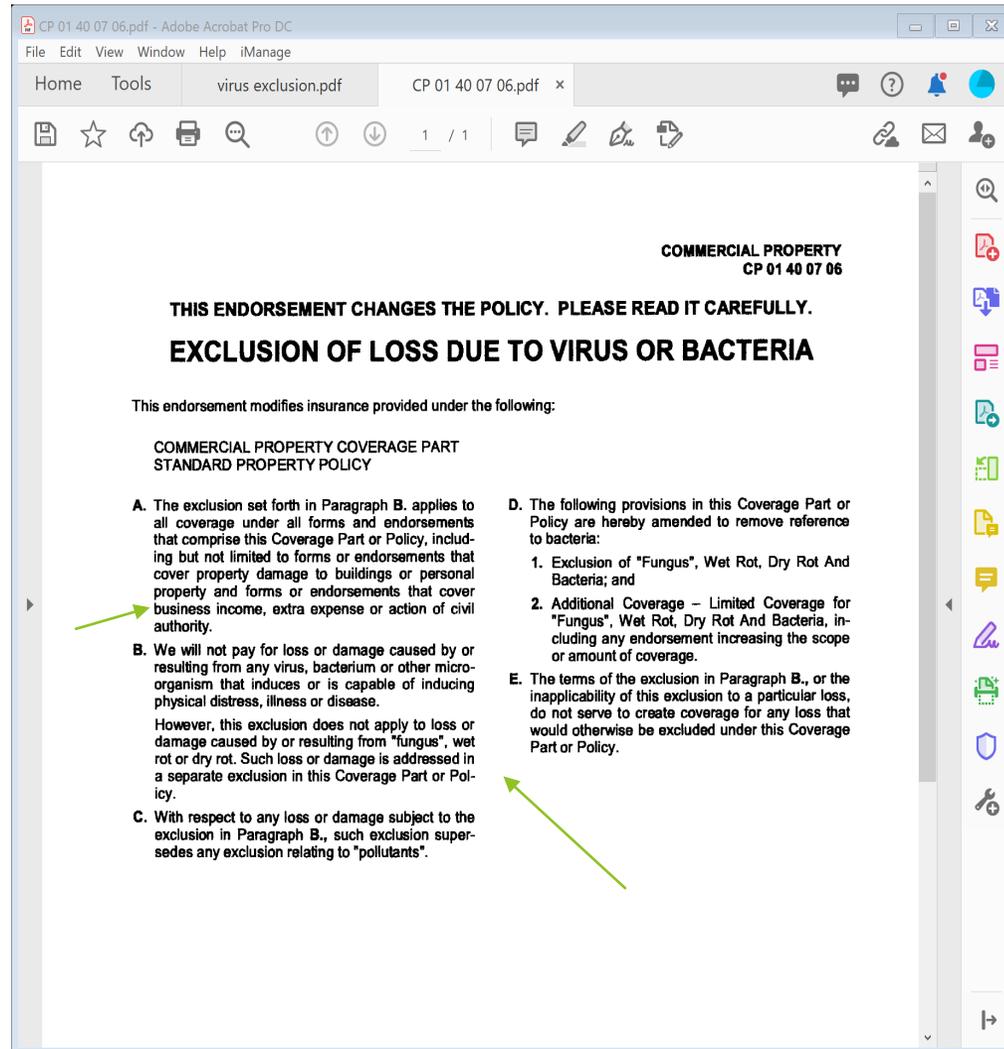
OTHER CONDITIONS

Other Terms Remain in Effect --

The "terms" of this endorsement, whether or not applicable to any loss, cost, or expense, cannot be construed to provide coverage for a loss, cost, or expense that would otherwise be excluded under the policy to which this endorsement is attached.

CL 0700 10 06

2006 ISO-based form



So is it “game over” if my policy has a virus exclusion?

Argument being advanced is that even if these exclusions are in policy they should not be enforced as a matter of public policy...

What did ISO and AAIS tell regulators

ISO submitted Circular (7/6/06) to regulators that stated in relevant part:

“While property policies have not been a source of recovery for losses involving contamination by disease-causing agents, the specter of pandemic or hitherto unorthodox transmission of infectious material raises the concern that insurers employing such policies may face claims in which there are efforts to expand coverage and to create sources of recovery for such losses, contrary to policy intent.

In light of these concerns, we are presenting an exclusion relating to contamination by disease-causing viruses or bacteria or other disease-causing microorganisms.

Separately, AAIS filed the following Filing Memorandum:

“Property policies have not been, nor were they intended to be, a source of recovery for loss, cost, or expense caused by disease-causing agents.

With the possibility of a pandemic, there is concern that claims may result in efforts to expand coverage to create recovery for loss where no coverage was originally intended ...

This endorsement clarifies that loss, cost, or expense caused by, resulting from, or relating to any virus, bacterium, or other microorganism that causes disease, illness, or physical distress or that is capable of causing disease, illness, or physical distress is excluded ...”

So what?

- ▶ Prior to 2006, courts had found coverage under property policies for the following:
 - ▶ E Coli bacteria,
 - ▶ radioactive dust,
 - ▶ noxious air particles,
 - ▶ lead,
 - ▶ asbestos,
 - ▶ mold,
 - ▶ mildew,
 - ▶ “health-threatening organisms,”
 - ▶ vaporized agricultural chemicals, and
 - ▶ pesticides.
- ▶ Creates an argument that insurance industry was misrepresenting state of law to regulators.

But can't the insurers just add an exclusion?

- ▶ Yes, but it effects what premium they can charge if they are removing coverage that is there. Regulators would REDUCE allowable premium amounts if coverage is reduced
- ▶ Commentators are asserting that 2006 introduction of Bacteria and virus exclusion, coupled with representation that exclusion did not reduce coverage (i.e., asserting that this risk was never covered), allowed insurers to still charge same premiums
- ▶ Raises question of whether the exclusion is enforceable if procured through misrepresentation to regulators
- ▶ This argument likely to be tested in lawsuits

My policy covers closures caused by civil authorities...does that provide coverage despite the virus exclusion?

Depends on wording, but probably does not alter virus exclusion...

- ▶ For coverage to apply, government action has to be taken to close a business “in response to dangerous physical conditions resulting from the damage or continuation of the Covered Cause of Loss that caused the damage.”
- ▶ Governor’s orders closing businesses arguably not based on damage in a particular business or actual dangerous physical condition
 - ▶ Designed to reduce extent of virus outbreak

Isn't presumption that virus could get on surfaces within business enough?

- ▶ Seems like a difficult argument...
- ▶ Key to civil authority coverage is that the action to close business is taken in response to a dangerous condition, not fear of a potential dangerous condition developing.
- ▶ Courts are split on whether threat of damage meets policy requirements
 - ▶ E.g. evacuation cases when a hurricane threatens to impact an area
 - ▶ GA - hurricane evacuation order was a covered loss
 - ▶ TX - opposite conclusion - threat of harm not enough for a “direct physical loss” so civil authority coverage did not provide coverage

What about “spoilage” coverage?

- ▶ This comes into effect when you suffer losses due to spoilage of inventory
- ▶ Triggered by breakdown in refrigeration equipment due to things like power outage, or actual contamination of food products (like e.coli outbreak)
 - ▶ Not what is happening here

I bought “Contingent Business Interruption” coverage, does that apply?

- ▶ This type of coverage covers business loss because of a disruption in supply or distribution chain because the supplier or customer has suffered a covered loss
- ▶ This type of insurance is typically an add-on - You need to ask for it and probably pay an extra premium for it
- ▶ Same coverage analysis applies, only you examine whether the supplier or customer had the “direct physical loss” that then affects your business...
 - ▶ You can’t get the supplies you need
 - ▶ You can’t deliver your product because of the customer’s covered loss

Some state legislatures are introducing bills to require coverage of COVID-19...

- ▶ Headlines report that other states (e.g., NJ, OH and MA) are introducing legislation to mandate coverage for business interruption notwithstanding virus exclusions.
 - ▶ Essentially trying to retroactively change the insurance policy to require coverage for COVID-19 losses.
- ▶ Creates significant constitutional problems - such laws unlikely to be enforceable.
 - ▶ Also cuts against insureds who are arguing that coverage does exist (wouldn't need law if coverage was there).

Challenging coverage

- ▶ First need to make claim with your insurer
- ▶ If insurer denies coverage... Declaratory Judgment action can be filed in State or federal court
- ▶ Insurer has burden of proving non-coverage
- ▶ If insured prevails, insurer must pay attorneys' fees and costs of action
- ▶ Typically 12 month limitations period from time coverage denied

ANY QUESTIONS?