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A Brief Primer On Business Interruption Claims

By Lucy E. Tufts, Cunningham Bounds, LLC

Given the devastating losses that businesses are enduring as a result of the cascading consequences associated with the COVID-19 pandemic, many are turning to their insurance policies to determine whether coverage exists that may alleviate the economic burdens of this catastrophe.

The following article is a general summary of some of the coverages that may be available, some of the policy provisions that may modify that coverage, and some of the exclusions or limitations that may limit the coverage in whole or in part. The purpose of this article is to help a practitioner who may not normally handle what are commonly termed "first-party" insurance claims identify some of the likely issues that will arise in the evaluation of claims of this type.

For lawyers evaluating these claims, the most important (and most obvious) part of their work is to read each provision of the policy and to understand those provisions in relation to one another. Some exclusions and limitations only apply to certain coverages. Some coverages are limited in time and scope while others are not. Some provisions affect the total amount of coverage available, which may be different than what appears on the declarations page. Additionally, strict adherence to the policy terms is absolutely necessary, as there are often substantive

and procedural requirements for filing the notice of claim, proof of loss, and other aspects of the claim. Deadlines should be monitored carefully.

The types of insurance that business clients may have purchased and which may provide coverage include, but are not limited to:

- (1) **Business income** claims related to business interruption;
- (2) **Civil authority** claims related to government orders to slow down or shut down a business;
- (3) **Extended business income** claims related to costs to restore operations;
- (4) **Contingent business income/dependent property** claims associated with losses that occur to the property of another business on which the insured's business depends to supply its products;
- (5) **Extra expense** claims associated with additional costs incurred as a result of the COVID-19 crisis (for example – increased property security, disinfectant efforts, or relocation costs);
- (6) **Ingress/egress** claims associated with losses related to prevention of ingress to or egress from the insured's property (e.g., as the result of a quarantine);
- (7) **Leader property** claims associated with lost earnings resulting from the closure of a property that attracts customers to the policyholder's business (e.g., coverage for hotels near stadiums and arenas; coverage for doctors' groups related to

closure of portions of hospitals for elective surgeries); and/or

(8) **Miscellaneous claims** such as event cancellation coverage, cancellation of bookings coverage, crisis management coverage, or other specific coverage.

While an entire book may be written as to the various interpretations of the standard language for each of these types of coverage, the key provisions in these policies that may modify coverage, and which must be carefully evaluated, include:

(1) **Language describing "physical loss"** – This language may affect the extent to which proof of actual physical damage (as opposed to loss of use) is required to trigger coverage.

a. Variations in policies include:

i. "Physical loss of or damage to property" – most common and arguably ambiguous

A. Because of the inclusion of both "loss of" and "damage to," and because they are in the disjunctive, and because meaning must be given to all words in the policy and harmonized if possible, then it may be argued that the ambiguous phrase "loss of" is reasonably interpreted as "loss of use."

ii. "Physical loss or damage" – most restrictive

iii. “Risk of direct physical loss” – most liberal

b. Although some courts have interpreted “physical loss of or damage to property” to mean a provable tangible alteration to the covered property, the general national trend is to interpret the phrase more liberally and find that a loss of use or utility is covered despite there being no structural damage to the property in question. Courts across the country have found “physical loss” to include loss of use because of odor, asbestos, ammonia, and smoke infiltration, among other things.

(2) Period of restoration – This language limits the amount of time that business income and/or extended business income coverage exists, which usually ends when (a) the property at the described premises should be repaired, rebuilt, or replaced with reasonable speed and similar quality; or (b) the date when business is resumed at a new permanent location.

(3) Definition of “suspension” of operations – This language may determine whether a complete cessation or merely a slowdown is necessary to trigger coverage.

a. Timing may also be an issue – e.g., if the suspension period is defined from the date of the physical loss to the date when that loss is remediated, and there is a suspension of production during that time but the lack of sales lags until much later, the coverage may be limited.

(4) “Directly resulting from” language – This language may be used to require that the business income loss is causally connected to the “physical loss” that triggers coverage.

a. A business interruption that is the result of a general decline in economic activity, lack of workers, a decline in tourism, or a reduction in aggregate demand for services will likely not trigger coverage.

b. A civil authority order that is issued to prevent property damage that has not yet occurred (as opposed to react to property damage that has already occurred) may not qualify for coverage.

(5) Coinsurance provision – This provision reduces business income coverage if the actual loss of income is substantially higher than the estimated income established at the time insurance was purchased.

(6) Covered locations – This language identifies which locations are covered and may include coverage for newly acquired locations or locations not actually owned by the insured.

(7) Other time limitations – Most civil authority coverage begins 72 hours after the governmental order and lasts for 2-4 weeks.

a. Some policies provide coverage until the civil authority order ends.

b. Review the definition of “occurrence” to determine whether consecutive, separate civil authority orders trigger additional coverage.

The key exclusions in these policies that may modify coverage, and which also must be studied carefully to determine their applicability, include:

(1) Exclusion of Loss Due to Virus or Bacteria

a. “We will not pay for loss or damage caused by or resulting from any virus, bacterium or other microorganism that induces or is capable of inducing physical distress, illness or disease.” (ISO Commercial Property Form CP 01 40 07 06)

b. “We will not pay for loss or damage caused by or resulting from any of the following, regardless of any other cause or event, including a peril insured against, that contribute to the loss at the same time or in any other sequence...The actual or suspected presence of any virus, organism or like substance that is capable of inducing disease, illness, physical distress or death, whether infectious or otherwise, including but not limited to any epidemic, pandemic, influenza, plague, SARS, or Avian Flu.”

(2) Microorganism Exclusion (Absolute)

a. “This Policy does not insure any loss, damage, claim, cost, expense or other sum directly or indirectly

arising out of or relating to: mold, mildew, fungus, spores or other microorganism of any type, nature, or description, including but not limited to any substance whose presence poses an actual or potential threat to human health. This Exclusion applies regardless whether there is (i) any physical loss or damage to insured property; (ii) any insured peril or cause, whether or not contributing concurrently or in any sequence; (iii) any loss of use, occupancy, or functionality; or (iv) any action required, including but not limited to repair, replacement, removal, cleanup, abatement, disposal, relocation, or steps taken to address medical or legal concerns.” (LMA 5018)

(3) Anti-Concurrent Causation Exclusions

a. “We do not insure for loss caused directly or indirectly by any of the following...Such loss is excluded regardless of any other cause or event contributing concurrently or in any sequence to the loss.”

b. The purpose of this exclusion is to prevent the theory of concurrent causation from providing coverage for losses never intended to be covered. Various state laws may regulate the scope and legality of this type of exclusion, so be sure to review the law that governs the policy being evaluated.

(4) Fungus, Wet Rot, Dry Rot and Bacteria Exclusion

a. Provides an exclusion for the “[p]resence, growth, proliferation, spread or any activity of ‘fungus,’ wet or dry rot or bacteria.”

b. While this exclusion most likely will not bar coverage, some definitions in this type of exclusion include the word “virus” and may be more difficult to overcome.

(5) Pollution Exclusion

a. “Bodily injury” or ‘property damage’ arising out of the actual, alleged or threatened discharge, dispersal, seepage, migration, release or escape of ‘pollutants.’”

b. “Pollutants” mean any solid, liquid,

gaseous or thermal irritant or contaminant, including smoke, vapor, soot, fumes, acids, alkalis, chemicals and waste. Waste includes materials to be recycled, reconditioned or reclaimed.”

c. There is case law in many states holding that the pollution exclusion only applies to industrial type pollution regulated by federal or state statutes.

(6) “Sick Building” Exclusion

a. “We will not pay for loss or damage caused by or resulting directly or indirectly from any of the following: ... (B) Any loss, damage or expense, or increase in loss, damage or expense caused by or resulting from ventilation, heating, air conditioning, or sick building condition(s). Sick building condition(s) as used herein means a building(s) or structure(s) with actual or alleged conditions which create or may create an environment which is, or is suspected to be, unhealthy in any way to any person or other living thing.” (ICAT SCOL 232 0709)

When evaluating these provisions to determine whether a potential client has a reasonable first-party insurance claim, keep in mind that the rules of construction associated with the interpretation of insurance policies generally favors the insureds. The Alabama Supreme Court has made clear that “when doubt exists as to whether coverage is provided under an insurance policy, the language used by the insurer must be construed for the benefit of the insured.” *St. Paul Mercury Ins. Co. v. Chilton-Shelby Mental Health Ctr.*, 595 So.2d 1375, 1377 (Ala. 1992). More specifically, “[i]f a provision in an insurance policy is found to be genuinely ambiguous, ‘policies of insurance should be construed liberally in respect to persons insured and strictly with respect to the insurer.’” *State Farm Mut. Auto. Ins. Co. v. Brown*, 26 So.3d 1167, 1170 (Ala. 2009) (other citations omitted).

The same general rules of construction also apply to exclusions: “[W]hen ambiguity exists in the language of an exclusion, the exclusion will be construed so as to limit the exclusion to the narrowest application reasonable under the word-

ing.” *St. Paul Mercury Ins. Co.*, 595 So.2d at 1377 (citing *Guaranty National Ins. Co. v. Marshall County Board of Educ.*, 540 So.2d 745 (Ala. 1989)). “However, it is equally well settled that in the absence of statutory provisions to the contrary, insurers have the right to limit their liability by writing policies with narrow coverage. If there is no ambiguity, courts must enforce insurance contracts as written and cannot defeat express provisions in a policy, including exclusions from coverage, by making a new contract for the parties.” *Id.*

Great care should be taken in evaluating whether a particular policy, given the specific factual circumstances and governing law applicable to it, provides coverage. There should be strict adherence to all policy terms, deadlines, and requirements. Every provision of every policy should be carefully read and understood. Only then can an effective determination be made as to whether a lawsuit should be filed to recover the insurance payments that have been denied.



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