INSURANCE LAW

(a/k/a Insurance Meets Life)

DRAKE GENERAL PRACTICE REVIEW
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I. INTRODUCTION

What a year!

A derecho. Flooding. A pandemic.

Life meets insurance.

And if the fallout of some or all of these natural or unnatural disasters hasn't landed on your desk yet, it's late. But in one form or another, your practice will likely be impacted by some of the consequences of those events so let's start with a roadmap on how to address the resulting issues.

II. THE DERECHO

2020 brought far too many opportunities to expand our vocabularies. For example:

> Derecho: a line of intense, widespread, and fast-moving windstorms and sometimes thunderstorms that moves across a great distance and is characterized by damaging winds.

And what is the origin/history of the word? It is of Spanish origin and means "straight ahead." The term was connected with the storm in 1888 by Gustavus Hinrichs, a physics professor at the **University of Iowa**. Reportedly, he adopted the term to distinguish straight-moving winds from the swirling and twisting tornadic winds. When those straight-moving winds hit the Midwest on August 10, 2020, it sent thousands scrambling for the insurance policies.

In order to analyze coverage, I recommend this approach, all starting with the Table of Contents and Dec (Declarations) pages of the Policy. Regardless of the type of policy, I recommend starting with these preliminaries:

- Confirm that the policy is complete and that all correct policy forms, addendums and riders are included
- Insured (identify and confirm)

- Check for additional insureds and insured interests
- Covered property (if property damage, make certain that the property or the auto is listed or additionally covered)
- Dates of Coverage (for liability coverage check for claims made v. "occurrence")
- Location of Property
- Find the general granting clause – insured's obligation to establish coverage initially
- Confirm all definitions – usually capitalized and/or words in bold typeface
- Review exclusions
- Review exceptions to exclusions
- Confirm all obligations upon loss (notice, cooperation, preservation of property, etc.)
- Confirm policy limits

Applying this approach to damages from a derecho, assume that a client came into your office August 11th with his homeowners' policy, his automobile policy, and photos showing downed trees entirely filling the south side of the yard and including a 50' oak that fell, broken windows in his home from limbs blown off trees, the neighbor's driveway blocked by his tree on his neighbor's car and a particularly interesting photo of his tree leaning across the driveway onto the neighbor's roof, having knocked the gutter loose with portions falling halfway down the wall. What advice do you provide?

Resolution of these issues is wholly dependent on the specific language of the particular policy under consideration. Do NOT rely on these summaries based upon sample language without detailed analysis and comparison of the language of the policy you are reviewing.

A. Property Damage

1. Removal of Felled Trees and Bushes

Inevitably and unfortunately, one of the highest expenses can be the cost of the trees, branches and bushes felled by the derecho. Is that expense covered? Look first at the homeowners' policy. Assume that you've confirmed the completeness of the policy, the effective dates of the policy, that the property address is covered and that your client is in fact the insured. Let's see what coverage is available to pay for the debris removal.

It is the obligation of the insured to establish coverage. Most homeowners' policies have language establishing that there is, similar to the following:

> *We will also pay your reasonable expense, up to $1000, for the removal from the "resident premises" of*
>
> *1) Your tree(s) felled by the peril of Windstorm or Hail or Weight of Ice, Snow or Sleet; or*
>
> *2) A neighbor's tree(s) felled by a Peril Insurance Against under Coverage C,*
>
> *Provided the tree(s):*
>
> *(a) Damage(s) a covered structure;*
>
> *(b) Does not damage a covered structure, but*
>
> *(1) Block(s) a driveway on the "resident premises" which prevents a "motor vehicle" that is registered for use on public roads or property from entering or leaving the "resident premises", or*
>
> *(2) Block(s) a ramp or other fixture designed to assist a handicapped person to enter or leave the dwelling building.*

2. Broken Windows and Damaged Shingles

Again, check the granting clause in the policy. Most policies will have language similar to the following:

> *1. We cover:*
>
> *a. The dwelling on the "residence premises" shown in the Declarations …*

Most policies will cover the described damage, subject of course to the deductible that can render the coverage valueless in this context.

3. Replacement of Trees and Shrubs

There are often provisions in the homeowners' policies that will cover replacement of trees and shrubs. BUT there are two significant factors limiting this coverage in the context of the derecho: 1) Wind is not always a covered peril for which replacement is provided; and 2) The expense of the replacement is frequently limited to a small amount of the total available coverage. The following language is an excellent example of the type of language frequently found in homeowners' policies:

> *We cover trees, shrubs, plants or lawns, on the "residence premises", for loss caused by the following Perils Insured Against:*
>
> *a. Fire or Lightning;*
> *b. Explosion;*
> *c. Riot or Civil Commotion;*
> *d. Aircraft;*
> *e. Vehicles not owned or operated by a resident of the "residence premises";*
> *f. Vandalism or Malicious Mischief; or*
> *g. Theft*
>
> *We will pay up to 5% of the limit of liability that applies to the dwelling for all trees, shrubs, plants or lawns. No more than $500 of*

this limit will be available for any one tree, shrub or plant. We do not cover property grown for "business" purposes.

4. Damage to Car from Falling Trees

So, will the homeowners' policy cover damage to your car if a tree falls on it because of the derecho? Probably not. Most policies will contain language similar to the following:

We do not cover:
. . .
"Motor Vehicles"

"Motor Vehicles" is a capitalized and italicized term in the policy and is therefore a defined term. In most cases, it will include a "self-propelled land vehicle."

But don't be discouraged yet. Go to the automobile policy. If there is comprehensive coverage on the policy, recovery is possible. Not every policy contains comprehensive coverage, however, so read the policy closely. Always.

B. Liability Coverage

But what about the neighbor, the one whose driveway is filled with my tree, whose car is buried under my tree and whose roof and gutters are bending under the weight of another of our trees? Assume that we have our trees inspected annually to make certain that they are healthy and in in good shape. There is no strict liability under the law that would make us responsible for the damage to our neighbor's property. And, given the facts states, it is unlikely that there is any liability for the resulting damage to our neighbor's property.

BUT, take a look at the same policy language stated above. The tree in the driveway will be removed at the cost of our neighbor's insurer because of the provisions governing removal if property is damaged or the driveway is blocked. Thanks to our trees, our neighbor had both. You're welcome.

III. THE PANDEMIC

Assume that your client's business had been essentially shut down by mandate of the governor because of COVID-19. She's concerned about losing everything BUT she has a commercial property insurance policy that provides protection for business interruption. Will it cover her losses?

Again, each type of damage will likely require separate analysis. Let's start with loss of business income as that is one that is probably the greatest concern. It is likely (although not uniform) that recovery for the lost income will only be triggered if there is a) "direct physical loss of or damage" to b) insured property by (c) a covered cause of loss. The first and third requirements are the most variant. And then there are the exclusions discussed below.

Resolution of these issues is wholly dependent on the specific language of the particular policy under consideration. Do NOT rely on these summaries based upon sample language without detailed analysis and comparison of the language of the policy you are reviewing.

In analyzing coverage, pay particular attention to the following provisions but ultimately you must analyze the entirety of the policy:

- These commercial policies often provide coverage, including business interruption protection, if there is a "direct physical loss." The case law is just developing in this area, the results are necessarily and understandably wholly dependent upon the policy language and the results are not uniform but are heavily fact dependent.

- Some policies specifically protect protection resulting from "communicable or infectious diseases" – some with and some without requiring physical damage to insured property. Notwithstanding the potential availability of coverage under standard business interruption insurance, businesses especially concerned about the risk of disruptions occasioned by communicable or infectious disease

outbreaks should consider whether to also purchase "communicable or infectious diseases" coverage.

- Check to see if there is coverage for action by civil authorities particularly if a governmental authority has limited access to or from the insured premises. Again, some require actual physical loss to trigger this coverage; others do not.

- Certainly there are other possible ports in the storm but many policies have some form of these coverage.

- Be wary of the exclusions as well as some specifically include losses resulting from a virus.

Let's review some of the most recent cases addressing these particular types of losses. First, the cases in which the potential for coverage was acknowledged, even if only based upon the pleading.

A. Acknowledgement of Possible Coverage

1. *Studio 417, Inc. v. Cincinnati Insurance Company,* 2020 WL 4692385, at *2 (W.D. Mo. Aug. 12, 2020)

The insureds (hair salon and restaurants) brought an action to seek coverage for losses suffered for loss of business over the previous several months as a result of the COVID-19 pandemic. In particular, they alleged that COVID-19 "is a physical substance" that "live(s) on" is "active on inert physical surfaces" and is "emitted into the air." Insureds further allege that the presence of COVID-19 "renders physical property in their vicinity unsafe and unusable," resulting in forced suspension or reduced business at their various operations. In fact, the civil authorities in Missouri and Kansas had issued orders requiring closure or reduction of the insureds' businesses.

Plaintiffs further allege that the presence of COVID-19 and the Closure Orders "caused a direct physical loss or direct physical damage to their premises 'by denying use of and damaging the covered property, and by causing a necessary suspension of operations during a period of restoration.'"

The insureds had policies with Cincinnati Insurance providing coverages entitled: Business Income, Civil Authority, Ingress and Egress, Dependent Property, and Sue and Labor Coverages. They filed an action for breach of contract and seeking a declaratory judgment under for their losses under these designated coverages.
The insurer responded with a motion to dismiss arguing that the policies in question provide coverage "only for income losses tied to physical damage to property, not for economic loss caused by governmental or other efforts to protect the public from disease … the same direct physical loss requirement applies to all the coverages for which Plaintiffs sue." And so the battle lines were drawn.

Because the case relied on jurisdiction based upon diversity of citizenship, state law applied. However, note how similar the Missouri state law is to the Iowa law (with Iowa citations below):

- Interpretation of an insurance policy is a question of law to be determined by the Court. [Iowa cite: *A.Y. McDonald Ind., Inc. v. Ins. Co. of North America*, 475 N.W.2d 607 (Iowa 1991) ("Construction of an insurance policy—the process of determining its legal effect—is a question of law for the court. Interpretation—the process of determining the meaning of words used—is also a question of law for the court unless it depends on extrinsic evidence or a choice among reasonable inferences to be drawn. *Farm Bureau Mut. Ins. Co. v. Sandbulte,* 302 N.W.2d 104, 107–08 (Iowa 1981)").]

- Insurance contracts are read as a whole. [Iowa cite: *Boelman v. Grinnell Mut. Ins. Co.*, 826 N.W.2d 494, 501 (Iowa 2013) ("We read the policy as a whole when determining whether the contract has two equally plausible interpretations, not seriatim by clauses.").]

- The intent of the parties controls, giving effect to the contract as written. [Iowa cite: *Monroe County v. International Ins. Co.,* 609 N.W. 522, 525 (Iowa 2000) ("In the construction of insurance policies, the cardinal principle is that the intention of the parties must prevail. If the language of the policy is unambiguous, as the parties concede it is in the present case, that intent is determined by what the policy itself says. *A.Y. McDonald Ind., Inc. v. Ins. Co. of North America, 475 N.W.2d 607, 618 (Iowa 1991).*)]

- Insurance policies are given a reasonable construction and interpreted so as to afford coverage rather than defeat coverage.

- Terms are given the meaning which would be attached by an ordinary person of average understanding if purchasing insurance, namely the "plain and ordinary" meaning of the phrase. [Iowa cite: *Farm and City Ins. Co. v. Potter*, 330 N.W.2d 263, 265 (Iowa 1983) ("The policy nowhere defines the term 'caused by accident.' Consequently we give these words their ordinary rather than a technical meaning, one which a reasonable person would understand them to mean. *Central Bearings Co. v. Wolverine Insurance Co.,* 179 N.W.2d 443, 445 (Iowa 1970); *Goodsell v. State Automobile and Casualty Underwriters*, 261 Iowa 135, 140, 153 N.W.2d 458, 461 (1967); *American Family Mut. Ins. Co. v. Petersen,* 679 N.W.2d 571, 577 (Iowa 2004) ("When a word is left undefined in a policy, we give it the ordinary meaning a reasonable person would understand the word to mean. *Farm & City Ins. Co. v. Potter,* 330 N.W.2d 263, 265 (Iowa 1983).")]

- If the insurance policy is unambiguous, it will be enforced as written absent a statute or public policy requiring coverage; if the *policy is ambiguous, it will be enforced against the insurer. [Iowa cite: Boelman* v. Grinnell Mut. Ins. Co., 826 N.W.2d 494 (Iowa 2013) ("If the policy is ambiguous, we adopt the construction most favorable to the insured. *Hamm v. Allied Mut. Ins. Co.,* 612 N.W.2d 775, 778

(Iowa 2000). This same rule applies when an exclusion is ambiguous, because "[a]n insurer assumes a duty to define any limitations or exclusionary clauses in clear and explicit terms." *Thomas,* 749 N.W.2d at 682 (quoting *Hornick v. Owners Ins. Co.*, 511 N.W.2d 370, 374 (Iowa 1993)). Thus, we strictly construe exclusions against the insurer. *Ferguson,* 512 N.W.2d at 299. We do so because insurance policies constitute adhesion contracts. *Allied Mut. Ins. Co. v. Costello,* 557 N.W.2d 284, 286 (Iowa 1996).")]

- When words in a policy are left undefined, we give them the meaning that a reasonable person would understand them to mean. [Iowa Cite: *Farm & City Ins. Co. v. Potter,* 330 N.W.2d 263, 265 (Iowa 1983); *Boelman v. Grinnell Mut. In*s. Co., 826 N.W.2d 494, 501 (Iowa 2013) ("The plain meaning of the insurance contract generally prevails. *Thomas v. Progressive Cas. Ins. Co.*, 749 N.W.2d 678, 682 (Iowa 2008)".)]

So, under those guiding principles, was there a "direct physical loss" resulting from COVID-19 and the action of the civil authorities potentially resulting in a covered claim?

According to Judge Bough in the Southern District of Missouri, YES! A review of the various theories of recovery and the court's analysis follows.

(a) Coverage for Direct Physical Loss

First let's look at the policy language. It requires "direct physical loss" – an undefined term that permits reliance on the "plain and ordinary meaning" of the term. According to the court, the dictionary defines "direct" in part as "characterized by close logical, causal, or consequential relationship." "Physical" is defined as "having material existence; perceptible especially through the senses and subject to the laws of nature." And "loss" is defined as "the act of losing possession" and "deprivation." According to the court, plaintiffs had alleged a causal relationship between COVID-19 ("a physical substances" that "live(s) on" and is "active on inert physical surfaces" and is also "emitted into the air."

Because the virus allegedly "attached to and deprived Plaintiffs of their property," rendering it "unsafe and unusable," there was a direct physical loss" based upon the "plain and ordinary meaning of the phrase." In reaching this conclusion, the trial court specifically noted that the policy required physical loss OR physical damage – not both. And, to give meaning to the entirety of the text, "loss" must mean something other than "damage." In support of its argument, the trial court offered several examples of instances in which the courts have recognized loss in the absence of physical damage, e.g., loss of use of home because of infestation of brown recluse spiders; possibly presence of asbestos rendering the structure uninhabitable; inability to inhabit the building for any reason is possibly a physical loss although not physical damage.

In reaching its conclusion, the trial court conceded that there is case law in support of the insurer's position that physical tangible alteration is required to show a "physical loss." The court, however, distinguished some cases appearing to be at odds with the holding in *Studio 417*, including *Source Food Tech, Inc. v. U.S. Fid. & Guar. Co.*, 465 F.3d 834 (8th Cir. 2006). First, please note that *Source Food* was decided under Minnesota law; secondly *Source Food* was a claim based on the inability to import product because of the closing of the border to Canadian beef products due to Mad Cow disease although there was no allegation that the product was actually that the product was in fact physically impacted in any manner. In the instant case, there are allegations of infiltration of the virus on the facility and in the air of the facility. In an effort to not merely distinguish but to find some support in Source Food, Judge Bough noted that the 8th Circuit did mention that property could be "physically contaminated … by the release of asbestos fibers" to meet the necessary criteria, analogizing it to the plaintiffs' assertion that the virus has physically contaminated its facility.

(b) Civil Authority Coverage

Plaintiffs also sought coverage for the loss resulting from the action of the civil authorities in the mandates against in-restaurant dining and restrictions on "non-essential" businesses. The insurer responded with two arguments:

1) Civil authority coverage requires "direct physical loss to property other than the Plaintiffs' property" and that the coronavirus does not cause direct physical loss to other property.

This argument was rejected in accordance with the above analysis.

2) Civil coverage analysis requires "that access to Plaintiffs' premises be prohibited by an order of Civil Authority" but the orders did not prohibit access to the premises as they were still able to remain open for food preparation, take-out and delivery.

According to the trial court, the policy language does not require that the civil order prohibit ALL access or ANY access. The limitation on access was sufficient to establish the potential for coverage.

(c) Ingress and Egress Coverage

In what became repetitive arguments and equally repetitive rejections, the trial court rejected the insurers argument that there was no qualifying direct physical loss and that the ingress or egress coverage from the premises is not applicable is the prohibited by civil authority. The trial court concluded that the ingress and egress from the premises was rendered unsafe as a result of both COVID-19 and the closure orders. The court found that that was sufficient to state a claim for ingress and egress coverage.

(d) Claim for Dependent Property Coverage

In addition to the already rejected claim that there was no direct physical injury, the insurer also argued that there was no alleged suspension of the businesses because of the lack of materials or services from a "dependent property." "Dependent property" was defined in the policy as "property operated by others whom (the insured) depends(s) on to … deliver materials or services to (the insured) … (a)ccept (the insured's) products or services … (or) (a)ttract customers to (the insured's) business." The court found the allegations sufficient.

And the insureds survived the motion to dismiss to fight another day.

CAVEATS:

In analyzing *Studio 417*, please note the following:

- EVERY CASE is determined by the language of the applicable policy so be certain to compare language to ascertain the applicability of this holding;
- The case was decided under Missouri law;
- The case has not been followed in any other jurisdiction of which I am aware;
- Iowa has case law that would impact this decision;
- The decision was a ruling on a motion to dismiss without evidentiary requirements and therefore the standard is lower.

2. *Blue Springs Dental Care, LLC v. Owners Ins. Co.*, 20-CV-00383-SRB, 2020 WL 5637963, at *6 (W.D. Mo. Sept. 21, 2020)

Same song; second verse. In *Blue Springs*, a group of dental practices sought coverage for lost income because of the pandemic resulting from a Stay at Home Order issued on April 3, 2020 and similar orders issued in the counties in which the dental clinics were located. Plaintiffs "allege that COVID-19 and the Stay Home Orders have forced them to suspend most of their business operations and deprived them of the use of their dental clinics, thus causing them to suffer "a direct physical loss" and entitling them to coverage under the Policies."

The court agreed, noting that

> the presence of COVID-19 on and around the insured property deprived Plaintiffs of the use of their property and also damaged it." (citation omitted) Plaintiffs also contend they sufficiently allege a physical loss, arguing their allegations that Plaintiffs were forced to end or dramatically reduce all operations at their clinics because of

> "actual contamination by COVID-19" as well as related restrictions imposed by the Stay Home Orders that "prohibited the public from accessing Plaintiffs' covered premises." (citation omitted) Plaintiffs argue that Owners attempts to equate the term "loss" with "damage" when those terms are not synonymous, and note the loss of access to a property or the loss of a property's essential functionality can constitute a physical loss.

Note, however, that this case too came before the court on a motion to dismiss and the plaintiffs' case was based upon allegations and not proof.

B. Authorities Rejecting Coverage

1. *Source Food Technology, Inc. v. U.S. Fidelity and Guar. Co.*, 465 F.3d 834 (2006)

Source Food sold cooking oil and shortening containing beef tallow. Its supplier of beef product was Hubbert's Industries in Ontario, Canada. In 2003, Source Food ordered beef product from Hubbert's Industries that manufactured, packaged and loaded a truck for shipping to Source Food. However, at that time, a case of mad cow disease was identified in Canada. As a result, the United States Department of Agriculture prohibited the importation of the beef products from Canada on May 20, 2003. The result was that Source Food was unable to fulfill its contracts to deliver its products and lost customers and income. It then sought insurance coverage for the loss.

The policy in question provided in relevant part as follows:

> (1) "Business income." We will pay the actual loss of "business income" you sustain due to the necessary suspension of your "operations" during the "period of restoration." The suspension must be caused by *direct physical loss to Property* (other than those items listed in SECTION I.A.2.), including Property Off Premises, and result from any Covered Cause of Loss....
>
> (4) Action by Civil Authority. We will pay for the actual loss of "business income" you sustain and necessary "extra expense" caused by action of civil authority that prohibits access to the described

> premises due to *direct physical loss to property*, other than at the described premises, caused by or resulting from any Covered Cause of Loss. (Emphasis added).

In order to recover, therefore, the damage must result from suspension of business caused by "direct physical loss to Property." The Eighth Circuit found no direct physical loss to Property, noting as follows:

> Although Source Food's beef product in the truck could not be transported to the United States due to the closing of the border to Canadian beef products, the beef product on the truck was not—as Source Foods concedes—physically contaminated or damaged in any manner. To characterize Source Food's inability to transport its truckload of beef product across the border and sell the beef product in the United States as direct physical loss to property would render the word "physical" meaningless. Moreover, the policy's use of the word "to" in the policy language "direct physical loss *to* property" is significant. Source Food's argument might be stronger if the policy's language included the word "of" rather than "to," as in "direct physical loss *of* property" or even "direct loss *of* property." But these phrases are not found in the policy. Thus, the policy's use of the words "to property" further undermines Source Food's argument that a border closing triggers insurance coverage under this policy.

465 F.3d at 838.

2. *Water Sports Kauai, Inc. v. Fireman's Fund Insurance Company*, 2020 WL 6562332, at *6 (N.D. Calif. Nov. 9, 2020)

The insured, Water Sports Kauai, Inc., was forced to shut down its twelve stores due *both* "to the spread of the coronavirus and to directives from Hawaii's Governor limiting the operation of non-essential businesses." To recover its loss, Water Sports made a claim against its insurers under the "Lost Business Income" and "Civil Authority" provisions. The claim was denied and suit filed.

The policy provided in relevant part as follows:

> g. Business Income
>
> We will pay for the actual loss of Business Income you sustain due to the necessary suspension of your operations during the period of restoration.
>
> ...
>
> The suspension must be caused by *direct physical loss of or damage to property* at the described premises, …..
>
> …..
>
> h. Extra Expense
>
> We will pay necessary Extra Expense you incur during the **period of restoration** that you would not have incurred if there *had been no direct physical loss or damage to property at the described p*remises, including personal property in the open (or in a vehicle) within 100 feet of the described premises, caused by or resulting from a Covered Cause of Loss.
>
> i. Civil Authority
>
> We will pay for the actual loss of Business Income you sustain and necessary Extra Expense caused by action of civil authority that prohibits access to the described premises *due to direct physical loss of or damage to property*, other than at the described premises, caused by or resulting from any Covered Cause of Loss. This coverage will apply for a period of up to two consecutive weeks from the date of that action.

Emphasis added.

The trial court made swift work of the insured's argument based upon the lack of direct physical loss of or damage to property, stating that

> The mere threat of coronavirus is insufficient to show a 'direct physical loss of or damage to' its covered property and the government closures orders are likewise insufficient to show the same. … I will follow the overwhelming majority of courts that have determined that the mere threat of coronavirus cannot cause a 'direct physical loss of or damage to' covered property as required under the Policy. That resolves the issue of coverage under the Business Income and Civil Authority provisions as a result of both the spread of coronavirus and the government closure orders.

In so doing, the court distinguished the line of cases that had found direct physical loss in under circumstances in which there was evidentiary confirmation of harmful chemicals or materials at such extreme levels as to render the property unsafe. See, e.g., *Port Auth. of New York and New Jersey v. Affiliated FM Ins. Co.*, 311 F.3d 226 (3d Cir. 2002) (confirmed evidentiary presence of asbestos at life-threatening levels); *Motorists Mut. Ins. Co. v. Hardinger*, 131 Fed. Appx. 823, 826–27 (3d Cir. 2005) (unpublished) (arsenic seeping into the "concrete slab, carpet, and interior objects are physical matter within the ordinary use of those words.").

It further distinguished the cases from Missouri cited above, dismissing their applicability because in the instant case there was no allegation that coronavirus was actually presence on the property or rendering it uninhabitable. Instead, the court found *Mudpie, Inc. v. Travelers Cas. Ins. Co. of Am.*, 20-CV-03213-JST, 2020 WL 5525171, at *5 (N.D. Cal. Sept. 14, 2020) (discussed below) which dismissed the insured's claim "for failure to allege COVID-19 or any other physical impetus caused the loss of functionality where plaintiff 'does not allege that 'Covid-19 entered the [property] through any employee or customer' and did not allege that store was closed 'because its employees became sick or coronavirus was discovered on the property'."

3. *Seifert v. IMT Insurance Company*, 2020 WL 6120002 (Minn. Oct. 16, 2020)

In *Seifert*, the insured's beauty salon was closed following a mandated closure of salons and barbershops on March 13, 2020 in response to the coronavirus

pandemic. In response, Seifert sought coverage for loss under his Businessowners Coverage Form, which covered "direct physical loss of or damage to Covered Property at the premises described."

The court held that no coverage was available. "… Seifert's claims fail to fall within the permissible realm of "direct physical loss," as he cannot allege facts showing his properties were actually contaminated or damaged by the coronavirus." Governmental action prohibiting the use of the property is insufficient. The motion to dismiss was granted.

Note also that this policy had an interesting and quite common exclusion for "loss or damage caused indirectly or directly by any 'virus, bacterium or other microorganism that induces or is capable of inducing physical distress, illness or disease'." Under Iowa law, as in most states, the insurer has the burden to establish the applicability of an exclusion. See., e.g., *Postello v. Am. Family Ins. Co.*, 823 N.W.2d (Iowa 2012); *Am. Family Mut. Ins. Co. v. Corrigan*, 697 N.W.2d 108, 111 (Iowa 2005); *Kalell v. Mut. Fire & Auto. Ins. Co.*, 471 N.W.2d 865, 867 (Iowa 1991). Particularly given the policy's provision stating that the virus need only be a concurrent cause, the court found the exclusion applicable.

4. *Mudpie, Inc. v. Travelers Cas. Ins. Co. of Am.*, 20-CV-03213-JST, 2020 WL 5525171, at *5 (N.D. Cal. Sept. 14, 2020)

Mudpie, Inc.'s retail store was forced to close with the issuance of a Stay at Home Order in California. It sought coverage for the resulting loss under the terms of its comprehensive business insurance from Travelers Casualty Insurance Company of America ("Travelers").

The insurer argued that the insured must support its claim with "a distinct, demonstrable, physical alteration of the property" or "a *physical change* in the condition of the property." While the trial court rejected Travelers's expansive interpretation of the relevant language, with a very articulate description of the distinguishing characteristics it rejected the insured's claim on the following basis:

Mudpie cites several non-California cases for the proposition that the "loss of functionality of, or access to, a property," such as Mudpie's loss of functionality of its storefront, "constitutes a direct physical loss of property."[5] ECF No. 19 at 15. However, each of these cases involved an intervening physical force which "made the premises uninhabitable or entirely unusable." (citations omitted)

Indeed, numerous courts outside the Ninth Circuit have found that some outside physical force must have *induced* a detrimental change in the property's capabilities before a plaintiff alleging loss of use can establish a "direct physical loss of property." (citations omitted*)* For instance, in *Western Fire Insurance Co. v. First Presbyterian Church* the Supreme Court of Colorado determined that a direct physical loss had occurred when the insured, acting upon the orders of the fire department, closed the church building because gas had infiltrated the soil underneath it. 165 Colo. 34, 437 P.2d 52, 54-55 (1968). The court clarified that "the so-called 'loss of use' of the church premises, standing alone, d[id] not in and of itself constitute a 'direct physical loss.' " *Id.* at 55. Rather, the direct physical loss resulted from the "accumulation of gasoline around and under the church building," which made further use of the building highly dangerous. *Id.* The California Court of Appeal reinforced the *Western Fire* court's reasoning, noting that *Western Fire* "does *not* stand for the proposition that loss of intangible property can constitute a physical loss." *Ward Gen. Ins. Servs., Inc. v. Emps. Fire Ins. Co.*, 114 Cal. App. 4th 548, 558, 7 Cal.Rptr.3d 844 (Cal. Ct. App. 2004). Rather, "[a] physical loss occurred when the foundations became saturated with gasoline." *Id.*

5. *Pappy's Barber Shops, Inc. v. Farmers Group, Inc.*, 2020 WL 5500221 (S.D. Calif. Sept. 11, 2020)

This case clearly articulates the dichotomy that ultimately defines the outcome in this series of cases. As the court stated:

> Here, Defendants move to dismiss on the grounds that the complaint does not allege any "direct physical loss of or damage to property" as is required for coverage under the business income, civil authority, and extra expense coverage provisions. In their opposition, Plaintiffs contend that this Policy language does not require "physical alteration to property," and that "jurisdictions around the country have held that a property that is uninhabitable or unsuitable for its intended purpose qualifies as a physical loss under commercial property insurance policies."

The court declined to accept the insured's effort to claim loss without physical impact.

> "Under California law, losses from inability to use property do not amount to 'direct physical loss of or damage to property' within the ordinary and popular meaning of that phrase. Physical loss or damage occurs only when property undergoes a 'distinct, demonstrable, physical alteration.'"

6. And yet more for your review and analysis:

- T*urek Enterprises, Inc. v. State Farm Mut. Auto. Ins. Co*., 2020 WL 5258484 (E.D. Mich. Sept. 3, 2020) ("Based on the foregoing, 'accidental direct physical loss to Covered Property' is an unambiguous term that plainly requires Plaintiff to demonstrate some tangible damage to Covered Property. Because Plaintiff has failed to state such damage, the complaint does not allege a Covered Cause of Loss.') Additionally, this policy included an Anti-Concurrent Causation Clause with an exclusion for loss/damage caused by a virus.

- *T & E Chicago LLC v. The Cincinnati Ins. Co.*, 2020 WL 6801845 (N.D. Ill. Nov. 19, 2020)

- *Diesel Barbershop, LLC, et al. v. State Farm Lloyds*, No. 5:20-CV-461-DAE, 2020 WL 4724305 (W.D. Tex. Aug. 13, 2020).

- *Gavrilides Mgmt. Co. v. Mich. Ins Co.*, No 20-258-CB, 2020 WL 4561979 (Mich. Cir. Ct. July 21, 2020).

- *Rose's 1, LLC v. Erie Ins. Exch.*, No. 2020 CA 002424 B., 2020 WL 4589206 (D.C. Super. Ct. Aug. 6, 2020).

- *Hillcrest Optical, Inc. v. Cont'l Cas. Co.*, l:20-CV-275-JB-B, 2020 WL 6163142 (S.D. Ala. Oct. 21, 2020).

- *UnCork and Create LLC v. Cincinnati Ins. Co.*, 2:20-cv-00401, 2020 WL 6436948 (S.D. W.Va. Nov 2, 2020).

- *Raymond H. Nahmad, DDS PA v. Hartford Cas. Ins. Co.*, No. 1:20-cv-22833-BLOOM/Louis, 2020 WL 6392841 (S.D. Fla. Nov. 2, 2020).

- *North State Deli, LLC v. Cincinnati Ins. Co.*, No. 20-CVS-02569, 2020 WL 6281507 (N.C. Super. Ct. Oct. 9, 2020).

- *West Coast Hotel Mgmt., LLC v Berkshire Hathaway Guard Ins. Co.*, 2:20-cv-05663-VAP-DFMx, 2020 WL 6440037, at *4 n.4 (C.D. Cal. Oct. 27, 2020).

- *Border Chicken AZ LLC v. Nationwide Mut. Ins. Co.*, 2020 WL 6827742 (D. Ariz. November 20, 2020)

IV. NEW CASE LAW

A. *Thornton v. American Interstate Ins. Co.*, 940 N.W.2d 1 (Iowa 2020)

To quote Yogi Berra, "It's *déjà vu* all over again." You might recognize the name of this case. We discuss it a couple years ago. Let's start with a refresher.

The facts:
In 2009, Mr. Thornton was driving a truck for Clayton County Recycling when he lost control of the rig. The truck rolled over, crushing the cab and resulting in serious injuries to Mr. Thornton, including paralysis below the check, loss of use of his left hand and only limited use of his right hand. American Interstate Ins. Co. was the employer's workers' compensation carrier and adjusted the claim.

Through the Workers' Compensation Commission, Mr. Thornton obtained rulings that he was totally, permanently disabled, that he was entitled to a partial commutation and that he needed a new wheelchair (described by the deputy as an agreed resolution).

The litigation history:
In 2013, Mr. Thornton filed a bad faith action. Cross motions for summary judgment were filed. The district court denied the motion filed by American Interstate and partially granted the motion filed by Mr. Thornton, ruling as a matter of law that the insurer acted in bad faith by challenging the claimant's entitlement to permanent total disability benefits. The matter proceeded to trial. The jury awarded $284,000 in actual damages and punitive damages of $25 million. The insurer's motions for judgment not withstanding the verdict, remittitur and new trial were denied.

Both parties appealed. The Iowa Supreme Court affirmed the district court's determination that, as a matter of law, the insurer knew or should have known that it lacked any reasonable basis to deny the claimant's total permanent disability. However, the appellate court concluded that the district court erred in its determination that the insurer committed bad faith by offering to settle the matter

on a closed file basis and by challenging the request for a partial commutation. The Court also agreed with the trial court that the claimant's attorney was not entitled to attorney's fees but did not address the sufficiency of the evidence to support damages for loss of the use of the money and home equity or the reasonableness of the punitive damages. The matter was remanded and proceeded to trial a second time.

At the second trial, the jury again returned a verdict in Mr. Thornton's favor, $382,000 in compensatory damages and $6.75 million in punitive damages. This appeal follows.

The Supreme Court divided the appeal into several separate issues as follows:

- The insurer did not dispute the compensatory damages related to the denial or delay in providing the wheelchair but strenuously objected to the jury's determination that the denial constituted bad faith. Because of the lack of evidence that the insurer was made aware of any role it needed to play to obtain the wheel chair, the ongoing questionable communications links and the fact that the insurance representative's records confirm very timely responses and authorization when requested, the appellate court determined that there was not substantial evidence to support a bad faith claim based upon delay in receipt of the wheel chair. As a result, the $100,000 damages awarded for loss of mind and body and $80,000 awarded for physical and mental pain and suffering resulting from the alleged bad faith in the failure to provide the wheelchair were eliminated.

- The first appeal found that American Interstate did act in bad faith in denying the claimant's permanent total disability. At the second trial, Mr. Thornton asserted that the failure to acknowledge Mr. Thornton's permanent total disability resulted in a delay in getting a partial commutation. The jury appeared to have awarded $114,000 in damages for that delay.

Mr. Thornton contended that, contrary to his representation at the hearing regarding the partial commutation, had he received the funds from the partial commutation earlier, he could have invested in a riskier fund and lost significant revenue as a result. The Supreme Court found that the evidence was simply insufficient to support the damages in connection with the claimed lost investment.

- Mr. Thornton also claimed that he lost an opportunity to buy a one-story home because of the delay in receiving the proceeds of the partial commutation. Again, the Supreme Court found the evidence presented at trial to be insufficient to sustain the $36,000 in damages apparently awarded.

- Next the Court addressed the claim for attorneys' fees related to the workers' compensation proceedings, having already lost the claim for entitlement to attorneys' fees for the bad faith claim. Because of the second jury found that there was no bad faith prior to 10/14/2012, the Court eliminated fees related to representation in the workers' compensation case prior to that date, leaving a balance of just over $18,000 rather than the $52,000 originally awarded.

As a result of the Court's determinations regarding the insufficiency of the evidence and the inappropriateness of a portion of the attorneys' fees, the compensatory damages were reduced from $382,000 to $58,452.42. Instead of dealing with a remittitur, the Supreme Court simply directed the trial court to enter compensatory damages in that amount.

And then the Supreme Court addressed the elephant in the room: an entitlement to and measurement of punitive damages. In a lengthy discussion more than one and a half times the volume dedicated to resolution of all other issues, Justice Appel takes us through the history, the theories, the methods of evaluating and awarding punitive damages, the mixed messages of the U.S. Supreme Court, the potential impact of the changing membership on the highest court in the land and the extensive history of decisions concerning punitive damages under Iowa law.

It is significant that the Court described Iowa law regarding punitive damages as "not highly developed and often quite conclusory" and the federal approach as "evolving." After review of the discussion, however, these appear to be significant conclusions:

- Punitive damages rely on the peculiar facts of each case;
- Punitive damages largely rest in the discretion of the jury but that discretion is not unlimited;
- Punitive damages are not determined by a numerical formula;
- Punitive damages that are so excessive as to demonstrate prejudice and passion on the part of the jury will not be upheld;
- Punitive damages are measured by the relationship between the award and the wrongful conduct of the offending party;
- Punitive damages will be tested "with a view of the extent and nature of the outrageous conduct, the amount necessary for future deterrence, and with deference to the relationship between the punitive award and plaintiff's injury, as reflected in any award for compensation damages. In addition to these traditional factors, we shall consider all circumstances surrounding the conduct and relationship between the parties."

Ultimately the Court followed the analysis of the *Gore/Campbell* U.S. Supreme Court case. The factors are:

1) **Reprehensibility.** The Iowa Supreme Court ultimately concluded that the "reprehensibility" of the insurer's conduct is "the most important factor" to consider and identified these give factors as guidelines to measure the degree of reprehensibility:

   - ✓ Whether the harm was physical as opposed to economic;
   - ✓ Whether the tortious conduct showed an indifference to or reckless disregard of the health or safety of others;
   - ✓ Whether the plaintiff was financially vulnerable;

- ✓ Whether conduct involved an isolated incident or repeated misconduct;

- ✓ Whether the conduct involved intentional malice, trickery, or deceit, or mere accident.

2) Actual harm to potential harm. The Court found that the calculation of ratios is not always helpful but noted the calculations for consideration.

3) Comparison to civil and criminal penalties. The Court found this factor to be much less important in the context of this case.

Based upon all of these factors, the Court concluded that American Interstate's conduct was indeed "reprehensible" but that a

> … double-digit punitive damages award as sought by the plaintiff in this case pushes beyond the upward limit established by the due process punitive damages cases of the United States Supreme Court. … In considering the *Gore/Campbell* factors, we conclude the highest punitive damage award that could be maintained based on the record in this case and this court's rulings in this appeal is $500,000. The conduct in this case is worthy of censure and demands a measure of punishment and deterrence. But after two trips to the Iowa Supreme Court and three years of litigation, a $500,000 punitive damage award is as far as we are willing to go based on the one-time event in this case in order to vindicate the state's legitimate objectives of punishment and deterrence.

The district court was directed to enter judgment accordingly.

B. *33 Carpenters Const., Inc. v. State Farm Life & Cas. Co.*, 939 N.W.2d 69 (Iowa 2020)

This is an interesting insurance-related case as the role of public adjusters is becoming more visible in the casualty insurance business. The case arose out of a claim for hail damage under a homeowners' policy. It's not that the homeowners knew that they had hail damage. To the contrary, they were approached by Mr. Shepherd following a hailstorm and asked if he could inspect the property. Mr. Shepherd reported that he found damage and presented the homeowners with two documents including an "Insurance Contingency" pursuant to which 33 Carpenters agreed to repair the storm damage in exchange for the homeowners' insurance proceeds. 33 Carpenters also agreed to file the insurance claim, handle communications with the insurance company, provide a copy of the report of the insurer and meet with the homeowners to make product selections in addition to other services regarding facilitation of receipt of payment. Repairs were made. The insurer paid what it contended was due but was sued for additional payment by the contractor on assignment of a claim by the homeowner.

Iowa Code section 103A.71(5) provides that contracts entered into by residential contractors who perform public adjuster services without the license required under section 522C.4 are void. 33 Carpenters argued, however, that the insurer could not void the contract because only the Insurance Commissioner could enforce the terms of the statute.

After extensive analysis of the services provided by 33 Carpenters, the Supreme Court affirmed the trial court's determination on summary judgment that 33 Carpenters was indeed acting as an unlicensed public adjuster and that the assignment contract was unenforceable under the governing statute and pursuant to public policy.

V. CONCLUSION

Stay safe. See you next year!