No. 21-1202

United States Court of Appeals
For the First Circuit

LEGAL SEA FOODS, LLC,

Plaintiff-Appellant,

v.

STRATHMORE INSURANCE CO.,

Defendant-Appellee.

ON APPEAL FROM A JUDGMENT OF THE UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF MASSACHUSETTS
CASE NO. 1:20-CV-10850-NMG
JUDGE NATHANIEL M. GORTON

BRIEF FOR UNITED POLICYHOLDERS AS *AMICUS CURIAE* IN SUPPORT OF APPELLANT AND REVERSAL OF THE DISTRICT COURT DECISION

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CORPORATE DISCLOSURE STATEMENT

United Policyholders ("UP") is a nonprofit, 501(c)(3) corporation and has no public ownership.

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STATEMENT OF INTEREST OF THE *AMICUS CURIAE*[1]

For nearly 30 years, the non-profit (501)(c)(3) United Policyholders ("UP") has been a source of insurance coverage and claim information and an advocate for the interests of individual and commercial insurance consumers throughout the entire United States. UP assists purchasers of insurance and those pursuing claims for loss indemnification. UP is routinely called upon to help policyholders secure paid-for benefits in the wake of large-scale national disasters such as floods, windstorms, and hurricanes and recently, pandemics. In the state of Massachusetts UP has assisted coastal property owners and purchasers of disability insurance and worked with the Division of Insurance on various matters.

Since March 2020 UP has been engaged in the critical effort to assist business owners around the country whose operations have been impacted by COVID-19 and public safety orders and present considerations to courts and regulators on the special rules of contract construction that are uniquely imperative in the context of insurance.

Commerce, government and society benefit when losses are indemnified through insurance purchased by individuals and businesses. The insurance system

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[1] The parties have consented to the filing of this brief. UP confirms that: (1) no party's counsel authored any part of this brief; (2) no party or party's counsel contributed any money to fund preparation of submission of this brief; and (3) no person, other than UP and UP's counsel, contributed any money to prepare or submit this brief.

is woven into the fabric of our economy through mandatory purchase requirements, prudent personal and business risk management and the pricing of goods and services. Each state regulates insurance contracts and transactions through its own set of laws and regulations, yet most insurers operate in multiple states. Because insurers must meet their own revenue objectives, plus the reasonable expectations of their policyholders, *plus* the demands of their investors and shareholders, judicial oversight is essential to maintain the purpose and value of insurance purchases by individuals and businesses.

Insurance policies are adhesive in nature and their language is increasingly less standardized. That means insurers are using far more creativity in drafting policy terms and conditions and exclusions and limitations than in the past. This has made it much harder for state insurance regulators to review those terms and limitations and determine whether they will effectuate or deprive the purchaser of the protection they intend to purchase. Compounding that challenge to state insurance regulators is that data mining, artificial intelligence and computerized risk modeling have made it literally impossible to give every new policy form the scrutiny it deserves.

Effectuating indemnification in case of loss despite these factors remains a fundamental economic and social objective that courts can advance. UP respectfully seeks to assist this Court in fulfilling these important roles.

UP serves on the Federal Advisory Committee on Insurance, which briefs the Federal Insurance Office and in turn, the U.S. Treasury Department. UP's Executive Director has been an official consumer representative to the National Association of Insurance Commissioners since 2009. In that role, UP assists regulators in monitoring policy language and claim practices through presentations and collaboration and the development of model laws and regulations.

UP gave three separate NAIC presentations in 2020 on the topic of coverage and claims for Business Interruption related to COVID-19 and public safety orders. The gist of UP's presentations was that there is evidence that insurers were not fully candid with regulators about the significance of virus and pandemic-related limitations and exclusions they added to their policies. Although insurers had paid business interruption losses from hotel reservation cancellations due to SARS, when they added limitations and exclusions after that event, some told regulators they had never paid virus-related losses and that therefore there would be no rate decrease associated with the policy language change. Because there was no rate decrease and no clear notice that virus and pandemic related losses could be excluded, commercial policyholders were not aware of insurers' efforts to drastically reduce business interruption loss protection until 2020. Because policyholders (including plaintiff in this case) had no notice of a potentially very substantial hole in their insurance,

they had no opportunity to cure the gap, hence the need for special judicial handling and careful scrutiny of this case.

Since 1991 UP has filed *amicus curiae* briefs in federal and state appellate courts across 42 states and in over 450 cases. *Amicus* briefs filed by UP have been expressly cited in the opinions of state supreme courts as well as the U.S. Supreme Court. *See Humana Inc. v. Forsyth*, 525 U.S. 299, 314 (1999); *Julian v. Hartford Underwriters Ins. Co.*, 110 P.3d 903, 911 (Cal. 2005); *Cont'l Ins. Co. v. Honeywell Int'l, Inc.*, 188 A.3d 297, 322 (N.J. 2018); *Allstate Prop. & Cas. Ins. Co. v. Wolfe*, 105 A.3d 1181, 1185-6 (Pa. 2014).

By submitting a brief in this matter, UP seeks to fulfill the classic role of *amicus curiae* in a case of general public interest, supplementing the efforts of counsel, and drawing the court's attention to law that escaped consideration. This is an appropriate role for *amicus curiae*. As commentators have often stressed, an *amicus* is often in a superior position to "focus the court's attention on the broad implications of various possible rulings." R. Stern, E. Greggman & S. Shapiro, Supreme Court Practice, 570-71 (1986) (quoting Ennis, *Effective Amicus Briefs*, 33 Cath. U.L. Rev. 603, 608 (1984)).

STATEMENT OF THE CASE

In the District Court, the policyholder restaurant chain sought Property and Business Income coverage for damage and loss caused by the COVID-19 pandemic at its 32 insured premises and orders of Civil Authority issued as a result of the pandemic stemming from SARS-CoV-2 and/or COVID-19, under an insurance policy that was sold by the defendant insurance company for a policy period that began on March 1, 2020.[2] Even though the insurer sold plaintiffs the subject insurance policy in the midst of the pandemic, *without a virus exclusion*, the District Court dismissed the case on the basis that the policyholder could not plead facts sufficient to show business interruptions resulting from "direct physical loss of or damage" to insured property.[3]

The District Court made multiple errors when dismissing the case prematurely. Rather than accepting the allegations of the pleading as true, the District Court made its own factual conclusions about the cause of the loss, the properties of the virus and the impact of the virus on property. The District Court reviewed Massachusetts authorities interpreting the phrase "direct physical loss"—and not the language at issue, being "direct physical loss of"—and wrongly concluded a "narrow" interpretation is required, including "some kind of tangible,

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2 Slip Op. at 1-2.

3 Slip Op. at 6-11.

material loss."[4] The court stated: "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.'"[5]

Even though prior Massachusetts authorities have understood that less tangible substances on or in properties such as odors can cause physical loss of or damage to property, including *Essex Insurance Co. v. BloomSouth Flooring Corp.*, 562 F.3d 399 (1st Cir. 2009) and *Matzner v. Seaco Insurance Co.*, No. 96-0498-B, 1998 Mass. Super. LEXIS 407 (Mass. Super. Aug. 12, 1998), the District Court disregarded those decisions, instead focusing on *SAS International, Ltd. v. General Star Indemnity Co.*, No. 1:20-cv-11864, 2021 U.S. Dist. LEXIS 31093, at *10 (D. Mass. Feb. 19, 2021). *SAS*, in turn, relied on the widely misinterpreted 10A COUCH ON INSURANCE § 148:46 as a so-called "leading insurance treatise."[6] The District Court then rejected more recent COVID-related coverage cases refusing to grant insurers' motions to dismiss, as "outliers" against "the weight of recent authority."

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4 Slip Op. at 7-8.

5 Slip Op. at 8 (citing *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).).

6 10A Couch on Ins. § 148:46 (3d ed. 2020).

As shown below, much of that recent authority relies on the misinterpreted COUCH treatise.[7]

In reaching these conclusions, the District Court disregarded the insurance company's decision not to include a virus exclusion in a policy sold in March 2020, as well as evidence that the insurance company (1) specifically stated its intention to provide coverage for virus-caused losses and (2) knew that restaurants expected to have coverage for business interruptions caused by virus and bacteria.[8] Finally, as to Civil Authority coverage, the District Court concluded that civil authority provisions cannot apply where access to a location is "limited" rather than "prohibited."[9]

I. INTRODUCTION

Amicus Curiae UP files this brief to give this Court further context in relation to two issues. UP demonstrates that the defendant insurance company here specifically intended to provide coverage for business interruption losses like that

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[7] Slip Op. at 11 (rejecting *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))

[8] Slip Op. at 11 ("The 'absence of an express [virus] exclusion does not operate to create coverage' for pandemic-related losses.") (*quoting SAS Int'l*, 2021 U.S. Dist. LEXIS 31093, at *9 (*quoting Given v. Commerce Ins. Co.*, 440 Mass. 207, 212 (2003)).

[9] Slip Op. at 13-14.

claimed by the policyholder, which are caused by virus. Indeed, this was coverage that the insurance company expressly told state insurance regulators that it intended to provide and that its policyholders would expect to receive. Accordingly the District Court erred both in failing to accept that the insurance company itself publicly agreed with the policyholder's interpretation of "direct physical loss or damage" prior to the loss at issue, which must be accepted as true, and in failing to accept the policyholder's allegations that its property was damaged by the presence of virus within its properties, which must also be accepted as true.

Second, UP shows that before the pandemic began, insurance companies had been placed on notice by courts for decades that virus and other vectors of communicable disease may cause direct physical loss or damage to property by making property unsafe for human use. The District Court's misinterpretation of "direct physical loss of or damage to" property in this specific case was compounded by disregarding controlling pre-pandemic Massachusetts authorities and the strong majority of cases nationwide that previously accepted that an event or condition which renders property unfit and unsafe for its intended use causes "loss" and "damage" to that property.

The District Court should have followed that guidance rather than relying on *SAS*, 2021 U.S. Dist. LEXIS 31093, at *7-8, which itself relies on the skewed history presented by COUCH. Viewing the policyholder's pleadings and precedent fairly, it

is simply not plausible, as well as an improper finding of fact, for the court to have concluded that COVID-19 does not involve the "unpleasant odors and fumes at issue in" controlling Massachusetts precedent.[10] Simply put, if a court can recognize that an unpleasant odor or dangerous gas may cause "physical loss of or damage to property," then so too can a deadly disease present on property, if both result in the property being unfit for safe human use.

UP observes the interpretation of this commonly-used insurance terminology, "direct physical loss of or damage to property," has potential applicability and importance far beyond this case, for multi-national corporations, the smallest of businesses that rely on the protections afforded by insurance, and ultimately consumers. Insurance companies have long known how courts interpret this undefined wording, and yet they persist in selling policies providing this coverage. UP respectfully suggests the District Court and this Court should not create more favorable wording for the insurance company here than it chose to sell.

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[10] Slip Op. at 10 (applying *SAS Int'l*, 2021 U.S. Dist. LEXIS 31093, at *7-8 while distinguishing *Essex Insurance Co. v. BloomSouth Flooring Corp.*, 562 F.3d 399 (1st Cir. 2009) and *Matzner v. Seaco Insurance Co.*, No. 96-0498-B, 1998 Mass. Super. LEXIS 407 (Mass. Super. Aug. 12, 1998)).

II. THE POLICYHOLDER'S INTERPRETATION IS SUPPORTED BY EVIDENCE THE INSURANCE COMPANY INTENDED COVERAGE FOR VIRUS-CAUSED BUSINESS INTERRUPTIONS AND DELETED THE VIRUS EXCLUSION BECAUSE IT KNEW POLICYHOLDERS EXPECTED THIS COVERAGE.

The District Court initially erred in disregarding the policyholder's pleading and attached exhibits setting forth evidence that the policyholder's interpretation of "direct physical loss or damage" to property, was not only reasonable, but correct. The policyholder submitted evidence of state regulatory filings from Greater New York Mutual Insurance Company, Insurance Company of Greater New York, INSCO, and the defendant, Strathmore Insurance Company (collectively "Strathmore"), in which the defendant admitted that viruses have long been anticipated and understood in the insurance trade to cause property damage and business interruption loss.[11]

More specifically, in 2005, the Insurance Services Office ("ISO") insurance trade group introduced the ISO Virus Exclusion to standard-form property insurance policies, while simultaneously acknowledging that viruses have the potential to cause damage to property and related business interruption losses.[12] Subsequently, Strathmore sought approval in New York to make a variation of the ISO Virus

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[11] *See* SAC ¶¶ 34-44 (JA0263-66), Strathmore Explanatory Memorandum (JA0522), Strathmore Side-By-Side Comparison (JA0524-25).

[12] *See* SAC ¶ 34 (JA0263), Strathmore Explanatory Memorandum (JA0522).

Exclusion "optional" rather than "mandatory," so they could issue policies to certain classes of policyholders (including, specifically, restaurants) without the ISO Virus Exclusion.[13]

Strathmore's regulatory filings directly contradict the defendant's position and the District Court's overly narrow interpretation, by demonstrating that insurance companies have long been aware that without a specific exclusion for "virus" or disease-causing agents, their "all risk" property insurance policies cover losses caused by viruses and disease-causing agents that make property unusable or unsafe to people. Strathmore explained this specific issue to New York's state insurance regulator after the regulator objected that Strathmore's proposal for an "optional" virus exclusion could conceivably lead to rate discrimination. The potential for discrimination that concerned the regulator arose because ISO had not accounted for any rate reduction when introducing its new ISO Virus Exclusion and had instead falsely asserted that the exclusion would not reduce existing coverage.

In Strathmore's supplemental explanation proposing a method for rating and charging coverage for virus-related perils, Strathmore pointed out that this coverage is simply provided by omission of the ISO Virus Exclusion. Strathmore's "Explanatory Memorandum" to the New York regulator expressly acknowledged the coverage that exists for "**this type of loss ('pandemic')**" in the absence of a virus

13 *Id.*

exclusion.[14] In the Explanatory Memorandum, Strathmore anticipated that viruses could result in potential covered losses "in Business Personal Property ('stock') and Business Interruption/Time Element coverage segments."[15] Strathmore also gave specific examples of communicable diseases spreading in indoor, highly trafficked spaces (like the plaintiff's restaurants) that may create covered losses, and recognized that "restaurants are probably the most likely to experience such events."[16]

Strathmore went so far as to acknowledge that a "pandemic" loss from "contagious disease" could involve a wide variety of vectors, including disease "transmitted to third parties via ingestion," exposure due to a "Typhoid Mary" or via "direct contact to an insured's products," or "spread through a HVAC system" in a building.[17] Although Strathmore expressed its optimism that a virus might not spread from building to building throughout a large city like New York, it recognized this was part of the "pandemic" type of loss it was insuring:

> **While it is possible that some type of disease (airborne Legionnaires Disease, for example) could spread through a HVAC system in any selected Apartment or Condo Building, it is highly unlikely that it**

14 *Id.*

15 *Id.*

16 *Id.*

17 *Id.*

> **would spread throughout a vast proportion of the apartments and condominiums across NYC that we insure.**[18]

Strathmore further **admitted** their restaurant-owning policyholders, like the policyholder here, reasonably expected this coverage and would never willingly part with it without a reduction in rates/premiums:

> **[W]e do not anticipate that any of our insureds will voluntarily request this [virus] exclusion; some (habitational risks) because it would never enter their minds as a problem for which they would voluntarily reduce coverage; others (restaurants) because they feel that such an event is well within the realm of possible fortuitous occurrences and should be covered should such an event arise.**[19]

Thus, the Strathmore filings put an end to the lie that a virus cannot cause "direct physical loss of or damage" to property. Strathmore expressed its intent to sell its policyholders insurance against that risk. The Strathmore filings demonstrate that insurance companies understood the meaning of "direct physical loss of or damage" to property includes the impact of disease-causing agents on the operation and profitability of a business. The Strathmore filings show that the insurance company **specifically expected** that merely removing a virus exclusion from a property insurance policy restores the expected coverage for virus-caused losses that existed before the introduction of virus exclusions. Because Strathmore's true understanding of the coverage is also set forth in the Second Amended Complaint,

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18 *Id.*

19 *Id.*

it must also be accepted as true as a factual matter when the Court engages in the interpretative task.

Here, holding Strathmore to what it said to the New York regulator is no different than holding Strathmore to what it said directly the policyholder: those statements are the complete context and reveal the insurance company previously enunciated the policyholder's interpretation as its own interpretation. When insurance companies attempt to misrepresent their policy wording to state insurance regulators or to courts, or when statements to these authorities differ (as here), it is particularly important to policyholders for courts to understand this process by which insurance industry drafting organizations like ISO or insurer groups like Strathmore seek approval to sell standard-form insurance policy language. The process is set forth in detail in *Morton International, Inc. v. General Accident Insurance Co.*, 629 A.2d 831 (N.J. 1993). First, the insurance industry will identify a change it wishes to make to standard forms, such as an exposure it wishes to exclude.[20] The insurance industry drafting organizations will draft the change.[21] The insurance industry drafting organizations will then seek regulatory approval, typically by submitting the same change and the same explanatory memorandum to

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20 *Id.* at 849-50.

21 *Id.* at 850.

each of the state regulators and meeting with individual regulators as necessary.[22] The insurance industry drafting organizations will then negotiate with the insurance regulators with regard to the changes they seek to make and whether those changes will require adjustment of rates.[23]

For present purposes, two points are critical. First, once approval is obtained, the standard form is sold throughout the United States, with no ability of individual policyholders to negotiate changes.[24] As *Morton* explained in relation to the insurance industry's efforts, through the Insurance Rating Board ("IRB"), an ISO predecessor, to add a pollution exclusion to the standard-form comprehensive general liability ("CGL") policy:

> In considering the IRB's explanatory memorandum concerning the effect of the pollution-exclusion clause which the record suggests was the only explanation offered to New Jersey insurance officials-we accord special significance to the process by which that clause gained approval in New Jersey and other states. Realistically, once the clause gained regulatory approval, it was uniformly adopted as an endorsement to the standard form CGL policies that were issued to innumerable commercial enterprises and governmental agencies for more than a decade. The abundant case law called to our attention by counsel for all parties may be regarded merely as an illustrative sample of the virtually universal inclusion of the standard clause, or one of its derivatives, in CGL policies issued throughout the United States. **Of course, after regulatory approval the specific provisions of the pollution-exclusion clause ordinarily were not negotiable by purchasers of CGL policies.** As some commentators observe, the

22 *Id.* at 851.

23 *Id.* at 851-52.

24 *Id.* at 851.

> typical commercial insured rarely sees the policy form until after the premium has been paid. Ballard and Manus, supra, 75 Cornell L.Rev. at 621; W. David Slawson, Mass Contracts: Lawful Fraud in California, 48 S.Cal.L.Rev. 1, 12 (1974). **Accordingly, to the extent that the pollution-exclusion clause ever was subjected to arms-length evaluation by interests adverse to the insurance industry, that evaluation occurred only when the clause was submitted to and reviewed by state regulatory authorities**.[25]

Second, because drafting organizations and insurer groups like Strathmore seek approval for a standard-form on behalf of all of their members for sale throughout the United States, statements by these groups to any regulator as to the content of the standard form bind all of the member companies everywhere. This is why the *Morton* court looked to what the IRB said on behalf of its members in New Jersey, Georgia, West Virginia, Kansas, Puerto Rico, and elsewhere. [26]

Because this interpretation was set forth in the Second Amended Complaint, it should have been accepted as true by the District Court when resolving the Motion to Dismiss. To the extent the matter were considered as an issue of evidence, context to words in a contract, extrinsic evidence of usage of a word in trade, or a specialized meaning, or industry and trade practices, may be considered to prove the meaning of a word or phrase in an insurance policy or contract, or to establish an

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25 *Id.* at 852-53 (emphasis added).

26 *See id.* at 851-54.

ambiguity.[27] This evidence should not have been disregarded because it not only establishes that the policyholder's interpretation is reasonable (and thus sufficient to prevail in any ambiguity analysis) but also **correct** and **subjectively intended** by the defendant.

III. DECADES OF CASE LAW WARNED INSURERS THAT THE CLAUSE "PHYSICAL LOSS OR DAMAGE" IS BROAD AND NOT LIMITED TO "DISTINCT, DEMONSTRABLE, PHYSICAL ALTERATION" TO PROPERTY.

The insurance company's pre-pandemic understanding of how a virus, bacteria or other disease-causing agent can cause "direct physical loss of or damage to" property was no mistake. It was a well-founded view with a pedigree. Before the pandemic, courts in seventeen jurisdictions had already addressed the insurance industry's argument that "physical loss or damage" required some sort of "distinct,

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[27] *See Commercial Union Ins. Co. v. Seven Provinces Ins. Co.*, 217 F.3d 33, 38-39 (1st Cir. 2000) (applying Massachusetts law) (holding the district court "properly considered extrinsic evidence to determine what the parties meant" where "each side proffered an expert who worked in the insurance business and could testify to what the terms in the policy must have meant in light of industry practice."); *Affiliated FM Ins. Co. v. Constitution Reins. Corp.*, 626 N.E.2d 878, 881 (Mass. 1994) ("Where, as here, the contract language is ambiguous, evidence of trade usage is admissible to determine the meaning of the agreement."); *Cohen v. Union Warren Sav. Bank*, 1991 Mass. App. Div. 95, 97, 1991 Mass. App. Div. LEXIS 49, at *7 (1991) ("Where, however, the policy terms are ambiguous and the coverage issue is reasonably disputed, a court may consider extrinsic evidence of the surrounding circumstances and of the parties' intent. For example, evidence of the construction given to the language by the parties and of the customary usage of persons in the same commercial setting is normally admissible. If the meaning of the policy terms remains unclear, the policy is generally construed in favor of the insured in order to promote the policy's objective of providing coverage.").

demonstrable, physical alteration" to property, and all but one ruled against the industry. Despite this consensus, insurers insist that the weight of authority tilts their way. They do so by citing a swath of unpublished or trial-level decisions (both pre- and post-pandemic).

Virtually all of those cases did not face, or have not yet faced, appellate scrutiny. It is not accurate to equate the rulings of trial courts with the judgments of state and federal appellate courts. And the overwhelming majority of published appellate law cuts against the insurance industry.

A. The Overwhelming Weight of Published Authority Gives "Physical Loss" Its Broad, Ordinary Meaning.

Insurance coverage is a matter of state law. Before the pandemic, five states' high courts[28] and eight other states' intermediate appellate courts[29] held in binding

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[28] *W. Fire Ins. Co.* v. *First Presbyterian Church*, 437 P.2d 52 (Colo. 1968) (gasoline fumes); *Sentinel Mgmt. Co.* v. *Aetna Cas. & Sur. Co.*, 615 N.W.2d 819 (Minn. 2000) (asbestos); *Mellin* v. *N. Sec. Ins. Co.*, 115 A.3d 799 (N.H. 2015) (urine odor); *Dundee Mut. Ins. Co.* v. *Marifjeren*, 587 N.W.2d 191 (N.D. 1998) (power outage); *Murray* v. *State Farm Fire & Cas. Co.*, 509 S.E.2d 1 (W. Va. 1998) (threat of rockfall).

[29] *Hughes* v. *Potomac Ins. Co.*, 18 Cal. Rptr. 650 (Cal. Ct. App. 1962) (erosion of land beneath a house); *Azalea, Ltd.* v. *Am. States Ins. Co.*, 656 So. 2d 600 (Fla. Ct. App. 1995) (death of bacteria colony in treatment plant); *Bd. of Educ.* v. *Int'l Ins. Co.*, 720 N.E.2d 622, 625-26 (Ill. Ct. App. 1999) (presence of asbestos); *Widder* v. *La. Citizens Prop. Ins. Corp.*, 82 So. 3d 294 (La. Ct. App. 2011) (lead contamination); *Wakefern Food Corp.* v. *Liberty Mut. Fire Ins. Co.*, 968 A.2d 724 (N.J. App. Div. 2009) (power outage); *Farmers Ins. Co.* v. *Trutanich*, 858 P.2d 1332 (Or. Ct. App. 1993) (methamphetamine fumes); *Graff* v. *Allstate Ins. Co.*, 54 P.3d 1266 (Wash. Ct. App. 2002) (methamphetamine residue). New York law is difficult to categorize, but the most recent appellate decision agrees with the policyholders'

decisions that "physical loss" and its variants included risks that rendered property unsafe or unusable, even without visible, tangible, or structural damage. Federal appellate courts reached the same conclusion applying the law of four other states, including the First Circuit's treatment of this very issue under Massachusetts law.[30] Prior to the pandemic, Massachusetts courts were in agreement recognizing that "direct physical loss or damage" to property can include such varied, incorporeal conditions as carpet chemical odors, oil fumes in a house, and carbon monoxide contamination.[31]

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view. *See Pepsico, Inc.* v. *Winterthur Int'l Am. Ins. Co.*, 24 A.D.3d 743, 744 (N.Y. App. Div. 2005) (agreeing that "off-tasting" beverage that was **not** "unfit for human consumption" suffered physical damage because, "the product's function and value have been seriously impaired"); *but see Roundabout Theatre Co.* v. *Cont'l Cas. Co.*, 302 A.D.2d 1 (N.Y. App. Div. 2002) (holding that off-premises damage causing business interruption did not qualify for coverage).

[30] *Essex Ins. Co.* v. *BloomSouth Flooring Corp.*, 562 F.3d 399 (1st Cir. 2009) (Massachusetts law) (carpet chemical odors); *Hampton Foods, Inc.* v. *Aetna Cas. & Sur. Co.*, 787 F.2d 349 (8th Cir. 1986) (Missouri law) (risk of collapse); *Alliance Ins. Co.* v. *Keleket X-Ray Corp.*, 248 F.2d 920 (6th Cir. 1957) (Ohio law) (radium contamination); *Intermetal Mexicana, S.A.* v. *Ins. Co. of N. Am.*, 866 F.2d 71 (3d Cir. 1989) (Pennsylvania law) (dispossession of property).

[31] *Essex*, 562 F.3d at 406 (carpet fumes); *Arbeiter v. Cambridge Mut. Fire Ins. Co.*, Middlesex No. 9400837, 1996 WL 1250616 (Mass. Super. Mar. 15, 1996) (oil fumes); *Matzner v. Seaco Ins. Co.*, Suffolk No. CIV. A. 96-0498-B, 1998 WL 566658 (Mass. Super. Aug. 12, 1998) (carbon monoxide gas). These cases are treated in the plaintiff's brief. There is variation in some other states. *Compare Hughes*, 18 Cal. Rptr. at 655 (rapid erosion rendering house uninhabitable caused "physical loss" to the house) *with MRI Healthcare of Glendale, Inc.* v. *State Farm Gen. Ins. Co.*, 187 Cal. App. 4th 766 (2010) (no "physical loss" when MRI machine would not "ramp up" due to inherent defect); *compare also General Mills, Inc.* v. *Gold Medal Ins. Co.*, 622 N.W.2d 147, 152 (Minn. Ct. App. 2001) (FDA ban on

Prior to the pandemic, then, the totals were 17-0 in favor of policyholders. While the law is nuanced in some jurisdictions, it is false to claim that most states require a "distinct, demonstrable, physical alteration of the property" (or some similar test) to trigger the broader term "physical loss" in a business-interruption policy. There is no reason to believe that the Massachusetts Supreme Judicial Court would ignore the chorus agreeing with the policyholders' view, particularly where the Superior Court has twice ruled in favor of coverage on a similar issue, as has this Circuit. The sheer weight of out-of-state authority makes it impossible to discuss each case in detail in the space of one brief. But the key decisions illustrate why the insurance industry's position has persuaded few appellate judges.

Start with the seminal cases, *Hughes*, *First Presbyterian*, and *Murray*, decided in 1962, 1968, and 1998 respectively. In *Hughes* and *Murray* both policies promised to pay for "direct physical loss to the property," while in *First Presbyterian* the policy provided coverage against "all risks" of "direct physical loss."[32] In *Hughes*, erosion swept away the building's support, causing cosmetic damage but making it

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selling contaminated oats caused "physical loss") *with Source Food Techs., Inc.* v. *U.S. Fidelity & Guar. Co.*, 465 F.3d 834, 838 (8th Cir. 2006) (Minnesota law) (USDA ban on importing contaminated beef did not cause "physical loss"); *compare also Alliance*, 248 F.2d at 925 (radium contamination triggered business-income coverage) *with Mastellone v. Lightning Rod Mut. Ins. Co.*, 884 N.E.2d 1130, 1143 (Ohio Ct. App. 2008) (construing "physical injury" as requiring structural damage).

[32] *Murray*, 509 S.E.2d at 16; *Hughes*, 18 Cal. Rptr. at 655.

unsafe to inhabit.[33] In *First Presbyterian*, "the accumulation of gasoline around and under the church building . . . ma[de] further use of the building highly dangerous."[34] In *Murray*, unstable rocks above a house prompted an evacuation order from the government.[35]

The insurance companies denied in each of these cases. Like here, they contended that their policies "only insured the physical damage to the dwelling."[36] Each court disagreed:

> To accept [the insurer's] interpretation of its policy would be to conclude that a building which has been overturned or which has been placed in such a position as to overhang a steep cliff has not been "damaged" so long as its paint remains intact and its walls still adhere to one another.
>
> **Despite the fact that a "dwelling building" might be rendered completely useless to its owners, [the insurer] would deny that any loss or damage had occurred unless some tangible injury to the physical structure itself could be detected**. Common sense requires that a policy should not be so interpreted in the absence of a provision specifically limiting coverage in this manner.[37]

These courts stressed that the property was not **safe** – giving weight to perhaps the most important characteristic of physical property.[38] *Hughes* reasoned that "[i]t

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33 18 Cal. Rptr. at 655.

34 437 P.2d at 55.

35 509 S.E.2d at 16-17.

36 *Id.*

37 *Id.* (quotations omitted, emphasis added).

38 *Id.*

goes without question that [the homeowners]' 'dwelling building' suffered real and severe damage when the soil beneath it slid away and left it overhanging a 30-foot cliff."[39] Likewise, *First Presbyterian* underscored that an unsafe, highly dangerous condition infiltrating a building is more than a mere "loss of use" and constitutes "direct physical loss."[40] *Murray* echoed these themes, pointing out that the houses beneath the cliff "could scarcely be considered 'homes' in the sense that rational persons would be content to reside there."[41] That was a "physical loss."

Similarly, in *Wakefern*, the court rejected "the narrowly-parsed definition of 'physical damage' which the insurer urges us to adopt" and held that "loss of function" sufficed. 968 A.2d at 735-38. This discussion could go on for pages, but UP will stop here. The Court should review the many other pre-pandemic cases that found coverage in analogous circumstances.[42]

Having failed to "defin[e] direct physical loss or damage as they (and others

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39 18 Cal. Rptr. at 655.

40 437 P.2d at 55.

41 509 S.E.2d at 17.

42 *See, e.g.*, *Motorists Mut. Ins. Co.* v. *Hardinger*, 131 F. App'x 823, 827 (3d Cir. 2005) (e-coli contamination); *General Mills*, 622 N.W.2d at 152 (FDA rule that harmless oats were nonetheless "adulterated"); *Manpower Inc.* v. *Ins. Co. of Pa.*, 2009 WL 3738099 (E.D. Wis., Nov. 3, 2003) (police order forbidding access to unstable building); *TRAVCO* v. *Ward*, 2010 WL 2222255 (E.D. Va., June 3, 2010) (toxic gas); *Or. Shakespeare Festival Ass'n* v. *Great Am. Ins. Co.*, 2016 U.S. Dist. LEXIS 74450 (D. Or., June 7, 2016) (wildfire smoke), *vac'd as a condition of settlement.*

before them) have argued it should be interpreted," the insurance company here must honor its broad promise of coverage.[43] The Court of Appeals should not be in the business of redefining established policy terms and rescuing insurance companies who—after 60 years of published precedent—did not change or define narrowly those terms in their broadly-worded insurance policies.

B. COUCH ON INSURANCE Misrepresented the State of the Case Law.

As shown above, 10A COUCH ON INSURANCE § 148:46, titled "Generally; 'Physical' loss or damage," and the slanted approach to the cases cited within it, largely drove the decision in *SAS*, 2021 U.S. Dist. LEXIS 31093, on which the District Court relied. More specifically, the District Court essentially applied the standard suggested in the third paragraph of that section, which reads:

> The requirement that the loss be "physical," given the ordinary definition of that term, is widely held to exclude alleged losses that are intangible or incorporeal and, thereby, to preclude any claim against the property insurer when the insured merely suffers a detrimental economic impact unaccompanied by a distinct, demonstrable, physical alteration of the property.[44]

For its conclusion, COUCH cites **five** cases,[45] as supporting the insurance industry's restrictive view: two from New York, the *MRI* case from California, an Oregon

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[43] *Cherokee Nation* v. *Lexington Ins. Co.*, 2021 WL 506271, at *4 (Cherokee Cnty., Okla., Jan. 14, 2021).

[44] 10A COUCH ON INSURANCE § 148:46.

[45] *Port Auth. of N.Y. & N.J. v. Affiliated FM Ins. Co.*, 311 F.3d 226, 236 (3d Cir. 2002); *Universal Image Prods., Inc.* v. *Federal Ins. Co.*, 475 Fed. App'x 569, 573 (6th Cir. 2012); *Newman Myers Kreines Gross Harris, P.C. v. Great N. Ins. Co.*, No.

federal district court opinion (abrogated three years later in *Trutanich*, *supra*), and an unpublished decision (*Universal Image*). 10A COUCH ON INSURANCE § 148:46, however, continues, by noting – perhaps tellingly, in passive voice – that "[t]he opposite result has been reached":

> The opposite result has been reached, allowing coverage based on physical damage despite the lack of physical alteration of the property, on the theory that the uninhabitability of the property was due to the fact that gasoline vapors from adjacent property had infiltrated and saturated the insured building, and the theory that the threatened physical damage to the insured building from a covered peril essentially triggers the insured's obligation to mitigate the impending loss by undertaking some hardship and expense to safeguard the insured premises.[46]

In support of this conclusion, COUCH cites **two** of the **twenty-one** appellate-level and other cases discussed above (*First Presbyterian Church* and *Hampton Foods*). This is an inaccurate and misleading distortion of the state of the case law as it existed prior to the COVID-19 pandemic. More correctly, under both longstanding precedent and well-understood canons of construction, "loss" must mean something different than "damage," and "direct physical loss" should be understood to require "tangible, concrete, and measurable losses" as opposed to "speculative or intangible

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13 Civ. 2177(PAE), 2014 WL 1642906 (S.D.N.Y. Apr. 24, 2014); *Great N. Ins. Co. v. Benjamin Franklin Fed. Sav. & Loan Ass'n*, 793 F. Supp. 259, 263 (D. Or. 1990); *MRI Healthcare Ctr. of Glendale, Inc. v. State Farm Gen. Ins. Co.*, 115. Cal. Rptr. 3d 27, 38 (Cal. App. 2010).

[46] 10A COUCH ON INSURANCE § 148:46.

losses."[47] That is the correct standard, and UP suggests it would be applied by the Massachusetts Supreme Judicial Court. Further, as the policyholder observes in its Opening Brief, the pleadings allege tangible alteration of property due to virus on the insured premises, and these well-pled facts should have been credited.

C. The Better-Reasoned Cases Addressing Loss Related to the Pandemic Follow the Pre-Pandemic Consensus.

The insurance industry's early and categorical refusal to pay claims arising from the COVID-19 pandemic compelled a flood of litigation by their policyholders. The insurance company here will no doubt cite to the many trial-level decisions that summarily dismissed policyholder suits. Those orders, though, contain serious errors, egregious departures from the text, or both. Given existing law, appellate benches may well invert that count. Fortunately, a growing number of trial courts are staying faithful to the text of the policies and the actual, pre-pandemic consensus. This Court should adopt their reasoning.

A recent ruling by Judge Chang in the COVID-19 MDL litigation is representative.[48] *Society* analyzed the policy text in detail and concluded that

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[47] *James W. Fowler Co. v. QBE Insurance Corp.*, No. 3:18-cv-1705-S1, 2020 WL 4291272, *7 (D. Or. July 24, 2020) (applying Oregon law) (distinguishing and rejecting 10A COUCH ON INSURANCE § 148:46 and accepting that buried but otherwise undamaged tunnel-boring machine had suffered "direct physical loss" where there was no cost-effective way to recover it).

[48] *In re Soc'y Ins. Co. Covid-19 Bus. Interruption Prot. Ins. Litig.*, MDL No. 2964, 2021 U.S. Dist. LEXIS 32351 (N.D. Ill., Feb. 22, 2021). *See also Henderson Rd. Rest. Sys.* v. *Zurich Am. Ins. Co.*, 2021 U.S. Dist. LEXIS 9521 (N.D. Ohio, Jan.

coverage existed for COVID-19 losses.[49] Judge Chang started, as one should, with the text. "[T]he operative text is 'direct physical loss of or damage to covered property."[50] He swiftly desiccated the "tangible alteration" requirement:

> The disjunctive "or" in that phrase means that "physical loss" must cover something different from "physical damage." It is axiomatic that courts interpret contracts so as to give effect to all of their provisions. That interpretive principle refutes [the insurer]'s first argument: that the coronavirus could not constitute "direct physical loss of or damage to" the covered property because the virus "does not cause a tangible change to the physical characteristics of property."[51]

Society observed that the "more challenging interpretive question is whether the restrictions imposed on the [policyholders]' use of their premises count as *physical* loss."[52] It concluded that they did. Although the restaurants could offer take-out services, the COVID-19 orders "impose a *physical* limit: the restaurants are limited from using much of their physical space."[53] "It is not as if the shutdown orders

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19, 2021); *Derek Scott Williams PLLC* v. *Cincinnati Ins. Co.*, 2021 U.S. Dist. LEXIS 37096 (N.D. Ill., Feb. 28, 2021); *NECO, Inc.* v. *Owners Ins. Co.*, 2021 U.S. Dist. LEXIS 28761 (W.D. Mo., Feb. 16, 2021); *Elegant Massage, LLC* v. *State Farm Mut. Auto. Ins. Co.*, 2020 WL 7249624 (E.D. Va., Dec. 9, 2020); *Studio 417* v. *Cincinnati Ins. Co.*, 478 F. Supp. 3d 794 (W.D. Mo. 2020); *Choctaw Nation of Okla.* v. *Lexington Ins. Co.*, 2021 WL 714032 (Bryan Cty., Okla., Feb. 15, 2021); *Cherokee Nation*, 2021 WL 506271, at *3-7; *Ungarean* v. *CNA Ins.*, 2021 Pa. Dist. & Cnty. Dec. LEXIS 2 (Mar. 22, 2021).

49 *Id.*, at *15-16.

50 *Id.* at *37.

51 *Id.* (cleaned up).

52 2021 U.S. Dist. LEXIS 32351, at *38.

53 *Id.* at *39.

imposed a *financial* limit on the restaurants by, for example, capping the dollar-amount of daily sales the restaurant could make."[54] "No, instead the [policyholders] cannot use (or cannot fully use) the physical space."[55]

Here, the policyholder has pled the presence of virus and that the virus damaged the property and, as a consequence of that damage, the policyholder is unable to use its property. Alternatively, orders of Civil Authority caused it to lose the full use of its property. In every sense, that loss "relates to natural or material things." *Physical*, WEBSTER'S THIRD NEW INT'L DICTIONARY 1706 (1993) (contrasting "physical" things with "things mental, moral, spiritual, or imaginary"). Nevertheless, the decision below concluded that "COVID-19 virus does not impact the structural integrity of property," and "is incapable of damaging physical structures."[56] As a factual matter, the court found facts based on no record. As a legal matter, the court rewrote the policy, which does not require impact on structural integrity or damage to physical structures. It requires only "physical loss of" property. Regardless, there was a "physical" force here—the pandemic and virions of the virus, and the District Court recognized the presence of virus on and within

54 *Id.*

55 *Id.*

56 Slip Op. at 8.

property "harms human beings."[57] Thus, the danger caused by the pandemic and virions in properties "ma[de] further use of the building highly dangerous," no less than the fumes and gas in *First Presbyterian*, *Essex*, *Arbeiter* and *Matzner*,[58] or the rocks in *Murray*.[59]

In each of these cases, the government subordinated the owners' property rights to its interest in protecting human life. It did not matter that the policies insured property, and not people. The government barred the use of physical property in response to a physical threat, and that was enough. Churches, houses, or restaurants that are unsafe for human use can "scarcely be considered [churches, houses, or restaurants] in the sense that rational persons would be content to reside there."[60]

Finally, *Society* addressed one final argument:

> Remember that [the insurance company] promised to pay only for loss of business income during the "period of restoration" .... The definition of "Period of Restoration" says that coverage for loss of business income "ends ... when the property at the described premises should be repaired, rebuilt, or replaced with reasonable speed and similar quality; or the date when business is resumed at a new permanent location." In [the insurance company's] view, "repaired, rebuilt, or replaced" implies that covered "physical loss or damage" is necessarily tangible,

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57 Slip Op. at 8.

58 *First Presbyterian*, 437 P.2d at 55; *Essex*, 562 F.3d at 406; *Arbeiter*, 1996 WL 1250616; *Matzner*, 1998 WL 566658.

59 509 S.E.2d at 16-17

60 *Murray*, 509 S.E.2d at 17.

> requiring a physical injury to the covered property rather than mere loss of use.[61]

Judge Chang considered and rejected this point. Reading the policy as a whole, "too many textual clues point the other way."[62] The Period of Restoration "describes a *time* period during which loss of business income will be covered, rather than an explicit definition of coverage."[63] The coverage grant applied to "loss of" property, not just "damage to" property.[64] The construction-as-a-whole canon cannot be used to render other terms meaningless.[65]

Further supporting this reading was that "repair" and "replace" need not be construed narrowly. "Repair," for example, means "to restore to a sound or healthy state." *Repair,* MERRIAM-WEBSTER'S COLLEGIATE DICTIONARY 1055 (11th ed. 2003). "Replace" means "to restore to a former place or position." *Replace*, MERRIAM-WEBSTER ONLINE DICTIONARY. "There is nothing inherent in the meanings of those words that would be inconsistent with characterizing the [policyholders]' loss of their space due to the shutdown orders as a physical loss."[66] "If, for example, the coronavirus risk could be minimized by the installation of

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61 2021 U.S. Dist. LEXIS 32351, at *40-41 (cleaned up).

62 *Id.* at *41.

63 *Id.*

64 *Id.*

65 *Id.*

66 *Society*, 2021 U.S. Dist. LEXIS 32351, at *40-41.

partitions and a particular ventilation system, then the restaurants would be expected to 'repair' the space by installing those safety features."[67] Other courts agree.[68]

At worst, tension exists under either side's interpretation. The court could either ignore the disjunctive coverage grant, or it could adopt an alternate (though still reasonable) reading of "repair" and "replace."[69] As a result, the policy was ambiguous and the tie went to the policyholder.[70] That should have occurred here.

CONCLUSION

For the foregoing reasons, UP respectfully suggests the District Court erred in dismissing the policyholder's case and should accordingly be reversed.

Respectfully submitted,

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67 *Id.*

68 *Derek Scott Williams*, 2021 U.S. Dist. LEXIS 37096, at *12 ("'Repair,' however, is not inherently physical; one need only consider common references to repairing a relationship or repairing one's health.") (citing Merriam-Webster); *see also NECO*, 2021 U.S. Dist. LEXIS 28761, at *19-20; *Cherokee Nation*, 2020 WL 506271, at *7-8 & n.15; *Ungarean*, 2021 Pa. Dist. & Cnty. Dec. LEXIS 2, at *18-21.

69 *Society*, 2021 U.S. Dist. LEXIS 32351, at *40-41.

70 *Id.*

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CERTIFICATE OF COMPLIANCE UNDER RULE 32(g)(1)

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