

NOT FOR PUBLICATION

FILED

UNITED STATES COURT OF APPEALS

OCT 17 2022

FOR THE NINTH CIRCUIT

MOLLY C. DWYER, CLERK
U.S. COURT OF APPEALS

KARA MCCULLOCH, DMD, MSD, PLLC;
JAE Y. HONG, DDS, PS; JAE Y. HONG,
PLLC; NOSKENDA, INC.; PUYALLUP
ORAL AND MAXILLOFACIAL
SURGERY, LLC; OWENS DAVIES, PS,

Plaintiffs-Appellants,

v.

VALLEY FORGE INSURANCE
COMPANY; TRANSPORTATION
INSURANCE COMPANY; NATIONAL
FIRE INSURANCE COMPANY OF
HARTFORD,

Defendants-Appellees.

No. 21-35520

D.C. No. 2:20-cv-00809-BJR

MEMORANDUM*

Appeal from the United States District Court
for the Western District of Washington
Barbara Jacobs Rothstein, District Judge, Presiding

Argued and Submitted August 12, 2022
Submission Vacated August 19, 2022
Resubmitted October 13, 2022
Seattle, Washington

Before: BERZON, CHRISTEN, and FORREST, Circuit Judges.

* This disposition is not appropriate for publication and is not precedent except as provided by Ninth Circuit Rule 36-3.

Plaintiffs timely appeal the district court’s dismissal of their claims in this insurance coverage dispute with Defendants. We review de novo the order granting Defendants’ motion to dismiss for failure to state a claim on which relief can be granted, *Mudpie, Inc. v. Travelers Cas. Ins. Co.*, 15 F.4th 885, 889 (9th Cir. 2021); Fed R. Civ. P. 12(b)(6), and we affirm.

Plaintiffs own and operate small businesses in Washington State, and each holds an insurance policy issued by one of the Defendants.¹ Plaintiffs seek coverage under those insurance policies for economic losses incurred during the COVID-19 pandemic. Plaintiffs allege that Defendants breached the policies when they denied coverage of those losses. Plaintiff Owens Davies additionally asserts extracontractual claims, including bad faith, negligence, and violations of the Washington Consumer Protection Act (“CPA”), Wash. Code Rev. § 19.86, *et seq.*, and the Washington Insurance Fair Conduct Act (“IFCA”), Wash. Code Rev. § 48.30.015.

A. Contractual Claims

1. **Direct Physical Loss.** Plaintiffs allege that they are entitled to coverage for business losses resulting from “direct physical loss of or physical damage to” the insured properties. The Washington Supreme Court has foreclosed this

¹ Except as otherwise noted, the relevant language of the policies is the same for each of the Plaintiffs.

argument. While this appeal was pending, the Court held that, as a matter of contractual interpretation, “loss of intended use of property” and “loss of business income” resulting from the Governor’s COVID-19 orders do not qualify for insurance coverage as “direct physical loss of or damage to property.” *See Hill & Stout, PLLC v. Mut. of Enumclaw Ins. Co.*, 515 P.3d 525, 531-35 (Wash. 2022). “When interpreting state law, we are bound to follow the decisions of the state’s highest court” *Mudpie*, 15 F.4th at 889 (quoting *Diaz v. Kubler Corp.*, 785 F.3d 5 1326, 1329 (9th Cir. 2015)). Thus, Plaintiffs’ alleged loss of the use of their properties does not qualify as physical loss or damage.

2. Civil Authority. Plaintiffs also argue that they are entitled to coverage under a separate “civil authority” provision, which provides coverage when an “action of civil authority . . . prohibits access” to the insured’s premises due to “physical loss of or damage to property at locations, other than the insured premises.” Plaintiffs’ argument fails because the complaint includes no colorable allegation that the Governor entered his orders in response to any *physical* property damages. *See Hill & Stout*, 515 P.3d at 533 (explaining that there was no physical alteration of the covered property as a result of the COVID-19 pandemic, nor was the property “rendered unsafe or uninhabitable because of a dangerous physical condition”).

3. Business Income for Interruption of Practice. The policies of Plaintiffs

Owens Davies and Jae Y. Hong contain an additional “Business Income for Interruption of Practice” Endorsement (“Interruption Endorsement”), which modifies the coverage provided under the “Business Income and Extra Expense” Endorsement (“Business Income Endorsement”). The Business Income Endorsement provides coverage for loss of business income due to the suspension of operations caused by “direct physical loss of or damage to property” at the insured premises. The Interruption Endorsement “modifies” the Business Income Endorsement in two ways: (1) by providing two alternative methods for calculating the loss amount for a qualifying claim; and (2) by extending coverage for the inability to obtain drinkable water at the insured premises. Davies and Hong argue that the Interruption Endorsement abrogated the direct physical loss requirement, because the language of the Interruption Endorsement does not require physical damage for coverage.

Plaintiffs’ argument is unavailing. The Interruption Endorsement expressly states: “Except as otherwise stated in this endorsement, the terms and conditions of the policy apply to the insurance stated below.” Because the Interruption Endorsement does not state otherwise, it does not alter the requirements for coverage under the Business Income Endorsement, including the requirement that physical loss or damage be present. Instead, the Interruption Endorsement affects only the calculation of the loss amount for a claim that meets that requirement.

Because Plaintiffs have failed to allege direct physical loss or damage, the Interruption Endorsement has no application.

B. Extra-Contractual Claims

Davies additionally asserts that the district court erred by denying his extra-contractual claims for bad faith, negligence, and violations of the CPA and IFCA. The underlying allegations in the complaint as to these claims are the same; Davies asserts that his insurer unreasonably denied his claim for coverage and failed to conduct a reasonable investigation of the claim. To the extent Davies's claims are premised on an unreasonable denial of coverage, the allegations are dependent on first showing an erroneous denial of coverage. He has made no such showing. To the extent Davies's claims are premised on an unreasonable investigation, the allegations are insufficient because the insurer's denial of coverage was based on a legal interpretation of the policy. There was no need for factual investigation. The district court properly dismissed Davies's extracontractual claims.

AFFIRMED.