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March 16, 2021

Sen. Heather Sanborn, Chair
Committee on Health Coverage, Insurance and Financial Services
Cross Building, Room 220
Augusta, ME 04330

Rep. Denise Tepler, Chair
Committee on Health Coverage, Insurance and Financial Services
Cross Building, Room 220
Augusta, ME 04330

RE: LD 694, An Act Concerning Business Interruption Insurance

Dear Senator Sanborn and Representative Tepler,

The American Property Casualty Insurance Association ("APCIA") submits these comments in opposition to LD 694. LD 694 is unconstitutional insofar as it proposes to retroactively require coverage for business interruption losses arising out of the COVID-19 pandemic. It also proposes mandating coverage for a type of loss which was not explicitly or impliedly covered and which was never priced. If enacted as proposed, LD 694 would result in catastrophic losses which could imperil the solvency of many insurers. If enacted only on a prospective basis and required to be part of commercial policies, it would severely curtail or eliminate the availability of commercial insurance in Maine.

Constitutional Infirmity

APCIA submits with these comments the opinion memorandum of Gerald Petruccelli, a noted Maine attorney and professor at the University of Maine School of Law. Mr. Petruccelli notes that LD 694 mandates coverage for a risk that carriers explicitly did not assume and in most instances explicitly excluded from coverage. Legislation that seeks to impose retroactive liability on any specific party is subject to heightened constitutional scrutiny. LD 694 wilts under that bright light – it is unconstitutional under the due process clause of both the United States and Maine Constitutions. In addition, the contracts clause specifically precludes retroactively impairing contractual obligations and substantive contractual rights. As Mr. Petruccelli stated, LD 694 contravenes fundamental principles of fairness central to the Due Process, Takings and Contracts clauses of the federal Constitution and Article I, sections 11 and 21 of the Maine Constitution. (Petruccelli Memorandum at 2.)

Scope of Coverage

Business interruption coverage is intended to cover events, such as a fire, which damage property and preclude a business from operating. It is not intended to cover a worldwide pandemic which, as a single event, simultaneously strikes all businesses with like effect and does not do damage to property. Events such as COVID-19 are uninsurable and unmeasurable, like a nuclear disaster.

The contracts entered into by insurers and businesses in Maine did not contemplate coverage for a pandemic-like event. The Insurance Services Office ("ISO") made a filing in Maine in 2006 entitled, "Exclusion of Loss Due to Virus or Bacteria." See, *Commercial Property CP 01 40 07 06*. This nationwide endorsement, which is attached, was approved by the Bureau of Insurance and is part of most commercial policy business interruption coverages in Maine. In particular, subsection B of the Exclusion states:

> 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.

The NAIC, in March of 2020, issued a statement "opposing proposals that would require insurers to retroactively pay unfunded COVID-19 business interruption claims that insurance policies do not currently cover because these policies were generally not designed or priced to provide coverage against communicable diseases" and that private insurance is not typically well suited "for a global pandemic where virtually every policyholder suffers significant losses at the same time for an extended period." The NAIC warned that requiring companies to cover these claims would create substantial solvency risks, undermine the ability of insurers to pay other types of claims and potentially exacerbate the "negative financial and economic impacts the country is currently experiencing."[1]

This issue was also addressed in a timely decision rendered by Nathaniel M. Gorton, United States District Judge for the Eastern District of Massachusetts on March 5, 2021. A copy of that decision is attached. In the case of *Legal Sea Foods LLC v. Strathmore Insurance Company,* Civil Action No. 20-10850-NMG, 2021 U.S.Dist. LEXIS 43097 (D. Mass, Mar. 5, 2021), Judge Gorton stated that the claim by Legal Sea Foods that it was entitled to coverage under its business interruption policy turned on the meaning of the phrase "direct physical loss of or damage to" property. Judge Gorton concluded there was no direct physical loss of or damage to property and that a virus is incapable of damaging physical structures, because a virus harms human beings, not property. The Judge also found that the absence of an express virus exclusion did not operate to create coverage for pandemic-related losses.

The U.S. Congress considered the issue of coverage for COVID-19 pandemic business losses. Members of the House Financial Services Subcommittee, in a hearing entitled "Ensuring Against a Pandemic: Challenges and Solutions for Policyholders and Insurers," and held on November 19, 2020, explicitly recognized that the insurance industry could not and should not cover this pandemic. Subcommittee Chairperson William Lacy Clay (D-MO) commented in his opening statement that it is "not realistic or practical to expect the insurance industry to shoulder the astronomical cost of a global pandemic."

[1] See, National Association of Insurance Commissioners, *NAIC Statement on Congressional Action Relating to COVID-19*, (Mar. 25, 2020), https://content.naic.org/article/statement_naic_statement_congressional_action_relating_covid_19.htm.

There are other immediate consequences of the enactment of LD 694. The losses to the Maine insurance market could be in the range of $400 million to $1.7 billion per month, considering loss of revenue, incidental expense and payroll. These losses simply could not be borne by the industry. The revenue for business interruption insurance in Maine this past year was $20 million per month. In order to pay COVID-19 claims, all other claims (auto, homeowners, other business-related claims, etc.) would not be able to be paid. The exposure simply would be too staggering.

In addition, this legislation would imperil the Maine Guaranty Fund. The Guaranty Fund (24-A M.R.S. §4431 et seq.) exists to cover claims by insureds against carriers which have become insolvent or are otherwise unable to pay claims. The Guaranty Fund exists in three separate accounts – auto, workers compensation, and all other. So, if an auto insurer becomes insolvent, the legitimate claims made against that carrier's policies have to be paid by the other carriers in that market. 24-A M.R.S. §4440-A creates a spillover provision whereby if the losses attendant to one of the three categories are so great that that one category of insurers cannot absorb them, then the other two accounts step in and assist in covering the claims. There is an annual cap on the spillover provisions, but providing coverage for these losses would be so significant that it could force the spillover provision to operate almost in perpetuity if indeed these pandemic losses could be covered at all. In addition, the ability of the industry to respond to other calls against the Guaranty Fund would be non-existent.

Even if LD 694 is only applied prospectively, its mandate would likely preclude commercial insurance in Maine. It is impossible to price out a pandemic-like event. There is no way that the industry could quantify the scope of a pandemic, or the scope of possible losses, or establish premiums for such exposure. What would be its duration, or its geographic extent, or its impact across all businesses? Put another way, the insurance industry could not possibly have expected or planned, or priced policies to anticipate, this COVID-19 pandemic, which has raged for over a year and is still going, and has affected businesses not only in Maine and the U.S., but globally, and has resulted in losses that have crippled state and national economies. Can we even imagine how many times higher premiums would have been going into 2020? Or whether any businesses anywhere in Maine could possibly have afforded such premiums?

For the above reasons, APCIA respectfully opposes LD 694 and urges the Committee to vote the bill out unanimously Ought Not to Pass.

Respectfully submitted,

Bruce C. Gerrity

Enclosures (3)
cc: Committee members
Colleen McCarthy Reid, Committee Analyst
Christian Ricci, Committee Clerk

CONSTITUTIONAL LIMITS ON RETROACTIVELY EXPANDING INSURANCE COVERAGE FOR LOSSES RELATED TO COVID-19

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Introduction and Executive Summary

This analysis of constitutional and legal issues generated by LD 694 is submitted on behalf of the American Property Casualty Insurance Association (APCIA), the principal national trade association for home, automobile, and business insurers. Through a succession of organizational changes, APCIA traces its roots to the founding of the National Board of Fire Underwriters in 1866. Currently, APCIA represents nearly 60% of the United States Property Casualty Insurance Market.

On March 4, 2021, Representative Gramlich of Old Orchard Beach and three cosponsors submitted LD 694 as emergency legislation. The stated purpose of the bill, entitled "An Act Concerning Business Interruption Insurance," is to "ensure that insurers provide coverage for business losses related to COVID-19."[1] LD 694 is designed to compel insurers with business interruption coverage to pay enormous claims that are not covered by any insurance policy. For that reason, it substantially and materially conflicts with federal and state constitutional principles and is economically untenable. The constitutional flaws relate generally to the retroactivity. This bill would not have been introduced if insurance contracts actually did provide business interruption coverage for slow-downs or shut-downs in business activity during the COVID-19 Pandemic. This is an effort to impose a liability that is contractual in form but is in reality a confiscation of the property of the insurers to address systemic societal consequences of a major public health crisis. This is legally impermissible.

Any legal analysis, of course, also ought to be informed by the economic and business realities to be affected by the proposed legislation. Insurance policies are underwritten with due regard to the risks contractually assumed by the insurers and the judgments of underwriters who price the risk assumed. No premium has been paid for risks that were not included in the coverage but were explicitly textually excluded from the coverage. A risk like business interruption from a global pandemic is excluded because it is fundamentally uninsurable. Economically and actuarially, it is particularly unwise as a matter of public policy to wipe out or materially impair the reserves that all insurers must maintain for the benefit of all of their insureds in order to create a peculiar private form of "unfunded mandate" for the benefit of business insureds. If this bill were to be enacted and enforced, the solvency of many insurers would be imperiled. That of course is a problem for the insurers, but it is also a problem for all of their insureds and for Maine.

The economic hardship on businesses, both in Maine and nationwide, as a result of the ongoing COVID-19 pandemic calls out for federal legislative solutions. However, this proposed legislation would almost surely be unconstitutional and void under federal and Maine law and should not be enacted. It would impose massive liability on the insurance industry for a risk property and casualty insurers explicitly *did not assume* and in most cases *specifically excluded* from risks covered by their contracts of insurance. Under Supreme Court precedent, legislative solutions to social problems cannot "single out certain [parties] to bear a burden that is substantial in amount ... and unrelated to any commitment that [those parties] made or to any injury they caused."[2] Such legislation contravenes "fundamental principles of fairness"

[1] Preamble to LD 694.

[2] *Eastern Enterprises v. Apfel,* 524 U.S. 498, 537 (1998) (plurality op.).

embedded in the Due Process, Takings, and Contracts Clauses of the federal Constitution, as well as Article I, §11 and Article I, §21 of Maine's Constitution.

Background

Commercial property insurance policies that include business interruption coverage generally do not cover disease-related or pandemic-related losses. First, policies typically require "direct physical loss of or damage to property," such as from fire or wind, to trigger coverage. Where business interruptions arise instead from decreased economic activity as a result of a virus or preventive public-safety measures enacted to mitigate transmission, no direct physical loss or damage *to property* has occurred that triggers coverage.

On March 5, 2021, the United States District Court for the District of Massachusetts dismissed the Second Amended Complaint of Legal Seafoods, LLC. *See Legal Seafoods, LLC v. Strathmore Insurance Company*, Civil Action No. 20-10850-NMG, 2021 U.S. Dist. LEXIS 43097, at *3 (D. Mass. Mar. 5, 2021). The gravamen of the Complaint was that Legal owns and operates dozens of restaurants in the eastern United States that were either closed or experienced significant reductions in capacity as a result of the pandemic and associated governmental regulations. Legal claimed that its business insurance policy covered business interruption losses secondary to the pandemic, but the Court ruled otherwise and dismissed the case. As is the case in all or nearly all such business policies, the predicate for business interruption coverage is "direct physical loss of or damage to" the physical structures or perhaps operating equipment of the insured. Absent a fire or other physical damage, there is no business interruption coverage. As noted, the point of LD 694 is to create such coverage where none exists as a matter of contract and that is the fatal problem.

Second, since 2006, commercial property policies across the country have typically included a specific, separate "Loss Due to Virus or Bacteria" endorsement that expressly excludes coverage 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."[3] This endorsement was submitted to regulators by the Insurance Services Office (ISO) in 2006 and adopted by the industry following regulatory approval.[4] The exclusion was expressly approved by the Maine Bureau of Insurance and has been used in most Maine property and casualty policies issued since. The virus exclusion applies to all coverage, including 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."[5] In explaining to regulators the concerns that motivated the drafting of the virus endorsement, ISO specifically stated that "[w]hile property policies have not been a source of recovery for losses involving contamination by disease-causing agents, the specter of pandemic or hitherto unorthodox transmission of infectious material raises the concern that insurers employing such policies may face claims in which there are efforts to expand coverage and to create sources of recovery for such losses, contrary to policy intent."[6]

[3] CP 01 40 07 06, ISO CF-2006-OVBEF (approved by Maine 1/1/2007).
[4] *See* ISO form CP 014007 06 (Exclusion Of Loss Due To Virus Or Bacteria).
[5] *Id.* at ¶ A.
[6] ISO Circular, *New Endorsements Filed to Address Exclusion of Loss Due to Virus or Bacteria,*

By creating business interruption coverage retroactively "regardless of policy language," even where a standard-form endorsement specifically excludes virus-related losses from coverage, the proposed legislation would impose a massive financial obligation on property and casualty insurers for an *uninsurable risk* that they specifically foresaw and explicitly excluded from the risks for which they were willing and able to provide coverage. Losses that result from a pandemic cannot be underwritten affordably because they are fundamentally different from losses that result from risks that are insurable. Pandemic losses are not incurred by a relatively few policyholders for separate loss incidents occurring at various times in discrete locations (like losses from fire damage). Even losses from major storm events are local or regional and not national or international. Instead, pandemic losses have a widespread impact on a substantial percentage of *all* policyholders *all at the same time.* The COVID-19 pandemic is global and simultaneous. There are no unaffected policy holders whose premiums permit payments to a subset of affected policy holders. Standard-form policies also generally do not cover loss resulting from nuclear disasters for similar reasons. The premiums that businesses paid for their insurance reflected the express exclusion by endorsement of Loss Due to Virus or Bacteria.

Indeed, an analysis recently completed by APCIA currently estimates Maine COVID-19 related business interruption losses for businesses with fewer than 500 employees in the range of $400 million to $1.7 billion per month for those with business interruption coverage. By contrast, monthly premiums collected by all insurers providing coverage in the fire, allied, and multi-peril non-liability lines are only about $20 million per month. Importantly, this analysis understates the problem because LD 694 is not limited to companies of any particular size.

APCIA also estimates the *total* property-casualty industry surplus-for insurers of all sizes-is currently about $800 billion. That surplus protects *all* auto, home, and business policyholders for *all* types of future insured losses. If enacted by Maine and other states, the proposed legislation would retroactively impose hundreds of billions of dollars of liability on insurers for coverage policyholders did not purchase and for which insurers did not collect premiums or set aside reserves. The magnitude of this liability would likely render many insurers financially incapable of making timely payment on valid claims (even for non-pandemic related causes of loss) from all the coverages that are written for all the risks that are insurable and could pose a serious threat to insurers' solvency. Property and casualty insurers would be unable to continue their important role in risk-transfer going forward, thereby impeding the recovery of the Maine economy from the economic impact of the COVID-19 pandemic.

Analysis

While state legislatures have broad authority to regulate economic activity, legislation like the proposed bill that seeks to impose liabilities retroactively on specific private parties is subject to greater constitutional scrutiny. The Due Process Clause "generally does not permit the retroactive application of a statute if it has especially harsh and oppressive consequences, or results in manifest injustice." [7] Laws that substantially interfere with existing contractual rights

LI-CF-2006-176 (July 6, 2006).

[7] *Greenbergv. Comptroller of the Currency,* 938 F.2d 8, 11 (2d Cir. 1991); *see also BankMarkazi v. Peterson,* 136 S. Ct. 1310, 1325 (2016) ("The Due Process Clause also protects the interests in fair

and obligations are also subject to challenge under the federal Contracts Clause and can constitute uncompensated regulatory takings under the Takings Clause, which applies where government action "has unfairly singled out the property owner to bear a burden that should be borne by the public as a whole."[8] For example:

- In *Allied Structural Steel Co. v. Spannaus,* 438 U.S. 234, 244--47 (1978), the Supreme Court held that a statute that imposed pension obligations on employers beyond what had been negotiated in their contracts violated the *Contracts Clause* because it "nullifies express terms of the company's contractual obligations and imposes a completely unexpected liability in potentially disabling amounts."

- In *Eastern Enterprises v. Apfel,* 524 U.S. 498, 537 (1998), the Supreme Court struck down a statute that retroactively assessed premiums for retirement benefits against certain coal operators because the statute "singles out certain employers to bear a burden that is substantial in amount ... and unrelated to any commitment that the employers made or to any injury they caused." A plurality of the Court found that this constituted an *uncompensated regulatory taking,* and a concurring opinion concluded it violated the *Due Process Clause.*

- In *Vesta Fire Ins. Corp. v. Florida,* 141F.3d1427, 1429-32 (11th Cir. 1998), the Court of Appeals for the Eleventh Circuit held that Florida laws enacted in response to Hurricane Andrew that prevented insurance companies from withdrawing from the marketplace to avoid costs from the hurricane and required them to pay into a disaster fund could constitute *uncompensated regulatory takings.* The laws did not provide an effective mechanism for insurers to recoup losses and fell outside what insurers might reasonably expect based on the pre-existing regulatory scheme.

- In *U.S. Fidelity & Guar. Co. v. McKeithen,* 226 F.3d 412-18 (5th Cir. 2000), the Court of Appeals for the Fifth Circuit struck down, as an *uncompensated regulatory taking,* a Louisiana law that retroactively imposed workers' compensation costs on insurers who previously only served as administrators, finding it unreasonable to shift on a retroactive basis the cost of funding from employers to insurers.

- *In Ass'n of Equip. Mfrs. v. Burgum,* 932 F.3d 727, 730-732 (8th Cir. 2019), the Court of Appeals for the Eighth Circuit held that a North Dakota law that retroactively imposed requirements on transactions between farm equipment manufacturers and dealers "notwithstanding the terms of any contract" violated the *Contracts Clause.*[9]

The proposed retroactive business interruption coverage legislation at issue, like the legislation struck down in these cases, singles out property and casualty insurers to bear the

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notice and repose that may be compromised by retroactive legislation.") (internal quotations omitted).

[8] *Yee v. City of Escondido,* 503 U.S. 519, 523 (1992).

[9] By contrast, in cases in which the Supreme Court rejected Contracts Clause challenges, the laws Involved did not significantly disrupt the parties' contractual expectations or impose substantial, unforeseen liabilities. *See, e.g., Energy Reserves Group, Inc. v. Kansas Power & Light Co.,* 459 U.S. 400 (1983); *General Motors Corp. v. Romein,* 503 U.S. 181 (1992); *Sveen v. Melin,* 138 S. Ct. 1815 (2018).

economic consequences of COVID-19, even though those insurers' contracts do not cover this risk. The insurers made no commitments and caused no injuries that could provide a reasonable basis for imposing this disabling financial burden, much less doing so retroactively. The Maine Legislature should seriously consider the substantial constitutional and economic issues presented by such legislation before moving forward with any proposed retroactive business interruption coverage bill or similar legislative proposal.

Maine law is consistent with federal law, and the Law Court is particularly clear in its rejection of retroactive legislation that purports to affect existing substantive or contractual rights upon which a party has reasonably relied. Maine case law recognizes that retroactive legislation that impairs contractual obligations is void. The Maine Law Court has continuously and clearly distinguished retrospective or retroactive legislation that permissibly only alters a remedy with respect to the redress of existing contractual or property rights while uniformly, consistently, and continually rejecting any retroactive legislation that impairs those rights of contract or those vested rights of property. "The power of the Legislature…to enact retroactive measures is limited. For example, in Maine the Legislature may enact statutes retroactively affecting remedies but not substantive rights." *Op. of Justices*, 370 A.2d 654, 668 (Me. 1977)(citing *generally, Morris v. Goss*, 147 Me. 89, 83 A.2d 556 (1951)). There is no serious basis for suggesting that this is merely an adjustment of remedy that leaves undisturbed the fundamental contractual rights of the parties. Indeed, it does not alter the remedy all; it affects only the contractual duties and rights of the parties to each contract. This is the uncompensated enlargement of the duties of one party and a windfall expansion of the rights of the counterparty in a very large number of transactions in which the very point of the contract is to identify an insured risk and price the risk to set a premium that is the basis of the bargain. It is difficult to envision proposed legislation that could more starkly and more egregiously interfere with the obligations of existing contracts or oust vested property rights without just compensation or violate the most fundamental norms of due process.

- In *Merrill v. Eastland Woolen Mills, Inc.*, 430 A.2d 557 (Me. 1981), the Law Court found that a post-event statutory change to a procedure used to enforce a right was permissible because it only affected enforcement of claims arising from certain acts or events. "The limitation had been on the pursuit of the remedy, not on the creation of the substantive right." *Id.* at 560-61. As to substantive rights, the Court noted that the legislature "has no constitutional authority to enact retroactive legislation if its implementation impairs vested rights or imposes liabilities that would result from conduct pre-dating the legislation." *Id.* at 560 n.7.

- In *Finch v. State*, 1999 ME 108, 736 A.2d 1043, the Law Court held that a retroactive criminal appeals statute did not deprive prisoners of due process for habeas corpus actions because they had a full year within which to file a petition and address their rights prior to the effectiveness of the change. Importantly, the Court noted that a "statute that purports to extinguish the existing rights of a claimant without affording a reasonable opportunity for the exercise of those rights, may be held to be 'an unlawful attempt to extinguish rights arbitrarily…'" *Id.* at ¶ 10 (quoting *Texaco, Inc. v. Short*, 454 U.S. 516, 527 n.21, 70 L. Ed. 2d 738, 102 S. Ct. 781 (1982)).

- In *Atlantic Oceanic Kampgrounds, Inc. v. Camden Nat'l Bank,* 473 A.2d 884, 891 (Me. 1984), Justice Glassman's concurrence highlighted that a statute could not retroactively change a mortgage contract's provisions related to foreclosure because the contractual impairment was substantial.

- In *Portland Sav. Bank v. Landry*, 372 A.2d 573, 579 (Me. 1977), the Law Court found that a statute unconstitutionally affected the time of a mortgagee's right of redemption when it applied to "mortgages which were executed prior to the effective date of that statute, unless the mortgage contained language permitting foreclosure under any legal method existing at the time the mortgage became in default." The Court reiterated that the legislature "cannot impair rights or obligations" under a contract, and when a statute "lessens the value of a contract to the parties, the constitutional prohibitions has been violated." *Id.* at 576, 77 (citing *Kennebec & Portland R.R.Co. v. Portland & Kennebec R.R.Co.*, 59 Me. 9, 38-39 (1871).

- In *Hoag v. Dick*, 2002 ME 92, 799 A.2d 391, the Law Court found that the provisions of the Uniform Premarital Agreement Act could not be retroactively applied to a divorce agreement, because doing so "would interfere with the contract and violate the Maine Constitution." *Id.* at ¶ 10.

Any legislative attempt to rewrite existing property and casualty insurance policies to require the insurers to cover COVID-19 business interruption losses is bound to be void under Maine law as well as federal law. The property and casualty insurance companies relied on existing law in writing their policies and determining the coverage provided, the premium charged, and the reserves required to cover the risks they insured. They relied on the validity under existing law of the contract terms in their policies: those very contract terms were specifically approved by the Bureau of Insurance, including the exclusion of exactly this coverage. The U.S. and Maine Constitutions prohibit legislation to retroactively change the terms of insurance contracts to cover claims that are not covered and for which no premium was collected and, thereby, create immense potential liabilities that did not exist at the time the insurance companies issued the policies to their insureds. Placing the financial burden of the COVID-19 pandemic on property and casualty insurers whose policies expressly do not cover such losses would be substantially unfair to the insurers and will not stand up to judicial scrutiny.

THIS ENDORSEMENT CHANGES THE POLICY. PLEASE READ IT CAREFULLY.

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.

   □

2021 WL 858378
Only the Westlaw citation is currently available.
United States District Court, D. Massachusetts.

Legal Sea Foods, LLC, Plaintiff,

v.

Strathmore Insurance Company, Defendant.

Civil Action No. 20-10850-NMG
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Filed 03/05/2021

MEMORANDUM & ORDER

Nathaniel M. Gorton United States District Judge

***1** This case arises out of a dispute between Legal Sea Foods, LLC ("Legal") and Strathmore Insurance Company ("Strathmore") over insurance coverage for business interruption losses suffered by the insured during the COVID-19 pandemic. Pending before the Court is defendant's motion to dismiss plaintiff's second amended complaint.

I. Factual Background

Legal is a seafood restaurant chain that owns and operates dozens of restaurants in the eastern United States. Thirty-two of its restaurants located in Massachusetts, the District of Columbia, New Jersey, Pennsylvania, Rhode Island and Virginia ("the Designated Properties") are covered by a commercial property insurance policy ("the Policy") issued by Strathmore for a one-year term beginning on March 1, 2020.

The Policy provides for Business Income (and Extra Expense) Coverage for income lost and expenses incurred during a necessary "suspension" of operations caused by "direct physical loss of or damage to" the Designated Properties. The loss or damage must also be caused by or result from a "Covered Cause of Loss," which is defined in the Policy as a "Risk[ ] Of Direct Physical Loss unless the loss is: [excluded] or [limited]." The Policy also provides additional coverage for business income losses and expenses that are "caused by action of civil authority that prohibits access" to the Designated Properties when a Covered Cause of Loss "causes damage to property other than" the Designated Properties as long as two additional conditions are met.

During the term of the Policy, state and local governments nationwide issued various orders in response to the COVID-19 pandemic ("the Orders"). The Orders mandated, inter alia, that residents remain in their residences unless performing certain essential activities and temporarily prohibited on-premises dining at restaurants.

In late March, 2020, Legal submitted a claim to Strathmore seeking insurance coverage under the Policy for its business interruption losses purportedly caused by the Orders. Although the substance of each Order varies by state and locality, Legal alleges that the Orders caused many of its restaurants to close or required it to limit guest capacity and to install protective barriers to reduce the spread of the virus. Legal declares that it has experienced a significant adverse impact on its business even where its restaurants have been permitted to continue delivery and take-out operations. It also avers that the virus has been physically "present" at its restaurants, outlining a "handful of examples" of individuals who were known, or suspected, to be infected at various Designated Properties.

Following an investigation of plaintiff's claim, which Legal purports consisted of a single, brief telephone call, Strathmore denied the claim. It also denied a subsequent request by Legal to reconsider its coverage determination.

II. Procedural Background

Plaintiff filed its complaint against defendant in this Court on May 4, 2020, alleging two counts of breach of contract and one count seeking a declaratory judgment. It filed its first amended complaint ("FAC") on June 5, 2020, in which it added a claim for a violation of M.G.L. c. 93A ("Chapter 93A").

***2** Defendant filed its motion to dismiss the FAC pursuant to Fed. R. Civ. P. 12(b)(6) on June 19, 2020, which plaintiff timely opposed.

In September, 2020, plaintiff moved for leave to file a second amended complaint ("SAC"), which this Court allowed the following month. In the SAC, Legal alleges the same four counts as in the FAC: breach of contract for failure to pay business interruption and extra expense coverage (Count I); breach of contract for failure to pay civil authority coverage (Count II); unfair or deceptive acts or practices in violation

of Chapter 93A; and declaratory judgment (Count IV). Legal also alleged the actual presence of the COVID-19 virus at the Designated Properties and the purported resulting damage.

The parties subsequently filed short, supplemental memoranda in support of their positions with respect to the motion to dismiss.

III. Motion to Dismiss

A. Legal Standard

To survive a motion to dismiss, a claim must contain sufficient factual matter, accepted as true, to "state a claim to relief that is plausible on its face." Bell Atl. Corp. v. Twombly, 550 U.S. 544, 570 (2007). In considering the merits of a motion to dismiss, the Court may only look to the facts alleged in the pleadings, documents attached as exhibits or incorporated by reference and matters of which judicial notice can be taken. Nollet v. Justices of Trial Court of Mass., 83 F. Supp. 2d 204, 208 (D. Mass. 2000), aff'd, 228 F.3d 1127 (1st Cir. 2000).

Furthermore, the Court must accept all factual allegations in the claim as true and draw all reasonable inferences in the claimant's favor. Langadinos v. Am. Airlines, Inc., 199 F.3d 68, 69 (1st Cir. 2000). If the facts in the claim are sufficient to state a cause of action, a motion to dismiss must be denied. See Nollet, 83 F. Supp. 2d at 208.

Although a court must accept as true all the factual allegations in a claim, that doctrine is not applicable to legal conclusions. Ashcroft v. Iqbal, 556 U.S. 662 (2009). Threadbare recitals of legal elements which are supported by mere conclusory statements do not suffice to state a cause of action. Id.

B. Application

The instant dispute, like many others to have been adjudicated across the country in recent months, primarily turns on the meaning of the phrase "direct physical loss of or damage to" property, which is a prerequisite to coverage under the business income and extra expense provisions of the Policy.

The interpretation of an insurance policy is a question of law. See Ruggerio Ambulance Serv. v. Nat'l Grange Mut. Ins. Co., 430 Mass. 794, 797 (2000). The parties agree, and this Court concurs, that Massachusetts law governs the interpretation of the Policy and under Massachusetts law, courts are to

> construe an insurance policy under the general rules of contract interpretation, beginning with the actual language of the polic[y], given its plain and ordinary meaning.

Easthampton Congregational Church v. Church Mut. Ins. Co., 916 F.3d 86, 91 (1st Cir. 2019) (internal citation omitted).

Although ambiguous words or provisions must be resolved against the insurer, id. at 92,

> provisions [that] are plainly and definitely expressed in appropriate language must be enforced in accordance with [the policy's] terms.

***3** High Voltage Eng'g Corp. v. Fed. Ins. Co., 981 F.2d 596, 600 (1st Cir. 1992) (internal citation omitted).

1. Breach of Contract – Business Income & Extra Expense Coverage (Count I)

Strathmore contends that Count I should be dismissed because Legal cannot plead facts sufficient to show "direct physical loss of or damage to" property at any of the 32 Designated Properties. Legal rejoins, however, that its allegations in the SAC, namely that COVID-19 was present on its properties and caused physical loss or damage to those properties resulting in the suspension of its operations, are more than enough to survive dismissal at this stage.

First, Legal does not plausibly allege that its business interruption losses resulted from the presence of COVID-19 at the Designated Properties. Instead, it indicates in the SAC that "[t]he Orders caused and are continuing to cause" the losses for which it claims entitlement to coverage.

Second, even if Legal had properly alleged that COVID-19 caused business interruption losses due to its presence at the Designated Properties, it would not be entitled to coverage under the Policy. Courts in Massachusetts have had occasion to interpret the phrase "direct physical loss" and have done so narrowly, concluding that it requires some kind of tangible, material loss. See, e.g., Harvard St. Neighborhood Health Ctr., Inc. v. Hartford Fire Ins. Co., No. 14-13649-JCB, 2015 U.S. Dist. LEXIS 187495, at *18 (D. Mass. Sept. 22, 2015) ("Intangible losses do not fit within th[e] definition [of 'direct physical loss']."); Crestview Country Club, Inc. v. St. Paul Guardian Ins. Co., 321 F. Supp. 2d 260, 264-65 (D. Mass. 2004) (collecting cases). Accordingly, the plain meaning of "direct physical loss"

> require[s] some enduring impact to the actual integrity [of the insured premises and] does not encompass transient phenomena of no lasting effect.

SAS Int'l, Ltd. v. General Star Indem. Co., No. 1:20-cv-11864, 2021 U.S. Dist. LEXIS 31093, at *10 (D. Mass. Feb. 19, 2021).

The COVID-19 virus does not impact the structural integrity of property in the manner contemplated by the Policy and thus cannot constitute "direct physical loss of or damage to" property. A virus is incapable of damaging physical structures because "the virus harms human beings, not property." Wellness Eatery La Jolla LLC v. Hanover Ins. Grp., No. 20cv1277, 2021 U.S. Dist. LEXIS 23014, at *16 (S.D. Cal. Feb. 3, 2021). The presence of the virus at insured locations

> would not constitute the direct physical loss or damage required to trigger coverage under the Policy because the virus can be eliminated. The virus does not threaten the structures covered by property insurance policies, and can be removed from surfaces with routine cleaning and disinfectant.

Terry Black's Barbecue, LLC v. State Auto. Mut. Ins. Co., No. 1:20-CV-665, 2020 U.S. Dist. LEXIS 234939, at *20 (W.D. Tex. Dec. 14, 2020) (also observing that "[p]laintiffs have not pled any facts showing that the coronavirus caused physical loss, harm, alteration, or structural degradation to their property").

***4** Many other courts have concluded likewise and have dismissed complaints containing similar allegations. See, e.g., SAS Int'l, Ltd., 2021 U.S. Dist. LEXIS 31093, at *8 n.4 (D. Mass. Feb. 19, 2021) ("[N]o reasonable construction of the phrase 'direct physical loss,' however broad, would cover the presence of a virus."); Uncork & Create LLC v. Cincinnati Ins. Co., 2020 U.S. Dist. LEXIS 204152, at *13-14 (S.D.W. Va. Nov. 2, 2020) (stating that "even actual presence of the virus would not be sufficient to trigger coverage for physical damage or physical loss to the property [and] the pandemic impacts human health and human behavior, not physical structures"); Pappy's Barber Shops, Inc. v. Farmers Grp., Inc., No. 20-CV-907-CAB-BLM, 2020 U.S. Dist. LEXIS 182406, at *2-3 (S.D. Cal. Oct. 1, 2020) (denying motion for leave to amend the complaint to include allegations that COVID-19 was present on plaintiffs' premises because "the presence of the virus itself ... do[es] not constitute direct physical loss[ ] of or damage to property").

Legal attempts to distinguish the SAC from the cited cases but overstates the cogency of its allegations and the utility of purportedly supporting caselaw. Many of the decisions cited by Legal have subsequently been distinguished or refuted. For instance, Legal relies on the decisions in Essex Ins. Co. v. BloomSouth Flooring Corp., 562 F.3d 399 (1st Cir. 2009) and Matzner v. Seaco Ins. Co., No. 96-0498-B, 1998 Mass. Super. LEXIS 407 (Mass. Super. Aug. 12, 1998) for the proposition that a virus can cause physical damage. Another session of this Court addressed those cases, however, and held that COVID-19 fundamentally differs from the unpleasant odors and fumes at issue in those cases. See SAS Int'l, Ltd., 2021 U.S. Dist. LEXIS 31093, at *7-8.

Similarly, Legal has brought to the Court's attention the oft-cited decisions in Studio 417, Inc. v. Cincinnati Ins. Co., 478 F. Supp. 3d 794 (W.D. Mo. 2020) and Blue Springs Dental Care, LLC v. Owners Ins. Co., No. 20-CV-00383-SRB, 2020 U.S. Dist. LEXIS 172639 (W.D. Mo. Sept. 21, 2020) to demonstrate that dismissal is inappropriate. Multiple courts have considered those decisions of United States District Judge Stephen Bough and have found them to be outliers. See SAS Int'l, Ltd., 2021 U.S. Dist. LEXIS 31093, at *10-11 n.8 (observing that "courts have either tiptoed around [the] holding [in Studio 417, Inc.], criticized it, or treated it as the minority position); Cafe Plaza De Mesilla, Inc. v. Cont'l Cas. Co., No. 2:20-cv-354, 2021 U.S. Dist. LEXIS 29163 (D.N.M. Feb. 16, 2021) ("Blue Springs Dental Care, LLC, represents an outlier case and [ ] the weight of recent authority, created by the deluge of coronavirus-related insurance disputes, favors [the insurer's] position in almost uniformly rejecting [the insured's] reasoning."). It is clear that the weight of legal authority supports dismissal of Count I.

Legal also attempts to avoid dismissal of Count I by contending that Strathmore chose not to include a specific virus exclusion in the Policy. That argument is, however, unavailing. The "absence of an express [virus] exclusion does not operate to create coverage" for pandemic-related losses. SAS Int'l, Ltd., 2021 U.S. Dist. LEXIS 31093, at *9 (quoting Given v. Commerce Ins. Co., 440 Mass. 207, 212 (2003)). Under the express terms of the relevant provision of the Policy, Legal was entitled to coverage only for losses resulting from "direct physical loss of or damage to" the Designated Properties and the absence of a virus exclusion does not insinuate the expansion of such coverage.

Accordingly, Count I of the complaint will be dismissed.

2. Breach of Contract – Civil Authority Coverage (Count II)

***5** Strathmore also seeks dismissal of Legal's claim of breach of contract for failure to provide coverage under the civil authority provision.

That provision of the Policy requires Strathmore to pay for Legal's business interruption losses resulting from an action of civil authority only if that action "prohibits access" to the Designated Properties. Many courts that have addressed equivalent civil authority provisions have drawn a clear line between actions that "prohibit" access to insured properties and those that merely "limit" such access. See, e.g., Riverside Dental of Rockford, Ltd. v. Cincinnati Ins. Co., No. 20 CV 50284, 2021 U.S. Dist. LEXIS 20826, at *12-13 (N.D. Ill. January 19, 2021) (dismissing claim for civil authority coverage because the relevant government orders "did not forbid or prevent the ability to enter" the insured premises but rather "limited the types of services that could be provided"); Brian Handel D.M.D., P.C. v. Allstate Ins. Co., No. 20-cv-3198, 2020 U.S. Dist. LEXIS 207892, at *9-10 (E.D. Pa. Nov. 6, 2020) (dismissing claim for civil authority coverage because "the [Pennsylvania COVID-19] orders limit, rather than prohibit, access to the property"); Sandy Point Dental, PC v. Cincinnati Ins. Co., No. 20-cv-2160, 2020 U.S. Dist. LEXIS 171979, at *7-8 (N.D. Ill. Sept. 21, 2020) (dismissing claim for civil authority coverage because "coronavirus orders have limited plaintiff's operations, [but] no order issued in Illinois prohibits access to plaintiff's premises").

Although Legal alleges that the Orders mandated the closure of and prohibited access to some of its insured restaurants, plaintiff fails to identify any specific Order that expressly and completely prohibited access to any of the Designated Properties. In fact, Legal acknowledges in both the SAC and its memoranda opposing the instant motion that the Orders permitted its restaurants to continue carry-out and delivery operations. Consequently, Legal cannot establish a necessary prerequisite of coverage under the civil authority provision of the Policy. See 4431, Inc. v. Cincinnati Ins. Cos., No. 5:20-cv-04396, 2020 U.S. Dist. LEXIS 226984, at *32 (E.D. Pa. Dec. 3, 2020) ("Plaintiffs' ability to continue limited takeout and delivery operations at the premises precludes coverage under the Civil Authority provision: a prohibition on access to the premises, which is a prerequisite to coverage, is not present.").

To the extent Legal suggests that dismissal of its civil authority coverage claim is inappropriate because it would have suffered greater financial loss by keeping its restaurants open for carry-out and delivery services, it does so in vain. It is immaterial whether it is economically feasible for Legal to continue restaurant operations solely for carry-out and delivery sales. Rather, the relevant inquiry is whether the Orders prohibited access to the Designated Properties, which they clearly did not for the reasons stated above.

Because the Orders limit, rather than prohibit, access to the Designated Properties, Legal is not entitled to civil authority coverage under the Policy and Count II of the complaint will be dismissed.

3. Chapter 93A Claim (Count III)

***6** Strathmore seeks to dismiss Legal's Chapter 93A claim, which is based on the allegedly unfair and deceptive investigation and denial of Legal's claim to insurance coverage.

Chapter 93A prohibits "[u]nfair methods of competition and unfair or deceptive acts or practices in the conduct of any trade or commerce," M.G.L. c. 93A, § 2(a). In the insurance context, specifically, an insurer does not violate Chapter 93A in denying coverage "so long as [it] made a good faith determination to deny coverage" even if the insurer's interpretation of the policy was incorrect. Ora Catering, Inc. v. Northland Ins. Co., 57 F. Supp. 3d 102, 110-11 (D. Mass. 2014). Furthermore,

> [w]hen coverage has been correctly denied ... no violation of the Massachusetts statutes proscribing unfair or deceptive trade practices may be found.

Harvard St. Neighborhood Health Ctr., Inc. v. Hartford Fire Ins. Co., No. 14-13649-JCB, 2015 U.S. Dist. LEXIS 187495, at *24 (D. Mass. Sept. 22, 2015) (quoting Transamerica Ins. Co. v. KMS Patriots, 52 Mass. App. Ct. 189, 197 (2001)).

The Court has concluded that Strathmore correctly denied coverage under the Policy. Therefore, dismissal of the Chapter 93A claim is warranted.

4. Declaratory Judgment (Count IV)

Finally, Strathmore contends that Count IV, which seeks a declaratory judgment that the Policy covers Legal's claim and that no exclusion applies to bar or limit coverage for its claim, must also be dismissed.

Because the Court has determined that Legal has failed to plead facts sufficient to demonstrate that it is entitled to coverage under the Policy, dismissal of Count IV is appropriate.

ORDER

For the foregoing reasons, the motion of defendants to dismiss plaintiff's complaint (Docket No. 16) is **ALLOWED.**

So ordered.

All Citations

--- F.Supp.3d ----, 2021 WL 858378

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