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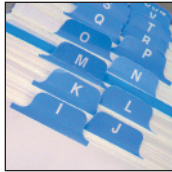
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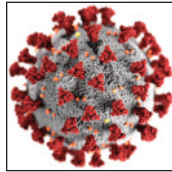


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**49** COVID 19 and Business Interruption Insurance for Small and Medium Businesses and Nonprofit Organizations

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# COVID 19 AND BUSINESS INTERRUPTION INSURANCE

## What Do Small and Medium Businesses and Nonprofit Organizations Need to Know to Make Informed Decisions?

By Craig R. Blackman and Corey S. D. Norcross, Stradley Ronon Stevens & Young, LLP

With the onset of COVID-19, attention has turned to business interruption (BI) insurance and the limits of its coverage for the economic damages caused by the pandemic. COVID-19's spread has caused governments to issue shut down orders that, while flattening the curve of virus transmissions, has also shuttered businesses and damaged national and local economies. With all the buzz and conflicting commentaries on BI, small and medium businesses and nonprofit organizations should prepare to work with their lawyers, board members, consultants, and trusted constituents to determine the availability of such coverage.

### BI Coverage Basics

BI coverage has long been an important component of most commercial insurance coverage programs, including those purchased by small and medium businesses and nonprofit organizations. The coverage is generally included under most package policies for such businesses, or as an endorsement to a property insurance policy. BI is a specialized form of first-party insurance designed to cover a business for lost income arising from the inability to continue its normal operations and functions. To trigger BI coverage, a claimed loss generally must result directly from a specified peril which causes damage to a specified property at a particular location. It is intended to compensate a company for income it would have earned had a covered loss event not taken place.

The types of losses commonly covered by BI insurance include:

- **Business Income.** This replaces income that would otherwise have been earned by the business had no loss taken place. Operating expenses, like electricity and phone, as well as employee salaries, may also be covered;
- **Extra Expense.** This pays for certain types of expenses necessarily incurred by the insured during the restoration for the property out of which the business interruption arose in order to get running again;
- **Contingent Business Interruption.** This is an extension of coverage designed to cover loss of income due to property loss at a key supplier or customer location; and,
- **Civil Authority.** This provides coverage for loss of business income and extra expense sustained as a result of governmental denial of access to the insured's property. *This component is the one most at issue from COVID-19 business closures and related income losses, and will be discussed in greater length below.*

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## COVID 19 BUSINESS INTERRUPTION INSURANCE

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### Triggers for BI Coverage

Simply having BI coverage is only the beginning of the analysis. The next step is to determine whether the coverage applies to a particular situation. While such coverage is contractual in nature, and thus likely to turn on the specific terms of the policy, there are general rules that apply in most instances.

The typical BI policy requires that the loss result: (1) directly from (2) a specified peril which causes damage to a (3) specified property (4) at a particular location. The interruption must also be: (5) reasonably limited in duration and must (6) occur within a particular time frame. As goes almost without saying, virtually all policies require that (7) the interruption of business be necessary. And finally: (8) the subject loss must not be subject to any policy exclusions, such as the virus exclusion added to most BI policies following the SARS episode nearly a decade and a half ago.

In order to trigger BI coverage, there typically must be some actual damage to or loss of covered physical property. The nature and extent of physical damage necessary to trigger BI coverage is a particular area of dispute between insureds and insurers in a COVID-19 claim setting. Also, depending upon the particular policy language at issue, courts generally limit BI coverage to losses resulting from damage or destruction to the particular location (or contingent location) listed or described in the policy. This might include contingent BI coverage for physical damage occurring at property other than the insured's, such as an insured's supplier and/or customer location. Of course, whether physical damage has occurred at the appropriate location to trigger coverage is also a disputed issue in COVID-19 claims.

The essential questions raised by insureds in many COVID-19 BI claims are: is there actual property damage to a covered physical property (or contingent location) as a result of a prophylactic

government closure order in the absence of any actual virus infection at that business; and, if there is an actual virus infection at the affected location, is that physical damage triggering BI coverage?

### BI Litigation Developments

Businesses experiencing financial losses due to disruption arising from the COVID-19 pandemic moved quickly to make claims for BI coverage. Many of these claims have been denied on multiple grounds, including the absence of damage to or destruction of a covered property and the application of a virus exclusion (a virus exclusion was added to most BI policies following the SARS outbreak nearly a decade and a half ago). Numerous for-profit and nonprofit entities have commenced litigation challenging the coverage determinations made by their insurers. Some of these entities have sought to accelerate or consolidate such claims through class action litigation or other procedural devices that seem neither feasible nor appropriate to resolve BI claims for a multitude of substantive and procedural issues.

### BI Legislative Efforts

While affected organizations and the insurance industry grapple with the current wave of COVID-19 BI claims, state and federal legislatures are also attempting to address such claims. At the Federal level, Congress is in the early stages of working on a bill that would establish a Federal reimbursement program for COVID-19 related coverage losses. The proposed legislation, currently named the Pandemic Risk Insurance Act of 2020 ("PRIA"), is modeled on the Terrorism Risk Insurance Act ("TRIA"), which provides an umbrella of federal reimbursement for excessive terrorism-related losses to insurers offering coverage for those risks. PRIA would provide compensation for BI losses resulting from COVID-19 when the losses paid by the insurers who participate in the program exceed



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\$250 million, but with cap of \$500 billion in any calendar year. As with TRIA, participating insurers would be charged an annual premium for this federal backstop for covered losses that exceed the \$250 million cap.

While potentially helpful to some, PRIA, as a practical matter, may be a band-aid on a lost limb. According to experts from the American Property Casualty Insurance Association, the estimated economic toll of COVID-19 business interruption losses due to government closure orders in the United States may be between \$220 billion and \$383 billion *per month* for small businesses, and the insurance industry could see as many as 30 million COVID-19 claims from such organizations.

Several states are also attempting to tackle the issue of COVID-19 coverage under BI policies. For example, some states are considering legislation that would require insurers to provide COVID-19 related BI coverage, even if it would negate the terms, conditions, provisions, and exclusions of an existing policy. Should such legislation pass, constitutional challenges are expected. For example, insurers may look to Article 1, Section 10 of the U.S. Constitution, otherwise known as the Contracts Clause, which provides that a State is not allowed

to pass any law that "impairs the obligation of contracts." Challenges based on state constitutional provisions also are expected to ensue.

Other states are taking a different approach. For example, there is draft legislation in Pennsylvania that purports to legislatively interpret key BI policy language in a way that would potentially force coverage for COVID-19 losses. At its heart, the draft legislation would determine that the "direct physical loss, damage, or injury to tangible property" generally required to trigger BI coverage includes the presence of the COVID-19 virus in the subject building, office, retail space, structure, plant, facility, commercial establishment, or other business activity area. The draft legislation further proposes very broadly that the presence of the virus in the affected location can be established by the insured's showing that an infected person was present or the virus was otherwise detected in either the business itself or in the municipality in which it is located. The draft legislation also provides that the March 19, 2020, Closure Order issued by the Pennsylvania Governor is a civil authority order issued due to physical damage at or in the near vicinity of the businesses impacted by that Order.

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## COVID 19 BUSINESS INTERRUPTION INSURANCE

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### Conclusion

The current state of BI coverage issues raised by COVID-19 is very much in flux. Unfortunately, litigation and legislation are unlikely to resolve these questions anytime soon. Such processes are inherently lengthy and could last years.

For that reason, it is important for small and medium businesses and nonprofit organizations to understand now whether they have BI coverage and determine the scope of any such coverage in consultation with experienced insurance industry professionals. Given the developments that are certain to occur in the coming days, weeks, and months, both in courts and in legislative chambers, you should remain in contact with your professional advisors as these processes play out. These entities should undertake these efforts even if there are questions regarding BI coverage for COVID-19 losses. Because of the unprecedented nature of the COVID-19 pandemic and the extraordinary efforts that have already been undertaken to address it, the possibility exists that coverage may become available as litigation and legislative efforts evolve.

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