

CLIENT ALERT

Insurers Keeping a Watchful Eye on Diverse Losses from Coronavirus Outbreak

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As authorities react to the Coronavirus outbreak originating from Wuhan, China, and its growing impact on world health, individual corporations and industries as a whole also are moving to mitigate any potential impact this health crisis may have on their business operations. Many major corporations have acted to protect staff by temporarily shuttering operations in China and advising against travel to the area.¹ⁱ Retailers and other consumer-facing entities have temporarily closed store fronts in affected areas to minimize the spread of the virus.²ⁱⁱ These interruptions to normal business operations are serious, and have real financial implications for individual companies and the economy. Global financial markets already have reacted to the ripple moving through international trade routes as a result of factory shutdowns and new regulations stopping or slowing the movement of goods out of China and the surrounding nations.³ⁱⁱⁱ

Along with the direct business losses suffered in the immediate area of the outbreak, corporations and their insurers must take care to evaluate additional exposures several steps removed from Wuhan, including those felt outside China and beyond the region. Following the international community's quick reaction to halt the spread of the virus, for instance, U.S. and European-based businesses are facing restrictions on international travel and disruptions in supply chains,^{4iv} reflecting how heavily international companies and markets depend on Chinese manufacturing and consumer markets in support of profitable revenue.^{5v} With some estimates projecting the health impact of the virus will be felt well into Q2 of 2020, companies and insurers will continue to feel the economic effects of shuttered operations and the anticipated delay of Chinese imports/exports well into the future.

Companies impacted financially by the Coronavirus likely will look to their insurers to recover. Much like other globally felt disasters and crises, the Coronavirus outbreak and resulting losses will give rise to important insurance coverage issues, particularly over recovery for business income losses. Insurers will need to evaluate resulting claims carefully in light of the scope of insuring agreements, operation of exclusions, conditions and limitations in the policy, and the facts of each claim.

Commercial policyholders will likely point to "business interruption" or "contingent business interruption" coverage in making a claim for recovery of their lost business income. While business interruption coverage addresses lost profits caused by damage to the policyholder's own property, contingent business interruption coverage addresses a policyholder's losses resulting from interruption of suppliers' or customers' business because of damage to their property. A threshold issue is therefore a determination about whether there has been any damage to an insured's property, or whether only indirect losses are at stake.

Further, insurance policies at issue may contain exclusions that preclude coverage. There can be no coverage for lost business income if the policy excludes coverage, even if the lost income resulted from damage to property. For example, common exclusionary language included in event cancellation and contingency policies precluding coverage for loss stemming from "communicable disease" or similar events, may apply here.

Courts have addressed disputes concerning more tangible, property-based business interruption losses and those rulings may be instructive. In a 2004 ruling in *City of Chicago v. Factory Mutual Insurance Co.*, a federal judge ruled that there was no coverage for business interruption losses by Chicago's airports from the 2001 Federal Aviation Administration order to halt all flights because the policy excluded coverage for "indirect or remote loss or damage." The 1972 U.S. Court of Appeals for the Seventh Circuit ruling in *Diamond Shamrock Corp. et al. v. Lumbermens Mutual Casualty Co.*, held that the insured had no right to recover its business interruption loss because the damage was caused by fire, a risk expressly excluded in the business interruption policy.

Besides the exclusions, there are other important policy terms that will determine whether coverage is available for claims for business losses arising from the Coronavirus. A key point is that, as courts have consistently recognized, a covered damage to or loss of physical property is necessary for business interruption coverage to exist. For business interruption coverage, the damage must be to the property of the insured or, for contingent business interruption coverage, to the property of a supplier or customer. If a supplier or customer is not named, the cover may be subject to a sub-limit.

Of particular import here is the precedent recognizing that losses may result from embargoes, logistical difficulties or other circumstances that do not constitute damage to or loss of physical property. A leading ruling on this point is the 2006 decision by the U.S. Court of Appeals for the Eighth Circuit in *Source Food Technology Inc. v. U.S. Fidelity & Guaranty Co.*, which established that there was no "direct physical loss to property" within the meaning of "business income" or "action by civil authority" coverage provisions when an embargo against Canadian beef rendered beef bought by the policyholder unshippable to United States, even though the beef was not contaminated or damaged in any way.^{6vi}

In the case of the Coronavirus, both the Chinese and other governments have restricted certain operations, travel, as well as imports and exports. For this reason, some commercial policyholders may look to the civil authority provisions in their policies for lost income and extra expense coverage. Civil authority provisions may cover loss of business income and necessary extra expenses caused by civil authorities prohibiting access to the insured premises, whereas an ingress/egress provision may cover loss of business income when access to the policyholder's premises is prevented.

Civil authority coverage has significant prerequisites, however. In *Dickie Brennan & Co. Inc. v. Lexington Insurance Co.*, the U.S. Court of Appeals for the Fifth Circuit explained: "The general rule is that civil authority coverage is intended to apply to situations where access to an insured's property is prevented or prohibited by an order of civil authority issued as a direct result of physical damage to other premises in the proximity of the insured's property."^{7vii} In some policies, civil authority coverage terms may be broader, without the requirements addressed in *Dickie Brennan*.

In the 2003 Fifth Circuit ruling in *730 Bienville Partners Ltd. v. Assurance Co. of America*, the court found the FAA's closure of airports after Sept. 11, 2001 did not "prohibit access" to the policyholder's hotels as required under the clause and the FAA did not "prevent" customers from going to the hotels.^{8viii} Another ruling on this point, the 2003 New York Supreme Court Appellate Division decision in *54th St. Ltd. Partners L.P. v. Fidelity & Guaranty Insurance Co.*, said "vehicular and pedestrian traffic in the area was diverted, (but) access to the restaurant was not denied," meaning no recovery for the policyholder.^{9ix}

Here, restrictions imposed by the company itself, absent a directive from a civil authority, would not support civil authority coverage. Coverage for business income losses from a civil authority order or directive would not generally exist without action by an authority that specifically barred access to an insured's property. Similarly, an ingress/egress provision does not afford

coverage if access to the insured premises is still possible, even though a company may have seen a significant diminution in its business. The viability of a claim based on the prohibitions imposed by Chinese authorities and others in response to the Coronavirus will depend on the presence and application of policy terms such as these.

Some international corporations impacted by the health crisis may have manuscripted or special policies written to address risks inherent in certain unique settings like those presented by the Coronavirus. As the number and severity of international health crises have grown, some insureds have undoubtedly sought special protections from the insurance market for related losses. On the other hand, insurers have also become increasingly mindful of these losses and have begun to append exclusionary language addressing loss in connection with disease or similar occurrences.

Insurers will play an important role in the recovery from the Coronavirus health crisis. Insurers will need to investigate, process and pay valid claims from a wide variety of policyholders. Although many business losses may be insured, there also are important limitations on the scope of coverage afforded for business interruption and contingent business interruption losses.

¹ “Coronavirus: Technology giants join China shutdown”, <https://www.bbc.com/news/business-51276322> (accessed January 31, 2020); “Coronavirus: Key Issues for Employers”, Crowell & Moring LLP: Alerts and Newsletters, January 31, 2020, <https://www.crowell.com/NewsEvents/AlertsNewsletters/all/Coronavirus-Key-Issues-for-Employers> (accessed February 4, 2020).

² “Coronavirus: Starbucks closes 2,000 Chinese branches”, <https://www.bbc.com/news/business-51276317> (accessed January 31, 2020).

³ James T. Areddy, “Coronavirus Closes China to the World, Straining Global Economy”, The Wall Street Journal, February 3, 2020, <https://www.wsj.com/articles/coronavirus-closes-china-to-the-world-straining-global-economy-11580689793> (accessed February 4, 2020);

⁴ “Coronavirus: DHS Announces New Travel Restrictions on Certain Inbound U.S. Flights and Travelers from China, Including Medical Screening and Quarantine”, Crowell & Moring LLP: Alerts and Newsletters, February 3, 2020, <https://www.wsj.com/articles/coronavirus-closes-china-to-the-world-straining-global-economy-11580689793> (accessed February 4, 2020)

⁵ Peter S. Goodman, “SARS Stung the Global Economy. The Coronavirus Is a Greater Menace”, February 3, 2020, <https://www.nytimes.com/2020/02/03/business/economy/SARS-coronavirus-economic-impact-china.html> (accessed February 4, 2020).

⁶ *Source Food Tech., Inc. v. U.S. Fid. and Guar. Co.*, 465 F.3d 834 (8th Cir. 2006)

⁷ *Dickie Brennan & Co., Inc. v. Lexington Ins. Co.*, 636 F.3d 683, 687 (5th Cir. 2011)

⁸ *730 Bienville Partners, Ltd. v. Assur. Co. of Am.*, 67 Fed.Appx. 248 (5th Cir. 2003)

⁹ *54th St. Ltd. Partners, L.P. v. Fid. and Guar. Ins. Co.*, 306 A.D.2d 67 (N.Y. 1st Dep't 2003)

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