Opposite Sides of the Table: Restaurants Seek Recovery From Insurers for Business Interruption in the Wake of COVID-19

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As COVID-19 cases have continued to spread across the country resulting in government-issued "shelter in place" orders, few industries have felt the impact as swiftly and deeply as the restaurant industry. Indeed, such government orders have required restaurants to shut down all onsite dining, causing a sharp decline in restaurant revenue. According to restaurant.org, since March 1, the industry has lost more than 3 million jobs and $25 billion in sales, and roughly 50% of restaurant operators anticipate additional layoffs in April. The National Restaurant Association has predicted that the industry will suffer $225 billion in losses in the next few months, forcing the elimination of as many as 7 million industry jobs.

Business Interruption Insurance

In response to the COVID-19 pandemic, many restaurants have sought to recover loss of income and other expenses via business interruption insurance, which is optional coverage typically purchased as part of a commercial peril policy. This type of coverage is designed to provide cash to cover businesses in the event of disaster when operations are suspended. In the wake of COVID-19-related claims, however, insurers are refusing to pay out. Business interruption coverage typically requires a "direct physical loss or damage to covered property," and insurers are gearing up to take the stance that COVID-19 losses do not involve the requisite physical loss or damage to trigger coverage. For example, some insurers have argued that losses due to an economic downturn, fear of contagion, or shutdowns aimed at limiting the spread of coronavirus are not themselves physical loss or damage, and even if they were, would trigger various policy exclusions. The American Property Casualty Insurance Association (APCIA) has issued a statement declaring that "[m]any commercial policies, including those that include business interruption coverage, do not include coverage for communicable diseases or viruses such as COVID-19." Moreover, with certain state legislatures publicly exploring the possibility of mandating business interruption coverage for such losses, the APCIA has stated that "[a]ny action to fundamentally alter business interruption provisions specifically, or property insurance generally, to retroactively mandate insurance coverage for viruses by avoiding these exclusions, would immediately subject insurers to claim payment liability that threatens solvency and the ability to make good on the actual promises

made in existing insurance policies." The APCIA has estimated that business interruption losses for small businesses alone could fall between $220-383 billion per month. However, restaurants should not blindly accept the insurance industry's overly pessimistic view of coverage for these losses.

The Recent Wave of COVID-19-Related Insurance Coverage Litigation

Restaurants facing mounting income losses are taking to the courts to pursue insurance recovery. For example, on March 25, 2020, Napa Valley's world-renowned and three-Michelin-starred the French Laundry, and the Thomas Keller Restaurant Group (the managing entity for French Laundry and Michelin-starred Bouchon Bistro), sued their insurers in Napa County Superior Court. The suit seeks a declaratory judgment affirming that the restaurants' insurance policy provides coverage for business income lost and additional expenses incurred due to government-mandated closures of the restaurants. The French Laundry suit alleges that its "all-risk" policies cover business income losses and reasonable expenses incurred when access to the insured premises is prohibited by an order of "civil authority," and that the restaurants were shut down per a March 18, 2020 Napa County Health Order. The complaint further notes that the Napa County Health Order states that it was issued based on evidence of physical damage to property, namely that the virus "physically infects and stays on surfaces of objects or materials . . . for up to twenty-eight days," and that other countries such as China, Italy, France, and Spain have "implemented the cleaning and fumigating of areas" before allowing these areas to be re-opened to the public.

Similar suits have been cropping up elsewhere in California and throughout the country. On March 20, in one of the initial suits for insurance recovery stemming from the COVID-19 pandemic, Oceana Grill (located on Bourbon Street in New Orleans) filed suit against its insurer and the Governor and State of Louisiana in state court in New Orleans. The suit seeks a declaratory judgment that the policy at issue provides coverage from direct physical loss and/or a civil authority shutdown due to a global pandemic based on allegations substantially similar to The French Laundry suit. Oceana Grill alleges that its policy covers "all risks" unless specifically excluded, and that it does not provide any exclusion due to losses from a global pandemic, though the policy does exclude losses due to biological materials such as pathogens in connection with terrorism or malicious use, which do not apply.

On March 27, 2020, a group of restaurants and movie theatres in Chicago and its suburbs filed suit against their insurer in federal court in Illinois, seeking a declaratory judgment that they are entitled to payment for their business losses stemming from the COVID-19 pandemic, and asserting claims for breach of contract and bad faith denial of insurance coverage under Illinois law. This suit alleges that the insurer issued blanket denials of the plaintiffs' claims for business interruption losses stemming from Illinois' closure orders, often within hours of receiving such claims, despite the fact that the "all risk" policies at issue do not include exclusions for losses caused by viruses or pandemics. The suit also alleges that the policies include coverage for loss of income and extra expenses "caused by action of civil authority that prohibits access" to covered properties, which is triggered when any non-excluded cause results in property damage and is intended to cover governmental action "taken in response to dangerous physical conditions."

On April 7, 2020, in what appears to be the first case involving a policy including an express "Pandemic Event Endorsement" covering pathogen-related business-interruption, a Texas hospitality and entertainment provider, SCGM, Inc., sued its insurer in federal court in Houston. SCGM, Inc. seeks a declaratory judgment that its COVID-19-related business interruption losses are covered by the "Pandemic Event Endorsement" in its insurance policy, and asserts claims for breach of contract for anticipatory breach/repudiation, breach of the covenant of good faith and fair dealing, and gross negligence and/or malice. The policy defines a "Pandemic Event" as "the announcement by a Public Health Authority that a specific Covered Location is being closed as a result of an Epidemic declared by the [Centers for Disease Control and Prevention] or [World Health Organization]." According to the suit, on the same day that SCGM, Inc. notified its insurer of its business interruption claim, the insurer indicated that coronavirus claims would not be covered because coronavirus is not one of the named pathogens in the endorsement. This is despite the fact that the endorsement specifically defines "Covered Disease" as a list of certain "pathogens, their mutations or variations" on which "Severe Acute Respiratory Syndrome-associated Coronavirus (SARS-CoV) disease" appears.

Proposed Legislation

As noted above, there are also legislative efforts underway that are aimed at compelling insurers to cover COVID-19-related losses in response to the pandemic. Several states including Ohio, Massachusetts, New York, Pennsylvania, and Louisiana[1] have introduced bills that would prevent insurers from denying claims for business interruption losses related to COVID-19. Some of these bills seek to require such coverage even where policies include exclusions that insurers would argue otherwise would apply to such risks. As of the date of this article, none of these bills has been signed into law.

Restaurant associations also have made direct appeals to federal and state governments for assistance. On March 18, the National Restaurant Association sent a letter to President Trump seeking relief, including targeted financial relief, $100 billion in federal-backed business interruption insurance through the U.S. Treasury Department that would allow restaurants to seek insured benefits on an expedited basis, a federal loan program equal to lost revenue, and tax measures. Similarly, on March 27, the California Restaurant Association wrote to Gavin Newsom seeking postponement of property taxes, deferrals of licensing fees and sales and payroll taxes, freezing of unemployment insurance rates, eviction protection, and a mandate that insurance companies assist or that state government support the insurance companies by having them approve restaurant COVID-19 related claims, with the state acting as the payment administrator.

Considerations and Action Steps for Policyholders

Restaurants and other businesses should carefully review the specific terms of their commercial policies in light of COVID-19-related business losses to assess whether such losses may be covered. The specific policy language and factual and loss circumstances affecting a particular business are paramount to that assessment.

Moreover, policyholders can and should view with skepticism insurers' blanket assertions that commercial policies for business interruptions do not cover business losses related to COVID-19. As a factual matter, the Centers for Disease Control and Prevention has confirmed that the virus that causes COVID-19 can live on surfaces for days, and indeed, recently found that RNA from COVID-19 existed on surfaces aboard the Diamond Princess cruise ship 17 days after cabins were

[1] New Jersey also filed a similar bill, which was set for a vote on March 16 but was subsequently withdrawn.

vacated. Further, at this juncture, there is no reasonable dispute that the number of coronavirus-related infections and deaths across the U.S. has continued to rise at an alarming rate. These facts undercut insurers' potential argument that the viruses are not physically present in high traffic businesses like restaurants. Therefore, restaurants seeking coverage for business interruptions resulting from COVID-19 may argue that physical contamination establishes the possibility of coverage. In fact, courts in many jurisdictions have found that the presence of contaminants in insured premises can, in fact, constitute "physical loss or damage" so as to trigger coverage.[2]

[2] For example, in *Gregory Packaging, Inc. v. Travelers Prop. Cas. Co. of Am.*, No. 2:12-CV-04418 WHW, 2014 WL 6675934 (D.N.J. Nov. 25, 2014), a packaging company sought to recover for business interruptions under its commercial property insurance policy that covered "direct physical loss of or damage to property" when ammonia was released in one of the company's packaging facilities. *Id.* at *1. The insurer denied the company's claim, because according to the insurer, the company did not suffer physical loss or property damage and the loss was subject to a specific exclusion under the policy terms. *Id.* at *2. The court granted summary judgment for the plaintiff packaging company, finding that the presence of ammonia rendered the packaging facility "unfit for normal human occupancy" and "temporarily incapacitated" the facility, which constituted "physical loss" under the policy at issue. *Id.* at *3-4, 6. The court specifically stated that "courts considering non-structural property damage claims have found that buildings **rendered uninhabitable by dangerous gases or bacteria suffered direct physical loss or damage**." *Id.* at *6 (emphasis added). Similarly, in *Sentinel Management Co. v. New Hampshire Insurance Co.*, 563 N.W.2d 296, 298 (Minn. Ct. App. 1997), an apartment building management company sought to recover under its "all risk" property insurance policy covering direct physical loss to buildings, where the building contained traces of released asbestos. There, the court found that there had been "direct physical loss" where the "building's function may be seriously impaired or destroyed and the property rendered useless *by the presence of contaminants*" even in the absence of tangible physical injury. *Id.* at 300 (emphasis added). And in *Western Fire Ins. Co. v. First Presbyterian Church,* 165 Colo. 34, 39 (Colo.1968) (*en banc*) the Colorado Supreme Court held that a property insurance policy was triggered where local authorities ordered a church building closed after gasoline vapors underneath the building rendered the building unusable, as this constituted a "direct physical loss." The court acknowledged that while neither the building nor its elements were demonstrably altered, its function was eliminated. *Id.* at 40-41; *see also TRAVCO Ins. Co. v. Ward,* 715 F.Supp.2d 699, 709 (E.D. Va. 2010), *aff'd*, 504 F. App'x. 251 (4th Cir. 2013) (finding "direct physical loss" where "home was rendered uninhabitable by the toxic gases" released by defective drywall); *Mellin v. N. Security Ins. Co.*, 115 A.3d 799 (N.H. 2015) (finding that "physical loss" required "a distinct and demonstrable alteration of the insured property" but that could include changes that are perceived by the sense of smell and exist in the absence of structural damage); *Port Authority of N.Y. and N.J. v. Affiliated FM Ins. Co.,* 311 F.3d 226, 235 (3d Cir.2002) (If "the presence of large quantities of asbestos in the air of a building is such as to make the structure uninhabitable and unusable, then there has been a distinct loss to its owner" which would constitute "physical loss."). Therefore, a reasonable argument can be made that property damage has occurred where a virus may be present.

Specific steps that restaurants and other affected businesses should be taking include the following:

(1) Retrieve and carefully review all applicable insurance policies.

(2) Contact the insurer to make a timely report of loss where applicable (as many policies include specific deadlines).

(3) Document all relevant factual circumstances: For example, does the restaurant have any facts to suggest that an infected person entered the premises? Which government orders triggered shutdown? How much in business income would the restaurant have generated had it remained open?

(4) Gather and retain supporting documentation including financial statements, bank statements, tax returns, forecasts and projections, payroll reports, inventory records, purchase orders, and documentation such as receipts to show additional related expenses.

(5) Consider engaging experienced counsel to pursue coverage.

Buchalter attorneys are here to help. Each policy and circumstance is unique, defying a one-size-fits all approach. The coronavirus presents novel challenges and complexities, which Buchalter attorneys are uniquely suited to address. Attorneys in the Firm's Insurance Coverage Practice Group have in-depth understanding of insurance industry policies, practices, procedures and issues, and decades of experience representing policyholders, including restaurants, in insurance recovery matters.

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