Insurance Coverage Lawsuits Quickly on the Rise in the Wake of COVID-19

Main Contact(s)

Tamara Smith Holtslag

Partners

Timothy O. Egan

Scarlett M. Rajbanshi

Related Practices

Insurance Coverage and Bad Faith Litigation

By Timothy O. Egan, Scarlett M. Rajbanshi, Tamara Smith Holtslag on May 15, 2020

INTRODUCTION

The COVID-19 pandemic has impacted nearly every aspect of society and commerce and the insurance industry is no exception. State and local governments have enacted a variety of orders, which have effectively closed all non-essential businesses including restaurants, bars, theaters and salons. Other businesses are operating on a reduced capacity and many remotely. A staggering number of workers have been furloughed, laid-off or let go, resulting in over 30 million people filing for unemployment benefits in a matter of weeks. As a result of these orders, national and local businesses are trying to contend with unprecedented losses. In an effort to cope with their losses, many businesses are seeking coverage under their commercial insurance policies. Disputes and lawsuits over insurance coverage have already begun in earnest.

An examination of the suits filed across the country so far reveals that many of the disputes between insurers and their insureds concern the availability of "business interruption" coverage. This coverage is often found under the "business income and extra expense" coverage part(s) of an "all- risk" policy, which typically include "Civil Authority" coverage. A common prerequisite for coverage under this "Civil Authority" provision is an action of civil authority that prohibits access to the insured's premises. However, as the filed lawsuits illustrate, while "all-risk" policies provide broad coverage, they are often issued with various exclusions/endorsements, which may limit or bar coverage for losses caused by viruses. However, some insurers provide additional coverage to their insureds for losses caused by viruses in exchange for a higher premium. As always, the particular policy language is central to any insurer's determination of coverage.

PENDING LAWSUITS

In the first quarter of 2020, various lawsuits have been filed in the state and federal courts in which policyholders have challenged their respective insurers' denials of coverage.

Since the end of March, Peabody & Arnold has been actively monitoring almost 200 new lawsuits seeking insurance coverage for COVID-19 related losses. Upping the ante, many of these cases have been brought seeking class action status. At the forefront of this recent activity, food service providers ranging from individual restaurants to national chains such as P.F. Chang's and Legal Seafoods have filed suits seeking coverage for their anticipated business losses. While restaurant policyholders make up a large percentage of claims, lawsuits have been filed by a wide variety of businesses including law firms, day care centers, dentists, landlords, hair salons, trucking companies and printing companies. Most, if not all, of the cases filed have sought declarations of coverage under the "Civil Authority" coverage part. By contrast, many of the insurers (according to the complaints) take the position that the government orders closing businesses are not a result of "direct physical loss of or damage to property" near the vicinity of the covered premises.

While all cases vary in the details, typically the insurer is alleged to have denied or threatened to deny coverage because the "actual or alleged presence of the corona virus" did not constitute "direct physical loss" as defined by the insured's policy. In challenging the declination of coverage, the plaintiff insureds have claimed that the presence of coronavirus on or around their business has rendered their premises unsafe and unfit, and therefore, the loss of use of the property constitutes "physical property damage."

In almost all of these cases, insurers are faced with trying to ascertain whether the closure of "non-essential" businesses by state and local ordinances, e.g. an act of civil authority prohibiting access to commercial business properties caused by COVID-19 health concerns, constitutes a direct physical loss of or damage to property caused by or resulting from a covered cause of loss. Unfortunately, unlike other types of claims, there is little historical or legal precedent to help guide insurers to appropriately determine coverage, under a particular policy or governing law, in this COVID-19 setting. Complicating the picture, insurers must be cognizant of state and local government ordinances when assessing whether such acts of civil authority actually prohibit access to their insured's commercial business, and whether the resulting business losses constitute covered property damage.

If an insurer concludes that coverage is afforded for its insured's business losses under its particular policy, there still remains the challenge of assessing the potential claim exposure. Traditionally, "Civil Authority" coverage subparts have a finite duration, e.g. three consecutive weeks seeming the most common. Other types of coverage provided under the business income and extra expense coverage part, such as extended business income coverage, provide coverage until the earlier of the date the policyholder could restore its operations to the level which would generate the business income that would have existed if no direct physical loss or damage had occurred or 30 consecutive days. In this COVID-19 setting, (even as some states are starting to encourage "re-opening" of certain businesses), the timeline associated with each insured's alleged damage to its operations is likely unique.

Against this backdrop of uncertainty, insurers are faced with making appropriate determinations of coverage but without similar, historical claims or legal precedent to guide them. As the COVID-19-related insurance coverage cases begin to make their way through the court system, many of these cases may become bellwethers for those yet to be filed.

PENDING STATE LEGISLATION

Outside the coverage battles in the courtroom, state legislators across the country have been introducing a series of bills that could force insurers to pay a policyholder's business interruption losses caused by COVID-19, regardless of the insurance contract terms. If passed, these bills could eviscerate any policy exclusion or endorsement limiting coverage based on viruses and would effectively change the insurance contract terms by retroactively inserting a new definition into many existing insurance policies to include COVID-19 related losses as physical damage.

For example, the Massachusetts legislature,[1] has put forth Bill S.2655, which, if enacted into law, would prohibit an insurer from denying a claim for business interruption because COVID-19 is a virus; or from denying coverage based on the absence of physical damage to the insured property or to any other relevant property. Notably, Bill S.2655 expressly states that it is subject to the Massachusetts insurance bad faith statute, G.L. c. 176D, "for the avoidance of doubt." Even though the proposed bill would only apply to policyholders with 150 or fewer full-time equivalent employees in Massachusetts, the impact

and unprecedented legislative interference in private insurance contract terms is likely to be profound; and would almost certainly be challenged on constitutional grounds. New Jersey, Ohio, and New York introduced substantially similar bills, but none have yet been passed into law.

If enacted, the insurance industry may be inclined to challenge the statutes on constitutional grounds. Colloquially known as the "Contracts Clause," Article 1, Section X, Clause 1 of the United States Constitution prohibits a State from passing any law impairing the private rights of contracting parties.[2] Insurers may well rely upon this oft-overlooked constitutional clause and the potential merits of a constitutional defense if forced to challenge any new state law requiring coverage against business losses due to COVID-19.

Our firm and our coverage litigation group are following these legal and statutory filings to keep our clients informed of these developments. Click HERE to receive periodic updates to this article.

_____

[1]https://malegislature.gov/Bills/191/SD2888?fbclid=IwAR1C92UdvFG7jj1KqivCdqGAh5mgUVMLqFrquRXL-Mm1K7UccX5iynGsg4A

[2] U.S. Tr. Co. of New York v. New Jersey, 431 U.S. 1, 32, 97 S. Ct. 1505, 1523, 52 L. Ed. 2d 92 (1977); Home Bldg. & Loan Ass'n v. Blaisdell, 290 U.S. 398, 429, 54 S. Ct. 231, 237, 78 L. Ed. 413 (1934).

