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COVID-19 business-interruption claims

GETTING AROUND THE "VIRUS" EXCLUSION MAY REQUIRE A LOT OF CAREFUL READING AS LANGUAGE DIFFERS BETWEEN POLICIES

Over the past few weeks during the COVID-19 pandemic, there have been flurries of claims made by businesses to their insurance companies for business-interruption coverage. By now, many lawyers have reviewed mind-numbing insurance policies to see if coverage can be captured for prospective clients. While there are many moving parts to analyzing business-interruption coverage claims, there are two that are at the top of the list.

The first is how to satisfy the threshold requirement of a "physical loss of or damage to" covered property. The second is how to deal with a "virus" exclusion if one is in the policy.

This article will not address the issue of establishing "physical loss of or damage to" covered property. Rather, the focus of the discussion will be on addressing the issue of a virus exclusion and ways to capture coverage around it.

All-risk vs. stated peril coverage

Most business interruption coverages are written on an "All Risk" basis, which means that all conceivable risks of loss are covered unless they are specifically excluded. It is the broadest form of first-party coverage available. In contrast, "Stated Peril" policies only cover those risks of loss that are specifically identified in the policy as covered.

But not every "All Risk" policy identifies itself as such in the same manner. With some policies, you must navigate through more than one section of a lengthy policy to

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determine if the policy is indeed an "All risk" policy. The following are examples taken from actual insurance policies that grant "All Risk" coverage albeit in different ways.

"All Risk" policy example #1

The following example is taken from the Declarations section of a policy that expressly indicates that it is an "ALL RISK" policy at the outset:

> E. INSURANCE PROVIDED:
>
> This Policy covers property, as described in this Policy, against ALL RISKS OF PHYSICAL LOSS OR DAMAGE, except as hereinafter excluded, while located as follows:

(Emphasis added).

This policy example clearly indicates on its face in the grant of coverage that it is an "All Risk" policy. But others aren't so obvious.

"All Risk" policy example #2

This next example requires the reader to look at two sections of the policy to determine that the policy is written on an "All Risk" basis:

> SECTION IV – TIME ELEMENT LOSS INSURED
>
> The Company will pay for the actual Time Element loss the Insured sustains, as provided in the
>
> Time Element Coverages, during the Period of Liability. The Time Element loss must result from the necessary Suspension of the Insured's business activities at an Insured Location. The Suspension must be due to direct physical loss of or damage to Property (of the type insurable under this Policy other than Finished Stock) caused by a *Covered Cause of Loss* at the Location, or as provided in Off Premises Storage for Property Under Construction Coverages.

(Emphasis added).

At first blush, one might think that this would be a "Stated Peril" policy because it requires that there be a "Covered Cause of Loss" in order to trigger coverage. However, this policy further defined a "Covered Cause of Loss" as follows: "Covered Cause of Loss – All risks of direct physical loss of or damage from any cause unless excluded." (Emphasis added).

Based on this definition, the Policy provides coverage on an "All Risk" basis since a "Covered Cause of Loss" is in fact defined as "All Risks…unless excluded." In essence, a "Covered Cause of Loss" under this policy is the equivalent of a Non-Excluded Peril.

"All Risk" policy example #3

In this third example, the policy provides "All-Risk" coverage through four sections of the policy. First, the insuring agreement of the policy coverage form states the following:

> A. Coverage
>
> We will pay for the actual loss of Business Income you sustain due to the necessary "suspension" of your "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*.

(Emphasis added).

Second, in the definitions section the policy defines a "Covered Cause of Loss" as follows:

> *3. Covered Causes of Loss, Exclusions And Limitations*
>
> *See applicable Causes Of Loss form as shown in the Declarations*.

(Emphasis added).

Third, the Declarations section of this policy indicates the following "Cause of Loss" form is made part of the Policy: "CAUSES OF LOSS – ENHANCED FORM."

Fourth, turning to the "CAUSES OF LOSS – ENHANCED FORM" that is part of the policy provides the following:

> A. Covered Causes Of Loss
>
> When Enhanced is shown in the Declarations, Covered Causes of Loss means direct physical loss unless the loss is excluded or limited in this policy.

(Policy Form MS52021212, p. 1 of 13.)

Connecting the dots between these four provisions, the policy provides "All-Risk" coverage in that it covers all "direct physical loss" unless "excluded or limited."

Under each of these "All Risk" policy examples, every peril conceivable is covered unless it is specifically excluded.

California rules of construction

California law requires that grants of coverage be interpreted *broadly* to afford the greatest possible protection to the insured, while exclusions are interpreted *narrowly* and against the insurer. (See *Shade Foods, Inc., v. Innovative Products Sales* (2000) 78 Cal.App.4th 847, 867; *Reserve Ins. Co. v. Pisciotta* (1982) 30 Cal.3d 800, 808.)

Also, if a policy provision is capable of two or more reasonable interpretations, then it is considered *ambiguous*. (*Stamm Theatres, Inc., v. Hartford Casualty Ins. Co*. (2001) 93 Cal.App.4th 531). Ambiguities must be resolved against an insurance company and *in favor of the insured.* (*Reserve Ins. Co. v. Pisciotta* (1982) 30 Cal.3d 800, 807-808).

Finally, the *burden of proof* to establish that a loss is excluded from coverage rests with the insurer under well-settled California law:

> First- and third-party coverage is today typically provided in a single policy, and under both types of coverage, once the insured shows that an event falls within the scope of basic coverage under the policy, the *burden is on the insurer* to prove a claim is *specifically excluded*. [Citations.] Moreover, exclusionary clauses are interpreted narrowly, whereas clauses identifying coverage are interpreted broadly. [Citations.]

(Emphasis added.) (*See Garvey v. State Farm*, 48 Cal.3d at 406, *citing Clemmer v. Hartford Ins.* (1978) 22 Cal.3d 865, 880; *Reserve Ins. Co. v. Pisciotta* (1982) 30 Cal.3d 800, 808.)

In the case of an "All Risk" policy, the starting premise is that every potential cause of loss is covered, and the burden of proving that any exclusion applies will rest with the carrier.

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The virus exclusion

One of the key reasons insurance companies are denying these business interruption claims is relying upon a virus exclusion in the policy. While not every policy contains a virus exclusion, for those that do, the exclusion can present itself in different ways.

The ISO Virus Exclusion

The most common form of virus exclusion is the ISO Virus Exclusion, which provides the following in relevant part: "We will not pay for loss or damage *caused by or resulting from any virus*, bacterium or other micro-organism that includes or is capable of inducing physical distress, illness or disease." (ISO Virus Exclusion) (Emphasis added).

While the scope of ISO Virus Exclusion excludes loss or damage "caused by or resulting from any virus,…" other non-ISO virus exclusions are more narrow.

Contamination exclusion due to the "actual or suspected" presence of virus

The following is taken from a policy that did not contain the ISO Virus Exclusion but did contain an exclusion for "Contamination":

> This Policy excludes:
>
> *Contamination*, and any cost due to contamination including the inability to use or occupy property or any cost of making property safe or suitable for use or occupancy. If contamination due only to the actual not suspected presence of contaminant(s) directly results from other physical damage not excluded by this Policy, then only physical damage caused by such contamination may be insured. This exclusion does not apply to radioactive contamination which is excluded elsewhere in this Policy.

This particular policy defined *"contaminant"* as "anything that causes "*contamination*."

The policy then defined "*contamination*" as:

> *any condition of property due to the actual or suspected presence of* any foreign substance, impurity, pollutant, hazardous material, poison, toxin, pathogen or pathogenic organism, bacteria, *virus*, disease causing or illness causing agent, fungus, mold or mildew.

(Emphasis added).

Under this policy, the "contamination" exclusion would trigger if there is the *"actual or suspected presence of… any "virus."* Notably, unlike the ISO Virus exclusion which excludes loss or damage "*caused by or resulting from… any virus,"* this "Contamination" exclusion tethers the *"actual or suspected presence of… any virus" to a "condition of property."* Thus, under this "Contamination" exclusion, it would be the carrier's burden to establish that the covered property had the *"actual or suspected presence of…any virus."*

Contamination exclusion due to the "actual" presence of virus

The following is another policy example containing a "Contamination" exclusion that provides:

> This Policy excludes the following unless it results from direct physical loss or damage not excluded by this Policy.
>
> Contamination, and any cost due to Contamination including the inability to use or occupy
>
> property or any cost of making property safe or suitable for use or occupancy, except as provided by the Radioactive Contamination Coverage of this Policy.

(Emphasis added).

This policy then defines "Contamination" as follows:

> *Contamination (Contaminated) – Any condition of property due to the actual presence of* any foreign substance, impurity, pollutant, hazardous material, poison, toxin, pathogen or pathogenic organism, bacteria, *virus*, disease causing or illness causing agent, Fungus, mold or mildew.

(Emphasis added)

This particular "Contamination" exclusion requires the "actual presence of …any virus" on property, and not the "actual *or suspected* presence of… any "virus." Again, it will be the carrier's burden to prove that the exclusion applies. But the burden would be enhanced under this provision to establish the "actual presence" instead of just the "actual or suspected presence" of a virus.

These are three examples of how a virus exclusion can present itself in a policy. *But, the mere presence of a virus exclusion does not end the coverage inquiry.*

The carrier must first meet its burden of proof to establish that the virus exclusion applies in the first instance. This may prove to be a difficult hurdle for carriers that have either form of the "Contamination" exclusion set forth above. Even if the carrier is able to establish that a virus exclusion applies, such exclusion must then be compared with other non-excluded perils that may have contributed to causing the insured's loss.

Non-excluded government actions or orders

Many insured businesses, such as restaurants and gyms, that have been deemed "non-essential" have been shut down because of governmental orders. Thus, it is important to evaluate each policy to determine if the types of governmental orders that are at issue are non-excluded perils.

As stated at the outset, most of these policies provide "All-Risk" coverage so that all non-excluded perils are covered. A common exclusion in many "All Risk" policies is for "Government Action." But the scope of the "Government Action" exclusion is usually limited to governmental actions regarding the "seizure or destruction of property." Specifically, take the following "Government Action" exclusion from one policy:

> We will not pay for loss or damage caused directly or indirectly by any of the following:
>
> c. Government Action
>
> Seizure or destruction of property by order of government authority.
>
> But we will pay for loss or damage caused by or resulting from acts of destruction ordered by governmental authority and taken at the time of a fire to prevent its spread, if the fire would be covered under this Coverage Part.

(Emphasis added).

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Thus, this policy recognizes a "Government Action" as a "cause" of loss or damage, but limits the scope of the exclusion to government actions resulting in a "seizure or destruction of property." Accordingly, since this is an "All-Risk" policy, other types of "Government Actions," such as the various governmental orders that closed non-essential businesses are not excluded from coverage.

The following is another example of an exclusion taken from an "All Risk" policy that excluded an "order of governmental or public authority," but also limited its application:

> This Policy *excludes direct physical loss or damage directly or indirectly caused by or resulting from any of the following* regardless of any other cause or event, whether or not insured under this Policy, contributing concurrently or in any other sequence to the loss:
>
> War, invasion, act of foreign enemy, hostilities or warlike operations (whether war be declared or not), civil war, rebellion, revolution, insurrection, civil commotion assuming the proportions of or amounting to an uprising, military or usurped power, nationalization, confiscation, requisition, *seizure or destruction by the government or any public authority*, including action in hindering, combating or defending against any of these. However, destruction by *order of governmental or public authority* to prevent spread of fire is covered.

(Emphasis added.)

This policy excludes an "order of governmental or public authority" resulting in the "seizure or destruction" of property. It goes on to make an exception to that exclusion in cases where the "seizure or destruction…order of governmental or public authority" was to prevent the spread of a fire.

But, the important takeaway is that this policy recognizes an "order of governmental or public authority" as a potential "cause" of loss or damage. Notably, since this was an "All-Risk" policy, and the policy only identified "orders of governmental or public authority" that result in "seizure or destruction" of property as excluded perils, it means that all other types of "orders of governmental or public authority" are non-excluded perils. Again, this would include the various governmental orders that forced non-essential businesses to close their doors.

When evaluating these policies, it is imperative to look to the limited scope of the exclusions for government actions or orders. The focus is not what the exclusion takes away, but rather, what it leaves behind and doesn't take away. The above policy examples demonstrate how the limited scope of the exclusion actually establishes government actions or orders as non-excluded perils in the analysis.

Concurrent-causation analysis

Assuming that the carrier can meet its burden of proving that a "virus" exclusion applies, and further assuming that a non-excluded peril of a "government action or order" is at play, the next step is to conduct a concurrent cause analysis.

A first-party concurrent-cause analysis comes into play where a non-excluded peril and an excluded peril combine to cause a loss. In such cases, so long as the non-excluded peril is the "Efficient Proximate Cause," there is coverage for the loss. This is so even though an excluded peril concurrently contributed to producing the loss. The "Efficient Proximate Cause" is also referred to as the "Predominate Cause."

We know that the order of events was that the COVID-19 virus came into existence, became a pandemic, which resulted in the various government orders adversely affecting non-essential businesses. In a concurrent-cause analysis, one can anticipate that the carrier will argue that the virus was the "Predominant Cause" since it is what "triggered" the government orders.

But, given the California Supreme Court language from *Sabella v. Wisler* (1963) 59 Cal.2d 21, 31-32., and then later its further clarification in *Garvey v. State Farm* (1989) 48 Cal.3d 395, the "Predominant Cause" is not automatically the "triggering" cause:

> [I]n determining whether a loss is within an exception in a policy, where there is a concurrence of different causes, *the efficient cause – the one that sets others in motion – is the cause to which the loss is to be attributed*, though other causes may follow it, and operate more immediately in producing the disaster." (*Sabella v. Wisler* (1963) 59 Cal.2d 21, 31-32. (Emphasis added).)
>
> "*Sabella* . . . sets forth a workable rule of coverage that provides a fair result within the reasonable expectations of both the insured and the insurer whenever there exists a causal or dependent relationship between covered and excluded perils." *Garvey v. State Farm* (1989) 48 Cal.3d 395 (*Id*. at 404.)
>
> . . .
>
> We use the term *'efficient proximate cause'* (meaning *predominant cause*) when referring to the *Sabella* analysis because we believe the phrase *'moving cause' can be misconstrued to deny coverage erroneously, particularly when it is understood literally to mean the 'triggering' cause*.

(*Id*. at 403.) (Emphasis added).

In a concurrent-causation analysis between an excluded peril of "virus" on the one hand, and a non-excluded peril of a "government action or order" on the other hand, it can be credibly argued that the government orders were the predominant cause of loss. This is because the government orders are what directly caused the shutdown of non-essential businesses. Before the government orders were issued, even though the virus existed in California and other parts of the world, these businesses were still allowed to keep their doors open and conduct business in a normal fashion. However, once the government orders were issued, the businesses were forced to temporarily close their doors.

Thus, if a non-excluded peril of a "government action or order" is deemed

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to be the "efficient proximate cause," there can be coverage for the loss. This is so even though the excluded peril of a "virus" may have also been a contributing concurrent cause.

Conclusion

When evaluating these business-interruption claims, it is important to recognize that the mere presence of a virus exclusion is not the end of the inquiry. Rather, it's just the beginning. Critical analysis of whether the carrier can meet its burden of proof to establish the application of the virus exclusion is necessary depending on the language of the policy. Moreover, even if a virus exclusion applies, it must be compared with other non-excluded government actions or orders in a concurrent-causation analysis.

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