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Coronavirus and Business Interruption Insurance: What Does The Physical Loss Or Damage Requirement Mean?

By Benjamin H. Nissim and Marilyn B. Fagelson | April 17, 2020

Many businesses forced to reduce or pause their operations as a result of the Coronavirus pandemic have turned to their insurance carriers for the support their insurance policies promised. Unfortunately, all that these businesses have received in response is a resounding – and nearly uniform – rejection of their claims. The question then is, is pursuing a claim and the potential resulting fight with the insurer worthwhile? For some, the answer is yes.

Although there are many possible routes to insurance coverage for losses arising out of the Coronavirus pandemic, one of the major avenues for recovery will be under Business Interruption insurance. Typically found as part of a commercial property insurance policy, Business Interruption coverage generally provides for the recovery of lost income and related "extra expense" in connection with a "direct physical loss" or "physical damage" to insured property.

The meaning of "direct physical loss" or "physical damage" to insured property has already become a flashpoint in Coronavirus related claims. Carriers have made clear their view that these terms require actual physical harm – destruction, damage, etc. – to property.[1] But this broad, self-serving proclamation is just that: a position, not the law. What this argument ignores is that many courts across the country have determined that "physical loss" includes odors, bacteria, airborne contaminants, and other such intrusions into a property – and that coverage is not limited to structural building damage or similar loss. Success on a claim for Coronavirus injuries will likely depend on the individual state law applicable to the claim.

The importance of individual state law to this inquiry is aptly illustrated by court decisions interpreting the "physical damage" or "physical loss" requirement from Connecticut, New York, and Massachusetts. While none of these states appear to have directly addressed the issue at hand (i.e. physical loss or damage caused by a virus/pandemic), case law from these jurisdictions establishes baseline legal principles that should inform a policyholder's ability to meet the coverage requirements.

[1] This purported requirement has also been echoed in some respects by regulators with, for instance, the Connecticut Insurance Department providing in its FAQ on Business Interruption insurance that "coverage typically can only be triggered if you have property loss that leads to the business interruption." (See https://portal.ct.gov/CID/Coronavirus/Coronavirus-Business-Interruption-FAQs).

Connecticut

Connecticut courts have had limited opportunity to construe "direct physical loss" or "physical damage" policy language in the Business Interruption context. Nonetheless, a U.S. District Court of Connecticut case applying Connecticut law provides a well-reasoned basis for an expansive understanding of the physical loss or damage requirement. *See Yale University v. CIGNA Ins. Co.,* 224 F. Supp. 2d 402 (D. Conn. 2002).

The dispute in *Yale* centered on coverage for alleged property damage arising out of asbestos and lead paint in the University's buildings. On summary judgment, the carrier sought to frame the property damage issue as involving the mere existence of asbestos and lead paint in the school's buildings – a condition, it claimed, did not in and of itself constitute a physical loss or damage to property. In contrast, Yale and the Court framed the issue as whether Yale's buildings were "contaminated" with *friable* asbestos and *non-intact* lead-based paint. In rejecting the carriers' view, the Court emphasized the difference between the mere "presence" of a material as compared to "contamination" caused by material. The Court further found that the carrier "fail[ed] even to consider, let alone distinguish, the substantial body of case law in which a variety of contaminating conditions have been held to constitute physical loss of or damage to property." To that end, after reviewing case law from a variety of jurisdictions, the Court concluded that "Yale has sustained its burden of demonstrating that it has suffered 'physical loss of or damage to property' as required under the all risk policies for the presence of asbestos or lead contamination in its buildings."

While *Yale* is not necessarily on all-fours with coverage disputes arising out of the Coronavirus, it plainly supports an expansive interpretation of the "physical loss" or "physical damage" requirement found in many Business Interruption coverage provisions.

Massachusetts

Similar to Connecticut, Massachusetts case law supports an expansive reading of the physical loss or damage requirement found in many Business Interruption policies. Courts in Massachusetts have specifically found that the "direct physical loss or damage" requirement should be interpreted broadly "to include more than tangible damage to the structure of insured property." *Matzner v. Seaco Ins. Co.,* 1998 WL 566658 (Mass. Super. Aug. 12, 1998) (finding "direct physical loss or damage" to property and coverage based on contamination of a building by carbon monoxide and citing cases). *See also Arbeiter v. Cambridge Mut. Fire Ins. Co.*, 1996 WL 1250616, at *2 (Mass. Super. Mar. 15, 1996) ("plaintiffs argue persuasively that fumes are a physical loss which attaches to the property."); *Essex Ins. Co. v. BloomSouth Flooring Corp.*, 562 F.3d 399, 406 (1st Cir. 2009) ("we are persuaded … that odor can constitute physical injury to property under Massachusetts law.").

Given this precedent, Massachusetts policyholders should be able to use these cases in support of coverage under their Business Interruption policies.

New York

By contrast to Connecticut and Massachusetts, New York courts have taken a narrower view of the meaning of "direct physical loss" or "physical damage." In particular, a New York intermediate appellate court has held "the language of the Business Interruption clause in the policy clearly and unambiguously provides coverage only where there is direct physical loss or damage to the insured's property." *Roundabout Theatre Co. v. Cont'l Cas. Co.,* 302 A.D. 2d 1, 2 (N.Y. App. Ct. 2002); *see also Newman, Myers, Kreines, Gross, Harris, P.C. v. Great N. Ins. Co.,* 17 F. Supp. 3d 323 (S.D.N.Y. 2014). In so holding, the court rejected an expansive reading of the policy provision that would have found coverage for a business interruption arising out of a "loss of use of" property rather than actual physical damage.

Even with this more narrow interpretation of "direct physical loss" or "physical damage" in mind, the analysis of future claims must be made based on the unique language and factual situations involved. Accordingly, each insurance contract should be assessed individually within the context of the state's laws to determine whether coverage is available.

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Insurance carriers have positioned the direct physical loss or physical damage requirement contained in many Business Interruption insurance provisions as a complete gatekeeper, precluding coverage for losses arising out of the Coronavirus pandemic. The truth is there is no such clear cut rule. Courts that have considered analogous situations across the country have come to different conclusions regarding the import of the physical loss or damage requirement. Policyholders and practitioners alike must give careful attention to these issues as they consider potential claims.

Ultimately an insurer's coverage obligation to its policyholder is contingent upon the terms and conditions of the individual insurance contracts. If you have questions about whether your current insurance policies provide coverage for losses arising out of the Coronavirus, do not hesitate to contact us.

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