

**How Public Policy is Impacting the Insurance Industry's Response to
COVID-19 Business Interruption Claims**
"Balancing the Pressures by Consumers, Courts, Legislators and Regulators"
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Background

As of this writing, the number of people testing positive for Coronavirus continues to increase in many U.S. states. The loss of business income associated with the large-scale disruption of global supply chains, interruptions of business operations, major events being cancelled, construction projects halted, and fallout from government-imposed closure orders also continues to increase. Businesses that have been forced to close by order from state authorities, or whose revenue have slowed to a trickle because of consumer fears and social distancing requirements have turned to their insurers seeking coverage for business interruption.

However, insurance companies, relying on the plain language of their policies, are concluding that most business interruption claims associated with COVID-19 are not covered. With no other options remaining, many businesses are filing suits against carriers and turning to insurance regulators and state and federal legislators for assistance in their fight against the insurance industry.

Under that backdrop, this article will examine how the insurance industry, regulatory agencies and legislative bodies are grappling to find common ground in their collective efforts to deal with the societal impact resulting from largely uninsured business losses of epic proportions.

Why Business Interruption Claims Related to COVID-19 are Being Denied

Business interruption insurance is designed to protect the *prospective earnings* of a business. It is also designed to do for the insured, in the event of a loss, what the business would have done for itself if an interruption in the operation of the business had not occurred. Three separate components must be connected in order to satisfy the requirements of the typical business interruption insuring agreement:

1. A covered cause of loss must cause *direct physical loss* of or damage to the property *at the described premises*;
2. The covered loss must cause a *necessary suspension or interruption of operations*; and;
3. The *business income loss* must be caused by the suspension or interruption.

With respect to the “covered cause of loss” requirement, most commercial property policies are written on “all-risk” forms. An all-risk form covers all perils that are not specifically excluded; however, it does not cover every risk. The "causes of loss" section of an all-risk policy lists the perils that are excluded. After the SARS outbreak in 2003, many business interruption policies were modified to specifically exclude coverage for losses related to virus or bacteria. Accordingly, a number of property policies now contain specific exclusions for property damage and business income losses arising from viral or bacterial related claims. For those carriers that have incorporated the following Insurance Services Office’s (ISO) endorsement into their commercial property policies, there is a valid argument that a business interruption loss relating to COVID-19 is excluded:

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 comprise this Coverage Part or 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 microorganism 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 provisions in this Coverage Part or Policy are hereby amended to remove reference to bacteria:

1. Exclusion of "Fungus", Wet Rot, Dry Rot And Bacteria; and

2. Additional Coverage – Limited Coverage for "Fungus", Wet Rot, Dry Rot And Bacteria, including any endorsement increasing the scope or amount of coverage.

E. The terms of the exclusion in Paragraph B., or the inapplicability of this exclusion to a particular loss, do not serve to create coverage for any loss that would otherwise be excluded under this Coverage Part or Policy (*CP 01 40 07 06 © ISO Properties, Inc., 2006*).

The major area of dispute for those insurers that have not added the above ISO endorsement or something similar to their property policies is based on whether the Coronavirus has caused *direct physical loss or damage to covered property*. Most COVID-19 related claims arguably lack such evidence. Whether property has sustained physical loss or damage is generally a question of fact, and courts are not in complete agreement on this issue. Hence, why suits against insurers, scrutiny by regulators and pressure by legislators is on the rise.

Increased Regulatory Pressure

Many insurers have received notifications from a number of state regulatory agencies demanding that they comply with additional and more stringent claims handling requirements and, in some cases, requiring insurers to submit advisory coverage opinions relating to COVID-19, before a claim is even filed. For example, the New York Department of Financial Services recently issued such a notice to insurers operating in that state:

Given the potential impact of COVID-19 on business losses, particularly concentrated effects in local communities, DFS considers Insurers' obligations to policyholders a heightened priority. In the interest of the timely and equitable fulfillment of insurance contracts, Insurers must explain to policyholders the benefits under their policies and the protections provided in connection with COVID-19. Any Insurer that writes none of the business described herein should notify DFS in a statement signed by an officer or other authorized representative of the Insurer in lieu of complying with the provisions below:

- First, each Insurer should provide to DFS the volume of business interruption coverage, civil authority coverage, contingent business interruption coverage and supply chain coverage the Insurer wrote that has not lapsed as of the date of this letter, which should be expressed in amounts of direct premium, policy types and numbers of policies written of each type.
- Second, each Insurer should examine the policies it has issued and explain the coverage each policy offers in regard to COVID-19 - both presently and as the

situation could develop to change the policyholder's status (i.e., is there any potential for coverage as a result of COVID-19).

- For each policy type, Insurers should prepare such information in a clear and concise explanation of benefits that is suitable for policyholder review. Insurers should then send such explanation to each of their policyholders of the applicable policy types. Insurers should also send copies of all such explanations to DFS, along with a representation that the explanations have been provided to the Insurer's policyholder.
- The explanation to policyholders should include all relevant information, including, without limitation:
 - o What type of commercial property insurance or otherwise related insurance policy does the insured hold?
- Does the insured's policy provide "business interruption" coverage? If so, provide the "covered perils" under such policy. Please also indicate whether the policy contains a requirement for "physical damage or loss" and explain whether contamination related to a pandemic may constitute "physical damage or loss." Please describe what type of damage or loss is sufficient for coverage under the policy.
- Does the insured's policy provide "civil authority" coverage? If so, please describe what type of damage or loss is sufficient for coverage under the policy. Please also describe any relevant limitations under the policy. Please explain whether a civil authority prohibiting or impairing the policyholder's access to its covered property in connection with COVID-19 is sufficient for coverage under the policy.
- Does the insured's policy provide "contingent business interruption" coverage? If so, please describe what type of damage or loss is sufficient for coverage under the policy. Please provide the "covered perils" under such policy. Please also indicate whether the policy contains a requirement for "physical damage or loss" and explain whether contamination related to a pandemic may constitute "physical damage or loss."
- Does the insured's policy provide "supply chain" coverage? If so, is such coverage limited to named products or services from a named supplier or company? Please also indicate whether the policy contains a requirement for "physical damage or loss" and explain whether contamination related to a pandemic may constitute "physical damage or loss."

- For each instance of coverage described above, please provide the applicable waiting period under the insured's policy. Please also indicate whether the amount of time coverage remains in effect once becomes active for a given incident.

Legislative Efforts to Compel Coverage for Business Interruption Losses

In addition to the recent spate of regulatory mandates on insurers, there are ongoing legislative efforts seeking to require insurers to waive legitimate policy exclusions, and to cover pandemic-related claims where coverage arguably does not exist. For example, the Ohio legislature is seeking to pass HB 589 whose goal is “to bring relief to small business who are already feeling a financial strain due to the COVID-19 pandemic shut down, and were shut out of relief efforts offered by the federal court.” The bill now awaits further hearings in the House Insurance Committee, but if passed would:

- Require certain policies of property and casualty insurance to provide coverage for business interruption losses to cover losses attributable to pandemic;
- Apply to policies of insurance in effect on the effective date of the bill for losses accrued during the State of Emergency declared by the Governor on March 9, 2020;
- Enable insurers providing the required coverage to apply to the Superintendent for reimbursement;
- Require the Superintendent to impose an assessment on all property and casualty insurers to recoup amounts reimbursed to insurers;
- Declare an emergency, allowing the proposal to go into effect immediately upon enactment.

Massachusetts introduced similar legislation in Bill No. SD.2888, which applies to companies that employ 150 or fewer full-time employees. While the Ohio bill does not expressly address the treatment of virus exclusion endorsements or the requirement that there be “direct physical loss or damage” to covered property, the Massachusetts bill is very clear on that point: “no insurer in the commonwealth may deny a claim for the loss of use and occupancy and business interruption on account of (i) COVID-19 being a virus (even if the relevant insurance policy excludes losses resulting from viruses); or (ii) there being no physical damage to the property of the insured or to any other relevant property.”

The Massachusetts bill also provides that “[f]or the avoidance of doubt, this act is subject to Chapter 176D of the General Laws.” Chapter 176D concerns Unfair Methods of Competition, and Unfair and Deceptive Acts and Practices in the Business of Insurance. By including this reference,

the Massachusetts legislature is sending a very clear warning to insurers that the bill, if enacted into law, must be complied with fairly and in good faith.

Several other states are seeking to enact similar legislation and It should be noted that most of these bills call for assessments against, and reimbursement to, insurers by the department of insurance:

- Louisiana House Bill 858 and Senate Bill 477 both require that policies be construed to include coverage for loss of business or business interruption due to the COVID-19 emergency;
- New York, Bill A10226A nullify exclusions for virus or pandemic in business interruption insurance and provides that “an act in relation to certain perils be covered under business interruption insurance during the coronavirus disease 2019 pandemic... for any loss of business or business interruption;”
- Pennsylvania, House Bill 2372 calls for coverage under business interruption policies for losses due to the COVID-19 emergency; and
- South Carolina Bill S. 1188 requires coverage for losses due to COVID-19 under business interruption policies.

It is important to note that in light of the legislative pressures being placed on insurers, insurance regulators have taken a bold stand in support of the insurance industry’s coverage rights. On March 2020, the National Association of Insurance Commissioners issued the following statement:

We thank Congress and the Administration for acting quickly to give states greater flexibility to protect consumers and deal with ever-changing market dynamics, and we look forward to continuing that partnership as issues arise. However, as Congress considers further legislative proposals to address the devastating impacts of the COVID-19 pandemic, we would caution against and oppose proposals that would require insurers to retroactively pay unfunded COVID-19 business interruption claims that insurance policies do not currently cover. Business interruption policies were generally not designed or priced to provide coverage against communicable diseases, such as COVID-19 and therefore include exclusions for that risk. Insurance works well and remains affordable when a relatively small number of claims are spread across a broader group, and therefore it is not typically well suited for a global pandemic where virtually every policyholder suffers significant losses at the same time for an extended period. While the U.S. insurance sector remains strong, if insurance companies are required to cover such claims, such an action would create substantial solvency risks for the sector, significantly undermine the ability of insurers to pay Other types of claims, and potentially exacerbate the negative financial and economic impact the country is currently experiencing.

Conclusion

The extraordinary number of insurance claims being filed associated with COVID-19, recent hurricanes and civil unrest is clearly taxing the insurance industry's resources and challenging its efforts to reach timely coverage determinations and adjustments, especially if there is an ongoing need for quarantining and social distancing. Notwithstanding, insurers operate under a continuing duty of good faith and fair dealing, even during extraordinary circumstances such as disasters and national emergencies. Needless to say, as of this writing no legislative bills nor regulatory notices have been issued that seeks to *relax* an insurer's obligations to conduct a prompt investigation or disposition of claims, or to lessen the penalties they suffer for any failure to do so, notwithstanding the ongoing pandemic.

Therefore, insurers should emphasize to their claims staff the importance of:

- Adhering to the timelines associated with each state's Fair Claims Practices Act;
- Open a line of communication with state regulators regarding their ongoing efforts to adhere to the contractual and regulatory timelines for reaching a coverage decision notwithstanding their resources being taxed by the pandemic;
- Conducting a reasonable, good faith and prompt investigation and maintaining a well-documented claims file that outlines the steps of an investigation and which explains the basis for any delays; and
- Ensuring that all coverage rights are properly reserved and that communication with the insured is maintained during the course of a COVID-19 claim investigation.

About the Author

Rick Hammond is a partner with HeplerBroom, LLC, and he serves as national counsel on matters relating to property insurance coverage, business interruption, fire and explosion cases, and bad faith. He also serves as an expert witness on insurance law, bad faith and coverage issues, and he is an adjunct professor on insurance law at Loyola University Chicago Law School.

Previously, Rick was the Assistant Deputy Director of the Illinois Department of Insurance's Chicago office, served as an Executive Director of a national insurance trade association, and held managerial positions in property claims and agency for two national insurance carriers.

Mr. Hammond is Past-President of the Illinois Association of Defense Trial Counsel and formerly served on the faculty and Board of Directors of the Insurance School of Chicago. He is a member of the Federation of Defense and Corporate Counsel and former Chair of their Property Insurance

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Mr. Hammond was one of two attorneys in the country selected by the Lexis Nexis Insurance Law Center in 2008 to receive its "Insurance Lawyer of the Year Award," and was appointed by the Illinois Supreme Court to serve on the state's COVID-19 Task Force on Court Operations. He is also a Fellow of the American College of Coverage Counsel, an organization that includes some of the most preeminent coverage and extra-contractual attorneys in the United States and Canada. Questions or comments can be directed to Mr. Hammond at the law firm of HeplerBroom, LLC, 30 North LaSalle, Suite 2900, Chicago, Illinois 60602, (312) 205-7743, or at the e-mail address of rick.hammond@heplerbroom.com.