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Courts Should Heed Contract Law In COVID-19 Physical Loss

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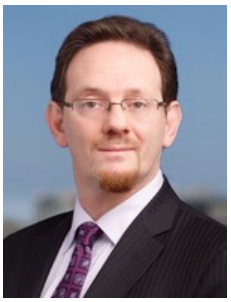

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A recent Law360 guest article, "Courts Should Defer To Science on COVID-19 Physical Loss," urges adoption of the particle theory of coverage.

This theory, policyholders argue, guides courts to conclude that virus particles landing within an insured premises constitute a direct physical loss of or damage to property because protein molecules of a virus undergo molecular changes when interacting with a surface, thereby microscopically altering the property and triggering commercial coverage for the lost or damaged property where the virus landed.

This particle theory of coverage misconstrues the contractual insurance requirements and the science itself.

There are at least four flaws that strip this theory of credibility: (1) business owners' concerns over "the carboxyl amino groups, COOH and NH2," interacting with surfaces is not the reason any business suspended operations; (2) insurance contract law requires a "perceptible and tangible" alteration of property, not a microscopic molecular change; (3) the ubiquitous nature of viruses in all communities renders the particle theory of coverage impossibly impractical; and (4) the interaction of spike proteins on a surface do not in fact alter the structure of the property.

The particle theory is not what caused policyholders to suspend operations.

Business income coverage under commercial property policies is generally triggered only when the suspension of business operations is caused by direct physical loss of or damage to property at the described premises.

This causation prerequisite requires the policyholder to present the insurer with the facts, pictures and damaged property that forced the business to suspend operations.

The contractual causation requirement provides the first barometer for the credibility of the claim and also provides a collaborative roadmap as to what property the insurer is being asked to repair or replace in order to get the policyholder's business up and running.

However, the particle theory of coverage ignores and intentionally obscures this contractual causation requirement by replacing the true undisputed cause of suspended operations with a meandering scientific exploration of hydrogen bonding, which has nothing to do with either why businesses shut down or why they were eventually able to reopen.

It is beyond dispute that the reason businesses across the globe suspended operations is because they were required to do so by government health orders, and that they then reopened when permitted to do so by government health orders.

Based on our analysis, over 200 court decisions across the country have agreed that business restrictions instituted to protect public health do not constitute direct or physical property loss or damage covered by commercial property insurance.[1]

Nevertheless, the particle theory asks courts to abandon judicial robes in favor of lab coats to ignore the factual cause of suspended operations and instead answer the contractually irrelevant question posed by the previous article: "What does the [virus] actually do to insured property?"

This is simply not the question on which coverage depends.

The question for coverage purposes is whether the insured possessed factual knowledge of direct and physical loss of or damage to its property that was so pervasive that it forced suspended operations.

Not only does the particle theory of coverage seek to circumvent the contractual inquiry of what facts the insured knew that were the alleged cause of suspending operations, but it misconstrues the legal test for direct physical loss of property that has been agreed upon by the vast majority of courts, as discussed below.

A "direct physical loss" of property must be "tangible" and "perceptible."

The particle theory argues that, a year or more after a policyholder suspended operations, legal experts in an insurance lawsuit should be permitted to convince a court that the molecular interaction of virus molecules on retroactively identified surfaces in the insured premises caused the structural alteration of the property that forced the suspended operations.

This theory fails to recognize the broader context and intent of commercial property insuring language as it has been interpreted across the country.

For example, as explained by the U.S. District Court for the Northern District of Illinois on June 11 in its Image Dental LLC v. Citizens Insurance Co. of America decision, policies generally require that the type of loss or damage necessary to trigger a commercial property policy is that which needs repair, rebuilding or replacement.[2]

The U.S. District Court for the District of Kansas further observed in its Dec. 3, 2020, Promotional Headwear International v. The Cincinnati Insurance Co. decision that the overwhelming majority of courts that have analyzed the context of this language within commercial property forms have determined that the type of direct physical loss of property required to trigger coverage is that which is perceptible and tangible.[3]

Applying the concepts of perceptible and tangible loss of property, commercial insurance responds when a window is cracked, or when property is infused with the odor of cat urine, or when a wall is precariously damaged.

It makes sense that commercial property coverage turns on the perceptible and tangible change to physical conditions in a premises that both the insured and the policyholder are capable of identifying, appraising and working together to fix.

The coverage can respond to the replacement of a broken floor and the elimination of the smell of gasoline or urine, but not to the subatomic formation of hydrogen bonds on molecules that was neither tangible nor perceptible, nor even the cause of suspended operations.

Microscopic molecular interactions on the surface of an object are simply impossible for the insured or insurer to investigate, preserve, appraise, repair or replace in conformity with the intent and function of the insurance policy.

The particle theory of coverage is impossibly impractical given the omnipresence of viruses.

Insurance policies are meant to be interpreted to avoid absurd results, and interpreted to consistently reflect the policy's logical intent and function.

Quoting the U.S. Court of Appeals for the Fourth Circuit's 1998 decision in United Capitol Insurance Co. v. Kapiloff, the U.S. District Court for the District of Maryland explained in its April 14 decision in Bel Air Auto Auction Inc. v. Great Northern Insurance Co. that policies are interpreted "as a whole, according words their usual, everyday sense, giving force to the intent of the parties, preventing absurd results, and effectuating clear language."[4]

The application of the particle theory to trigger commercial property coverage would lead to untenable and absurd results.

For example, the rhinovirus[5] has long been recognized as a source of the common cold and is present in every community, every day. Influenza viruses are so common as to give rise to what is known every year as flu season.[6] The norovirus is notorious for being highly contagious, causing those infected to shed billions of contagious norovirus particles.[7]

It is of course absurd and contrary to common sense to conclude that every business, everywhere in the world, suffers a potential direct and physical loss of property every day as viruses circulate through the community, or even as a person with a virus visits an insured premises, or virus particles otherwise land on floors, clothes or other objects.

As the Bel Air Auto Auction court noted, "if the presence of COVID-19 were actual 'contamination' ... then every place of business in the State and the country" would have a claim for contamination, "including hospitals, grocery stores and other businesses where people continue to flock during the pandemic."[8]

Virus particles do not change the physical structure of property.

The particle theory of coverage confuses the scientific notions of adsorption and absorption. While virus particles that land on a surface may undergo a molecular interaction with the surface, this does not mean that the structure of the surface is altered.

For example, the chemical process of adsorption can indeed take place when molecules from a virus adhere to a surface. This process creates a film of the adsorbate on whatever surface to which it adheres.

Adsorption is a surface phenomenon in which the molecules are loosely held on the surface and can be easily removed.[9] As is widely known, SARS-Cov-2 virus particles can be easily wiped clean from any surface.

Adsorption should not be confused with the chemical process of absorption.

In absorption, atoms actually pass through and enter from one material into another — _changing both materials. Absorption is what happens when you soak up a spill with a paper towel, but not what happens when a virus molecule lands on a surface.

Conclusion

Courts faced with business income claims arising from the COVID-19 pandemic are tasked with examining the facts that caused the policyholder to suspend operations, and reaching the legal conclusion as to whether those facts satisfy the contractual prerequisites to coverage.

As hundreds of courts have concluded, such prerequisites are typically not satisfied because the suspended operations were caused by government health instructions, and not by any direct or physical loss of or damage to property within any insured premises.

To accept the particle theory of coverage espoused in "Courts Should Defer To Science on COVID-19 Physical Loss" is to ignore the intent, function and language of the policy forms.

This would impermissibly create what the U.S. District Court for the Central District of California termed "a sweeping expansion of insurance coverage without any manageable bounds" in its Sept. 10, 2020, decision in Plan Check Downtown III LLC v. AmGuard Insurance Co.[10]

The science behind a pandemic is important for society to respect, understand and investigate, but it is not what determines coverage for commercial property claims.

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Disclosure: BatesCarey has submitted an amicus in support of Cincinnati Insurance Co., a party mentioned in this article, in the case of Neuro-Communication Services Inc. v. Cincinnati Insurance Co. pending before the Ohio Supreme Court.

[1] Oral Surgeons, P.C. v. Cincinnati Ins. Co., 2 F.4th 1141 (8th Cir. 2021) (rejecting insured's argument that "lost business income and the extra expense it sustained as a result of the suspension of non-emergency procedures were 'caused by direct 'loss' to property.'"); Social Life Magazine, Inc. v. Sentinel Ins. Co., Ltd., 1:20-cv-03311-VEC, 2020 WL 2904834 (S.D.N.Y. May 14, 2020) ("what has caused the damage is that the governor has said you need to stay home. It is not that there is any

particular damage to your specific property."); Image Dental, LLC v. Citizens Ins. Co. of Am., No. 20-cv-02759, 2021 WL 2399988, at *4 (N.D. Ill. June 11, 2021) (no coverage where suspension of operations was not caused by "harm [to] the buildings or anything inside them" but by pandemic-related government closure orders).

[2] Image Dental at *6.

[3] Promotional Headwear Int'l v. Cincinnati Ins. Co., No. 20-cv-2211, 2020 WL 7078735 at *6 (D. Kan. Dec. 3, 2020) ("[T]he overwhelming majority of cases to consider business income cases stemming from COVID-19 with similar policy language hold that 'direct physical loss or damage' to property requires some showing of actual or tangible harm to or intrusion on the property it"); Equity Planning Corporation v. Westfield Ins. Co., No. 1:20-CV-01204, 2021 WL 766802 at *9 (N.D. Ohio Feb. 26, 2021) ("direct physical loss of or damage to" means "an immediate material, perceptible harm that leads either to complete destruction or deprivation or partial destruction); Demoura v. Continental Cas. Co., No. 20-CV-2912 (E.D. N.Y. March 5, 2021)("it is clear that 'direct physical loss or damage to property' requires actual, tangible harm to the property."); Paradigm Care & Enrichment Ctr., LLC v. W. Bend Mut. Ins. Co., No. 20-CV-720-JPS-JPS, 2021 WL 1169565, at *7 (E.D. Wis. Mar. 26, 2021)("direct physical loss of or damage to" property requires "a direct material, tangible, corporeal, or perceptible, loss of or damage to [the] covered premises.").

[4] Bel Air Auto Auction, Inc. v. Great N. Ins. Co., No. CV RDB-20-2892, 2021 WL 1400891, at *6 (D. Md. Apr. 14, 2021).

[5] Centers for Disease Control and Prevention, Common Colds: Protect Yourself and Others, https://www.cdc.gov/features/rhinoviruses (accessed Feb. 12, 2021).

[6] Centers for Disease Control and Prevention, The Flu Season, https://www.cdc.gov/flu/about/season/flu-season.htm (accessed Feb. 12, 2021).

[7] Centers for Disease Control and Prevention, About Norovirus, https://www.cdc.gov/norovirus/about/index.html (accessed Feb. 12, 2021).

[8] Bel Air Auto Auction at *10.

[9] Difference Between Absorption And Adsorption in Tabular Form (toppr.com) (Accessed July 27, 2021).

[10] Plan Check Downtown III, LLC v. AmGuard Ins. Co., 485 F. Supp. 3d 1225, 1231 (C.D. Cal. 2020); Mark's Engine Co. No. 28 Restaurant, LLC v. Travelers Indemn. Co. of Connecticut, C.D. Cal. No. 2:20-cv-04423, 492 F.Supp.3d 1051, 2020 WL 5938689, at *4 (Oct. 2, 2020) (any interpretation "that 'direct physical loss of' encompasses deprivation of property without physical change in the condition of the property . . . would be an interpretation without any 'manageable bounds.'").