

COVID-19 and Business Interruption Insurance: What You Need to Know



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What Is Business Interruption Insurance?

- One coverage most businesses obtain is business interruption insurance, also known as business income insurance. It can help replace any income a business loses if the business can't open for a time after a covered loss.
- The business income insurance may also cover civil authority. This means if the business has to close down because a government agency prevents access to the business, the policy may help replace lost income.

What Is Business Interruption Insurance?

EXAMPLE: A tree falls and makes a large hole in the roof of your office, so nobody can enter your business premises. This forces the business to shut down for a period of restoration. Business interruption insurance coverage may help recover lost income until the insured is able to operate again.

WHAT IS COVERED BY BUSINESS INTERRUPTION INSURANCE?

If a covered loss forces a business to shut down, this interruption insurance may help the business cover operating expenses like:

- Revenue you'd normally make if your business was open.
- Mortgage, rent and lease payments for the space where your business is located.
- Loan payments that you need to make during that time.
- Taxes, whether you pay them monthly or quarterly.
- Payroll for your employees.
- Relocation costs if you have to move to a new or temporary location because of physical damages.

Coverage

- Business Income
 - 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 “loss” 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” must be caused by or result from a Covered Cause of Loss.

Definitions

“Suspension” means:

- The slowdown or cessation of your business activities; or
- That a part or all of the described premises is rendered untenable, if coverage for Business Income including “Rental Value” or “Rental Value” applies.

Definitions continued

- “Operations” means:
 - Your business activities occurring at the described premises; and
 - The tenantability of the described premises, if coverage for Business Income Including “Rental Value” or “Rental Value” applies.

Definitions continued

- “Period of restoration” means the period of time that:
 - Begins:
 - 72 hours after the time of direct physical loss or damage for Business Income Coverage; or
 - Immediately after the time of direct physical loss or damage for Extra Expense Coverage;caused by or resulting from any Covered Cause of Loss at the described premises; and
 - Ends on the earlier of:
 - The date when the property at the described premises should be repaired, rebuilt or replaced with reasonable speed and similar quality; or
 - The date when business is resumed at a new permanent location.
- “Period of restoration” does not include any increased period required due to the enforcement of any ordinance or law that:
- Regulates the construction, use or repair, or requires the tearing down, of any property; or
 - Requires any insured or others to test for, monitor, clean up, remove, contain, treat, detoxify or neutralize, or in any way respond to, or assess the effects of “pollutants”.

The expiration date of this policy will not cut short the “period of restoration”.

Coverage (duplicate)

- Business Income
 - 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 “loss” 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” must be caused by or result from a Covered Cause of Loss.

Coverage continued

- The term “loss” is sometimes defined to mean *physical* loss or damage.
- The requirement of direct physical loss also sometimes appears in the threshold requirement for any coverage requiring that there be a Covered Cause of Loss:

SECTION I – Covered Causes of Loss

- We will pay for direct “loss” to Covered Property at the “premises” caused by or resulting from any Covered Cause of Loss.
- “Covered caused of loss” means “direct ‘loss’ unless the ‘loss’ is excluded or limited in this Coverage Part.”

Coverage continued

- Extra Expense

- a. Extra Expense Coverage is provided at the premises described in the Declarations only if the Declarations show that Business Income Coverage applies at that premises.
- b. Extra Expense means necessary expenses you incur during the “period of restoration” that you would not have incurred if there had been no direct “loss” to property caused by or resulting from a Covered Cause of Loss.

We will pay Extra Expense (other than the expense to repair or replace property) to:

- 1) Avoid or minimize the “suspension” of business and to continue operations at the described premises or at replacement premises or temporary locations, including relocation expenses and costs to equip and operate the replacement location or temporary location.

Coverage continued

- Summarize: Business income and extra expense coverage applies when there is a suspension of the insured's operations at the insured premises caused by direct physical loss or physical damage to the insured premises and when such physical loss/physical damage was caused by a covered (i.e., not excluded or limited) loss.

Coverage continued

- If the business income loss was not caused by physical loss to the insured premises or the physical loss was not caused by a covered cause of loss, then there may not be coverage for the loss of business income or extra expense.
- Some policies continue with Civil Authority coverage.

Coverage continued

Civil Authority

In this Additional Coverage, Civil Authority, the described premises are premises to which this Coverage Form applies, as shown in the Declarations.

When a Covered Cause of Loss causes damage to property other than property at the described premises, we will pay for the actual loss of Business Income you sustain caused by action of civil authority that prohibits access to the described premises, provided that **both** of the following apply:

Coverage continued

1. Access to the area immediately surrounding the damaged property is prohibited by a civil authority as a result of the damage, and the described premises are within that area but are not more than one mile from the damaged property; and
2. The action of civil authority is taken in response to dangerous physical conditions resulting from the damage or continuation of the Covered Caused of Loss that caused the damage, or the action is taken to enable a civil authority to have unimpeded access to the damaged property.

Coverage summary

- This additional civil authority coverage pertains to the loss of business income caused by an action of civil authority that prohibits access to the insured premises provided the closure is the result of damage to another property that is not more than one mile from the insured premises, the closure is in response to dangerous physical conditions, and the other property suffered damage caused by a covered cause of loss.

COMMERCIAL PROPERTY

CP01 40 07 06

EXCLUSION OF LOSS DUE TO VIRUS OR BACTERIA

This endorsement modifies insurance provided under the following:

COMMERCIAL PROPERTY COVERAGE PART

STANDARD PROPERTY POLICY

- A. The exclusion set forth in Paragraph B. applies to all coverage under all forms and endorsements that compromise this Coverage Part of Policy, including but not limited to forms or endorsements that cover property damage to buildings or personal property and forms or endorsements that cover business income, extra expense or action of civil authority.
- B. We will not pay for loss or damage caused by or resulting from any virus, bacterium or other micro-organism that induces or is capable of inducing physical distress, illness or disease.

However, this exclusion does not apply to loss or damage caused by or resulting from “fungus”, wet rot or dry rot. Such loss or damage is addressed in a separate exclusion in this Coverage Part or Policy.

- C. With respect to any loss or damage subject to the exclusion in Paragraph B., such exclusion supersedes any exclusion relating to “pollutants”.
- D. The following provision in this Coverage part or Policy are hereby amended to remove reference to bacteria: . . .

Virus exclusion summarized

- Insured may not have coverage for any damage or business income loss caused by or resulting from any virus, bacterium or other micro-organism that induces or is capable of inducing physical distress, illness, or disease.

Diesel Barbershop, LLC, et al. v. State Farm Lloyds, No. 5-20-CV-461-DAE, 2020 WL 4724305, (W.D. Tex. Aug. 13, 2020)

- State Farm argued that for business income coverage to apply, the Policies required (1) an accidental direct physical loss to the insured property and (2) that the loss is not excluded.
- SF asserts that Plaintiffs failed to properly plead direct physical loss to the Properties as Plaintiffs argue that the Government Orders are the reason for the **business interruption** claim and fail to show that the Properties have been tangibly “damaged.”
- SF also argued the Virus Exclusion, which was added to Policies in response to SARS pandemic in the early 2000s.

Diesel Barbershop, LLC, et al. v. State Farm Lloyds, No. 5-20-CV-461-DAE, 2020 WL 4724305, (W.D. Tex. Aug. 13, 2020)

- Plaintiffs assert that the language in the Policies does not require a tangible and complete physical loss to the Properties, but rather allows for a partial loss to the Properties, which includes the loss of use of the Properties due to the Orders restricting usage of the Properties.
- Plaintiffs also argue that it is not **COVID-19** within Plaintiffs' Properties that caused the loss directly, but rather that it was the Orders that caused the direct physical loss and thus the Virus Exclusion should not apply.
- Plaintiffs also argue that the Orders were issued to protect public health and welfare, and that Plaintiffs claims thus fall under the Civil Authority provision within the Policies.

Diesel Barbershop, LLC, et al. v. State Farm Lloyds, No. 5-20-CV-461-DAE, 2020 WL 4724305, (W.D. Tex. Aug. 13, 2020)

- The court found that the line of cases requiring tangible injury to property are more persuasive and that the plaintiff's cases are distinguishable . The injury must be by a physical injury.
- Within the Fifth Circuit, the loss needs to have been a “distinct, demonstrable physical alteration of the property.”
- Thus, the Court found that Plaintiffs fail to plead the required direct physical loss.

Diesel Barbershop, LLC, et al. v. State Farm Lloyds, No. 5-20-CV-461-DAE, 2020 WL 4724305, (W.D. Tex. Aug. 13, 2020)

- Even if the Court had found that the language within the Policies was ambiguous and/or that Plaintiffs properly plead direct physical loss to the Properties, the Court found that the Virus Exclusion bars Plaintiffs' claims.
- Plaintiffs allege that the loss of business occurred as a result of the Order that mandated non-essential businesses to discontinue operations for a set period of time to help prevent community spread of COVID-19—triggering the exclusion.

Diesel Barbershop, LLC, et al. v. State Farm Lloyds, No. 5-20-CV-461-DAE, 2020 WL 4724305, (W.D. Tex. Aug. 13, 2020)

- The Court also found that the Civil Authority provision within the Policies was not triggered.
- “Civil authority coverage is intended to apply to situations where access to an insured’s property is prevented or prohibited by an order of civil authority issued as a direct result of physical damage to other premises in the proximity of the insured’s property.”

Diesel Barbershop, LLC, et al. v. State Farm Lloyds, No. 5-20-CV-461-DAE, 2020 WL 4724305, (W.D. Tex. Aug. 13, 2020)

- Plaintiffs' breach of contract, Texas Insurance Code, and breach of duty of good faith and fair dealing claims fail. While there is no doubt that the COVID-19 crisis severely affected Plaintiffs' businesses, State Farm cannot be held liable to pay business interruption insurance on these claims as there was no direct physical loss, and even if there were direct physical loss, the Virus Exclusion applies to bar Plaintiffs' claims. Given the plain language of the insurance contract between the parties, the Court cannot deviate from this finding without in effect re-writing the Policies in question. That this Court may not do.

Vandelay Hospitality Group LP, et al. v. The Cincinnati Ins. Co. et al., No. 3-20-CV-1348-D, 2020 WL 5946863, (N.D. Tex., Oct. 7, 2020)

- Cincinnati Insurance Company moved under Fed. R. Civ. P. 12(b)(6) to dismiss the lawsuit by Plaintiff Vandelay Hospitality Group to recover under an “all risk” commercial property insurance policy for losses to three of its restaurants caused by the COVID-19 pandemic.
- In its “narrow decision,” the court granted the motion but allows Vandelay to replead.

Vandelay Hospitality Group LP, et al. v. The Cincinnati Ins. Co. et al., No. 3-20-CV-1348-D, 2020 WL 5946863,
(N.D. Tex. Oct. 7, 2020)

- Vandelay has failed to plead a plausible breach of contract claim in its state-court first amended petition.
- Vandelay acknowledges in its response to the motion to dismiss that it must plausibly plead a direct physical loss or damage to recover for breach of contract.
- The state court petition's allegations are factually conclusory and/or legal conclusions and are therefore inadequate to plead a plausible claim for breach of contract.
- Without suggesting a view on whether Vandelay can plead a plausible breach of contract claim if allowed to amend, the court granted Cincinnati's motion to dismiss the breach of contract claim asserted in Vandelay's amended petition.
- Cincinnati policy did not have a virus exclusion.

Turek Enters. v. State Farm Mut. Auto. Ins. Co.,
No. 20-CV-11655, 2020 WL 5258484, (E.D. Mich.
Sept. 3, 2020)

- The plaintiff chiropractor sought coverage for loss of income due to government orders that restricted plaintiff's ordinary use of its property. The court dismissed the action with prejudice, holding that the plaintiff had failed to demonstrate tangible damage to covered property, as "plainly" required by the policy term "direct physical loss."

10E, LLC v. Travelers Indem. Co. of Connecticut,
No. 2-20-cv-04418, 2020 WL 5359653, (C.D. Cal.
Sept. 2, 2020)

- The plaintiff sought coverage for income lost as a result of government shutdown orders that prevented the ordinary and intended use of a property. The court dismissed the action, holding that the plaintiffs “cannot recover by attempting to artfully plead impairment to economically valuable use of property as physical loss or damage,” and noting that impaired use or value cannot substitute for physical loss or damage.

North State Deli, LLC v. The Cincinnati Ins. Co.,
No. 20-cv-02569, (C.N.C. Super. Ct. Oct. 9, 2020)

- Applying these definitions reveals that the ordinary meaning of the phrase “direct physical loss” includes the inability to utilize or possess something in the real, material, or bodily world, resulting from a given cause without the intervention of other conditions. In the context of the Policies, therefore, “direct physical loss” describes the scenario where businessowners and their employees, customers, vendors, suppliers, and others lose the full range of rights and advantages of using or accessing their business property. This is precisely the loss caused by the Government Order. Plaintiffs were expressly forbidden by government decree from accessing and putting their property to use for the income-generating purposes for which the property was insured. These decrees resulted in the immediate loss of use and access without any intervening conditions. In ordinary terms, this loss is unambiguously a “direct physical loss,” and the Policies afford coverage.

Questions

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