

COVID-19 AND BUSINESS INTERRUPTION COVERAGE

On March 23, 2020, Governor Whitmer issued [Executive Order No. 2020-21](#), which resulted in the forced shutdown of many businesses across the State of Michigan through April 13, 2020. Similar shutdowns are occurring in other states and around the world, resulting in substantial financial losses to affected businesses.

As a result, businesses are looking at their existing insurance policies to determine whether those policies include business interruption coverage that might help to minimize the financial consequences of these shutdowns. Unless those policies contain specific provisions for non-physical damage coverage or the law develops to say that cleaning a virus from property that is not physically damaged is, in fact, covered damage to property, businesses are unlikely to find relief.

Below is a brief overview of the law pertaining to business interruption coverage, along with the recommended course of action for those who have questions regarding potential business interruption coverage or claims.

Availability of Business Interruption Coverage (Generally)

Businesses obtain business interruption coverage as part of their commercial property insurance policies. Business interruption coverage is intended to compensate the insured for the income it lost during the period of restoration or the time necessary to repair or restore the physical damage to the covered property. Some insureds also have extended business interruption, and other extensions to this coverage, as further explained below.

Broadly, business interruption losses may be covered under three sections of a typical commercial property policy.

1. If there is physical property damage to the insured property that interrupts the insured's business operations;
2. Under the contingent business interruption extension found in some policies; or
3. Under the civil or military authority provision.

Generally, all three require "direct physical loss or damage" to covered property or to nearby property to trigger coverage, and the physical loss must have been caused by a cause of loss that is otherwise covered under the policy. However, as with any coverage question, the language of the policy is determinative.

Physical Property Damage

Physical property damage coverage is limited to losses that result from the direct physical loss of or damage to the covered property. Courts are split as to what constitutes physical loss or damage.

Some courts, including the Eastern District of Michigan, require tangible changes that result in material damage to property. See *Universal Image Productions, Inc v Chubb Corp*, 703 F Supp 2d 705 (ED Mich 2010), aff'd 475 Fed Appx

569 (6th Cir 2012) (insured claiming that water seepage caused a pervasive odor, mold, and bacterial contamination did not suffer a “direct physical loss” because there was no structural or any other tangible damage to the property, and the odor was not so pervasive as to render the premises uninhabitable). *See also Mastellone v Lightning Rod Mut Ins Co*, 175 Ohio App 3d 23 (Oh Ct App 2008) (mold staining was not physical injury because it was temporary and could be cleaned by using a chemical solution); *Columbiaknit, Inc v Affiliated FM Ins Co*, 1999 WL 619100 (D Or 1999) (“The mere adherence of molecules to porous surfaces, without more, does not equate to physical loss or damage”). Courts taking this approach would be unlikely to find that COVID-19 contamination also constitutes physical property damage.

Other courts take a more liberal approach and find physical damage if there is a demonstrable alteration of the property, even if the alteration cannot be seen or touched. *See Mellin v Northern Security Ins Co*, 167 NE 544 (NH 2015) (cat urine odor emanating from a neighboring condominium constituted physical loss); *Gregory Packing, Inc v Travelers Property Cas, Co*, 2014 WL 6675934 (D NJ 2014) (accidental release of ammonia into facility constituted physical damage, even though there was no structural alteration of the property). Courts taking this approach would be more likely to find that COVID-19 contamination constitutes physical damage.

We are critically examining whether the kind of disease-caused loss of use as created by the COVID-19 outbreak can be analogized to cases of this type and other similar losses, like environmental contamination, to demonstrate that the property is no longer fit for its purpose.

Extended Business Interruption

Some insureds also have extended business interruption coverage as an extension to business interruption coverage. This coverage, included for additional premium, is typically limited by a set period of time to compensate the insured for income it lost during the period after the property is repaired or restored but before the insured’s income reaches what it was before the covered loss took place. Typically the same triggers, limitations discussed also apply whether extended business interruption is covered.

Contingent Business Interruption

Contingent business interruption coverage applies when damage occurs to property owned by the insured’s primary supplier, partner, or customer and affects the insured’s ability to do business. These policies typically require direct physical damage to property owned by the supplier, partner, or customer, and that damage must have been caused by a covered peril. As with extended business interruption coverage, this is generally an extended coverage purchased by an insured for an additional premium.

Civil Authority

Civil authority coverage applies when an insured is unable to access its property as the result of a government order. However, a government order that interferes with an insured’s ability to operate does not automatically trigger civil authority coverage; an insured must otherwise satisfy all of the terms of its policy. Moreover, as a general rule, civil authority coverage is contingent upon physical damage to adjacent or nearby property, not fear of damage or contagion. *See United Air Lines, Inc v Ins Co of State of PA*, 439 F 3d 128 (2d Cir 2006) (United not entitled to coverage for economic losses resulting from government closure of Reagan National Airport in connection with 9/11 attacks because the shutdown was a preventive measure based on the fear of a future attack, not the “direct result of damage” to the adjacent property, as required by the policy); *Dicki Brennan & Co v Lexington Insurance Co*, 636 F 3d 683 (5th Cir 2011) (insureds could not recover for business losses resulting from an evacuation order issued in anticipation of Hurricane Gustav because insured “failed to demonstrate a nexus between any prior property damage and the evacuation order.”).

However, the Michigan Court of Appeals has held that, depending on the language of the policy, an insured may have civil authority coverage absent property damage. See *Sloan v Phoenix of Hartford Ins Co*, 46 Mich App 46 (1973) (movie theater owners could recover for losses resulting from their compliance with the governor’s executive order imposing a curfew and closing all places of amusement because policy clauses contemplated separate and distinguishable business interruption losses, one addressing business losses caused by damage to property, and the other addressing business losses occasioned by the denial of access to the premises by order of civil authority); *Allen Park Theatre Co, Inc v Michigan Millers Mut Ins Co*, 48 Mich App 199 (1973) (holding no physical damage was necessary; “[i]f the insurer wanted to be sure that the payment of business interruption benefits had to be accompanied by physical damage it was its burden to say so unequivocally”); *Southlanes Bowl, Inc v Lumbermen’s Mut Ins Co*, 46 Mich App 758 (1973) (accord).¹

Exclusions and Limitations on Coverage

Even if an insured can establish physical property damage, contingent business interruption, or civil authority coverage, policies often include several exclusions and limitations on coverage. These exclusions and limitations are varied, but the exclusion at the forefront of the COVID-19 issues will certainly be one that excludes damage resulting from biological agents, disease, virus, or bacteria.

Most commercial property policies exclude “loss due to virus or bacteria.” More specifically, this exclusion usually states that the insurer “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.” Businesses with property policies that include this exclusion are not likely to have their COVID-19 related business interruption losses covered.

Less often, some commercial property policies contain a very specific coverage extension for losses caused by communicable or infectious diseases, which could arguably encompass COVID-19. This specialty coverage is most often going to be found in policies obtained by clients in health care but may also be in some policies for hospitality industry clients. Hence, a careful review of the language is imperative. This is particularly true because this coverage usually requires that there actually be the presence of the “communicable disease” at the insured premises, not suspected based on other events in the world. This coverage is also usually tied to whether there is a government order restricting use of the insured’s property; therefore, the facts of the claim are as critical as the policy language. As with most extensions of coverage, if this is available, it is likely covered as a sub-limit, typically an amount significantly less than the overall policy limits for property loss.

What You Should Do

Send Jaffe the Policy and All Pertinent Facts

The policy language is critical. While articles that provide a general analysis are informative, the specific policy language at issue and the facts will ultimately determine whether coverage is triggered by COVID-19 and its impacts.

Begin Documenting Losses to Make a Claim for Coverage

As the impact of COVID-19 continues to grow, it is important for businesses to fully understand the property coverage they have — or potentially have — so they can start documenting their claim by keeping proper records of loss and gathering the necessary information. If appropriate, Jaffe will assist in pursuing coverage.

As explained above, the focus of a business interruption claim is on loss of income during the period of restoration. This loss of income can include revenue, relocation expenses, loan payments, payroll, taxes, and mortgage or lease

¹ It is important to note that, pursuant to MCR 7.215(J)(1), a panel of the Court of Appeals is not bound by any Court of Appeals decision issued prior to November 1, 1990. While Michigan trial courts are bound by these decisions, the present day Michigan Court of Appeals is not and could reach a different conclusion, even if the policy language is favorable.

payments. Every business and industry is different – a manufacturing facility, for example, will have different records, and the basis for its loss will be different from an apartment complex. Once a claim is submitted, the insurer will undoubtedly retain an accountant to request and review records, so considering what kinds of records to maintain now is critical. As a rule of thumb, irrespective of the type of business or industry, the insurer will likely request monthly profit and loss statements, invoices and purchase orders, accounting records, monthly or quarterly production and sales records, inventory records, rental records for equipment, budget forecasts, and historical financial statements for comparable time periods.

What You Should Not Do

Rush to File Suit

While a business may be understandably eager to pursue business interruption coverage, the premature filing of a lawsuit is more likely, and perhaps much more likely, to be disadvantageous than advantageous. Clients must be able to document actual business losses and must follow the appropriate claims process before pursuing a lawsuit.

Other Issues

Similar to other sectors, the insurance industry is facing claims and issues that have not been addressed before. There may be some comparable situations to provide guidance, such as the 2013 SARS Outbreak and the 9/11 terrorist attack, but overall, policy holders in the U.S., and thereby the courts, have not grappled with a pandemic on the scale we are currently seeing with COVID-19.

With that backdrop, there are likely to be many situations which could implicate different lines of coverage, such as claims by employees and individuals bringing third-party liability claims for personal injury, as well as potential claims by investors and dissatisfied shareholders who bring claims under directors and officer coverage for failure to proactively address the COVID-19 risks. Like the business interruption claims, these will be fact and policy specific. So we encourage you to gather as much information as possible for a thorough evaluation of ways we can assist in protecting it. We are here to help.

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