Case No. S_____

In the

Supreme Court

of the

State of California

THE INNS BY THE SEA,
Plaintiff and Appellant,

v.

CALIFORNIA MUTUAL INSURANCE COMPANY,
Defendant and Respondent.

PETITION TO TRANSFER FROM THE CALIFORNIA COURT OF APPEAL
SIXTH APPELLATE DISTRICT · CASE NO. H048443
AFTER A DECISION BY THE SUPERIOR COURT OF THE STATE OF CALIFORNIA
FOR THE COUNTY OF MONTEREY · CASE NO. 20CV001274
THE HONORABLE LYDIA M. VILLARREAL, PRESIDING

PETITION TO TRANSFER

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NATURE OF CAUSE

Small businesses employ more than 7 million Californians.[1] Half of these businesses are in danger of closing as COVID-19 ravages the economy.[2] When they do, The Kaiser Family Foundation estimates that 3.4 million Californians could lose their health insurance, despite being in the midst of a global pandemic.[3] This is a disaster in the truest sense of the term.

At a time when they need it the most, many businesses like The Inns by the Sea ("Petitioner") have turned to insurance policies that promised to insure ***all*** risks not otherwise excluded and to cover business income losses flowing from those risks. Yet,

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[1] U.S. Small Business Administration, California Small Business Profile 2020, *available at* https://cdn.advocacy.sba.gov/wp-content/uploads/2020/06/04142955/2020-Small-Business-Economic-Profile-CA.pdf ("California small businesses employed 7.1 million people, or 48.5% of the private workforce, in 2017.") (last accessed October 13, 2020).

[2] Kevin Baxter, *About Half of All Small Businesses in Danger of Failing During Pandemic, Survey Finds*, L.A. TIMES (May 16, 2020), *available at* https://www.latimes.com/california/story/2020-05-16/about-half-of-all-small-businesses-in-danger-of-failing-during-pandemic-new-report-says (last accessed October 8, 2020).

Indeed, according to *The New York Times*, roughly 20% of businesses have already closed. Ben Casselman, *Small-Business Failures Loom as Federal Aid Dries Up*, N.Y. TIMES (Sep. 1, 2020), *available at* https://www.nytimes.com/2020/09/01/business/economy/small-businesses-coronavirus (last accessed October 13, 2020).

[3] Rachel Garfield, *et al.*, *Eligibility for ACA Health Coverage Following Job Loss*, KFF (May 13, 2020), *available at* https://www.kff.org/coronavirus-covid-19/issue-brief/eligibility-for-aca-health-coverage-following-job-loss (last accessed October 8, 2020).

insurers have summarily denied these claims, taking the blanket position that the presence of coronavirus or COVID-19 does not damage property and, therefore, does not cause "physical loss of or damage to" property sufficient to trigger coverage.[4] Petitioner's claim, therefore, raises an issue common to claims made by thousands of California small businesses based on the same or similar policy wording.

ISSUE PRESENTED

Accordingly, Petitioner requests expedited Supreme Court review of an open and pressing question under California law:

> Could a policyholder reasonably expect the standard form "physical loss of or damage to" provision in an "all risk" property insurance policy to cover business interruption losses caused by COVID-19 (and the governmental orders resulting therefrom) because COVID-19 has caused the loss of safe and intended use of insured property?

SUMMARY OF SIGNIFICANT FACTS

In response to the physical presence of coronavirus on its properties and government closure orders, Petitioner shuttered its five locations on California's central coast. (Complaint at ¶¶ 2, 22.) Like thousands of other small businesses, Petitioner promptly made a claim for business interruption coverage with its property

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[4] This is the industry-standard policy language drafted by the Insurance Services Office ("ISO"). Most insurers use ISO forms, at least as a starting place. *See Sprinkles v. Associated Indem. Corp.* (2010) 188 Cal. App. 4th 69, 79, fn. 3 (2010). Other policies may use slightly different language, for example, "physical loss or damage to" property, which omits the "of" after "loss."

insurance company, California Mutual Insurance Company ("Respondent"), which sold Petitioner an "all risks" policy. (An all risks policy is meant to cover exactly that: "all risks" except those expressly excluded.)

Although the insurance industry created a standard form virus exclusion,[5] many insurers do not routinely use this exclusion in their policies, and Respondent did not include it in the policy it issued to Petitioner. Not only does "an insurance company's failure to use available language to exclude certain types of liability give[ ] rise to the inference that the parties intended not to so limit coverage" (*Fireman's Fund Ins. Cos. v. Atl. Richfield Co.* (2001) 94 Cal. App. 4th 842, 852), but here, it functions as an acknowledgement that the loss affirmatively triggers the policy. Otherwise, there would be no need for the exclusion.[6] Respondent nonetheless denied Petitioner's claim the same day, taking the position that Petitioner had not experienced a covered loss. (*Id.* at ¶¶ 23-24, Ex. B.)

Petitioner filed suit, challenging Respondent's interpretation of its standard-form "all risk" policy. (Monterey Superior Court Case No. 20CV001274.) Respondent filed a demurrer, arguing, *inter alia*, that the Complaint failed to state a

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[5] *See, e.g.*, *Mudpie, Inc. v. Travelers Cas. Ins. Co. of Am.* (N.D. Cal. Sept. 14, 2020) No. 4:20-cv-03213 (*Mudpie*), Dkt. No. 51 (Order on Motion to Dismiss) at 2 (noting virus exclusion in the policy at issue there).

[6] While there are reasons why this standard virus form exclusion in policies issued to some other California policyholders should not apply to COVID-19 related loss or damage, this petition does not put the issue before the Court.

cause of action because the presence of coronavirus does not cause "direct physical loss of or damage to" property.

Relying on two Court of Appeals cases[7] decided in much different contexts — one case involving whether the loss of computer data was a covered cause of loss, and another case involving the failure of an MRI machine to turn on — Respondent argued that "direct physical loss of or damage to" property requires direct, tangible, and perceptible alteration of property to trigger coverage.[8]

Petitioner argued that the plain meaning of the policy, or at least a reasonable reading of the policy, compelled coverage, as supported by numerous out-of-state cases finding coverage where a physical condition renders property unsafe or unfit for its intended purpose, even absent traditional structural alteration (such as that caused by fires and earthquakes) as there is no such

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[7] *MRI Healthcare Ctr. of Glendale, Inc.* (2010) 187 Cal.App.4th 776 (*MRI*); *Ward Gen. Ins. Servs., Inc. v. Emp'rs Fire Ins. Co.* (2003) 114 Cal.App.4th 548 (*Ward*).

[8] Lacking clear guidance from the Supreme Court on the meaning of "direct physical loss of or damage to" property, trial courts in California have variously accepted and rejected these two cases as binding authority in considering COVID-19 related business interruption claims. *Compare, e.g.*, *Mudpie*, Dkt No. 51 at 5, 14 (questioning applicability of *MRI* and noting "the law concerning business interruption coverage liked to the COVID-19 pandemic is very much in development") *with 10E v. Travelers Indem. Co. of Conn., et al.* (C.D. Cal. August 28, 2020) No. 2:20-cv04418, Dkt. No. 38 (Order on Motion to Dismiss) at 6 (applying *MRI* and *Ward* in holding the presence of COVID-19 does not count as "direct physical loss of or damage to" property because it does not produce "distinct, demonstrable, physical alteration").

restriction in the policy.[9] The fact that courts outside California have found a construction requiring coverage to be reasonable is *per se* evidence of its reasonableness. (*See, e.g., Minkler v. Safeco Ins. Co. of Am.* (2010) 49 Cal.4th 315, 332 (noting a jurisdictional split in authority gives rise to an ambiguity, which "must be resolved, if possible, in a way that preserves the objectively reasonable coverage expectations of the insured seeking coverage"); *E.M.M.I. Inc. v. Zurich Am. Ins. Co.* (2004) 32 Cal.4th 465, 482 (finding in favor of coverage despite majority of decisions denying coverage based on policy ambiguity).) And long-established principles of California law provide that insurance policies are to be reasonably construed in favor of the objective of the contract — providing coverage. (*See, e.g., Reserve Ins. Co. v. Pisciotta* (1982) 30 Cal.3d 800, 807 ("[A]ny ambiguity or uncertainty in an insurance policy is to be resolved against the

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[9] These include cases finding coverage for the dangerous physical presence of:

- **Smoke**, *Oregon Shakespeare Festival Ass'n v. Great Am. Ins. Co.* (D. Or. June 7, 2016) No. 1:15-CV-01932-CL, 2016 WL 3267247;
- **E. coli**, *Motorists Mut. Ins. Co. v. Hardinger* (3d. Cir. 2005) 131 F.App'x 823;
- **Asbestos**, *Port Auth. of N. Y. & N. J. v. Affiliated FM Ins. Co.* (3d Cir. 2002) 311 F.3d 226 (*Port Auth.*); *Sentinel Mgmt. Co. v. New Hampshire Ins. Co.* (Minn. Ct. App. 1997) 563 N.W.2d 296;
- **Carbon monoxide**, *Matzner v. Seaco Ins. Co.* (Mass. Super. Aug. 12, 1998) No. 96-0498-B, 1998 WL 566658; and
- **Ammonia**, *Gregory Packaging, Inc. v. Travelers Prop. Cas. Co. of Am.* (D.N.J. Nov. 25, 2014) No. 2:12-cv-04418 (WHW)(CLW), 2014 WL 6675934 (*Gregory Packaging*).

insurer and . . . if semantically permissible, the contract will be given such construction as will fairly achieve its object of providing indemnity for the loss to which the insurance relates").)

After a hearing, the Court issued a two-paragraph order sustaining the demurrer without leave to amend. The order does not explain the Court's reasons for granting the demurrer. The Court dismissed the case on September 3rd, and on September 8th, Petitioner filed a Notice of Appeal to the Sixth District.

WHY THIS CAUSE WARRANTS TRANSFER

This Court has not interpreted the undefined phrase "physical loss of or damage to" common in all risk property policies. The meaning and scope of this phrase is a threshold legal question affecting tens of thousands of California small businesses seeking relief from their insurers during this pandemic. This case thus presents an opportunity to resolve a critical aspect of the COVID-19 litigation tsunami swelling the dockets of California's trial courts. While the governing principles of insurance law are clear, California small businesses urgently need a decision from this Court addressing whether the dangerous presence of coronavirus amounts to "physical loss of or damage to property" — and presumably the insurance industry would like a decision too. In ordinary times, the prudent course might be to allow COVID-related insurance cases to work their way through the trial and appellate courts. But these are not ordinary times.

When a case pending in a Court of Appeal "presents an issue of great public importance that the Supreme Court must promptly resolve," this Court has the power to transfer the case to itself for

expedited review. (Cal. Rules of Court 8.552(c).) Extraordinary times call upon this Court to exercise extraordinary procedures.

I. The Court Should Transfer the Appeal to Itself, Because the Case Presents an Urgent Matter of Public Concern for Small Businesses and Californians Employed by Small Businesses

This case presents an issue of great public importance in need of prompt resolution, as the lives and livelihoods of millions of Californians hang in the balance. (*See* Cal. Rules of Court 8.552(c).) While case law interpreting Rule 8.552 is sparse, the Supreme Court has invoked original jurisdiction over writ petitions under a similar standard in cases affecting many fewer people.

For instance, in *Lockhart v. Wolden* (1941) 17 Cal.2d 628, the Court entertained an original writ petition from a female World War I veteran who claimed she was improperly denied veteran property tax relief because she was a woman. In accepting the original writ, the Court noted the question of whether the tax break extended to female veterans was of "considerable public importance" because it affected approximately 2,000 women in the state. The Court also noted that any other procedure would involve a "multiplicity of suits," which would merely delay relief for a class of persons who could be given final relief by the issuance of a single writ.

Likewise, in *Hollman v. Warren* (1948) 32 Cal.2d 351, this Court invoked original jurisdiction over a writ petition to compel the Governor to consider additional appointments of notaries public in the City and County of San Francisco, because the

question concerned "the entire City and County of San Francisco, a populous city." (*Id.* at 357; *see also Lindell Co. v. Bd. of Permit Appeals of City & Cnty. of San Francisco* (1943) 23 Cal.2d 303 (exercising transfer rights to an original petition from a homebuilder denied a building permit by the City and County of San Francisco during World War II, citing the urgent need for 1,000 additional homes in the city to support the defense industry).)

If this Court has found cases affecting the rights of thousands of Californians justified expedited review, this case, which affects ***millions*** of Californians, is *a fortiori* worthy of expedited review.

II. The Court Should Transfer the Appeal to Itself, Because It Presents a Pure Question of Law, the Resolution of Which Would Avoid Wasteful, Duplicative Litigation Below

California's trial courts already faced an unprecedented backlog before the pandemic. Now, a new wave of litigation brought on by insurance companies' summary denials of COVID-19 insurance claims threatens to engulf the lower courts. Insurers demonstrably intend to fight these lawsuits tooth-and-nail, and this kind of scorched-earth litigation has the capacity to overwhelm trial and appellate courts.

At the heart of this dispute is a legal question of policy interpretation: Can the standard form "loss of or damage to" policy wording drafted by insurers be reasonably construed to cover losses resulting from COVID-19? (*See, e.g., Waller v. Truck Ins. Exch., Inc.* (1995) 11 Cal.4th 1, 19 ("[W]e are guided by the

principle that interpretation of an insurance policy is a question of law").)

Resolution of this question would resolve a threshold issue in virtually every COVID insurance case pending below. There is no need to wait on multiple trial courts and appellate courts to separately consider this issue. The question is bound to arrive before this Court eventually on appeal or by receipt of a certified question from the federal courts. Delaying consideration "until some future case" would only force protracted litigation in the Superior Courts, the Courts of Appeals, and federal courts applying California law — a "wasteful" exercise for litigants (including the parties here) and a morass for California's trial courts. (*Cedars-Sinai Med. Ctr. v. Sup. Ct.* (1998) 18 Cal.4th 4, 6.) It is thus in the "public interest to decide the issue at this time." (*Id.*)

Petitioner's position — like that of many other policyholders — is that the presence of COVID-19 on insured property clearly constitutes the requisite "damage" as that term is reasonably understood, because its physical presence renders property unsafe and unfit for its intended purpose. The physical presence of coronavirus likewise results in "loss," a separate covered event under the coverage trigger "direct physical loss of or damage to property." (*See Total Intermodal Servs. Inc. v. Travelers Prop. Cas. Co. of Am.* (C.D. Cal. July 11, 2018) No. CV 17-04908 AB (KSX), 2018 WL 3829767, at *3 (*Total Intermodal*) ("to interpret 'physical loss of' as requiring 'damage to' would render meaningless the 'or damage to' portion of the same clause, thereby violating a black-

letter canon of contract interpretation — that every word be given a meaning").)

To be sure, COVID-19 is a novel disease, but there is California precedent for finding property policies cover losses analogous to COVID-19. For example, in *Hughes v. Potomac Insurance Co.* (1962) 199 Cal.App.2d 239, a sudden landslide left a policyholder's home perched on the edge of a cliff, deprived of lateral support and stability. However, there was no danger to the home itself. The court rebuffed the insurer's argument that the loss was not covered, while explaining the meaning of "damage" was much broader than the insurer posited:

> 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 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 policy should not be so interpreted in the absence of a provision specifically limiting coverage in this manner. [The policyholders] correctly point out that a "dwelling" or "dwelling building" connotes a place fit for occupancy, a safe place in which to dwell or live. It goes without question that [the policyholders'] "dwelling building" suffered real and severe damage when the soil beneath it slid away and left it overhanging a 30-foot cliff. Until such damage was repaired and the land beneath the building stabilized, the structure could scarcely be considered a "dwelling building" in the sense that rational persons would be content to reside there.

(199 Cal.App.2d at 248-49 (emphasis added).) Under *Hughes*, a policyholder could reasonably expect a claim constitutes physical loss where the insured property cannot function as intended or the property's integrity is compromised.

In fact, cases throughout the country routinely hold that the "loss" component of the standard form property policy is far more expansive than "damage" to the Insured Property itself. Whether framed as loss of use or functionality for an intended purpose,[10] inaccessibility,[11] or property lost through theft or during transport,[12] they make clear that conditions causing the loss of use of property gives rise to a covered loss.

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[10] *See, e.g., Wakefern v. Liberty Mut. Fire Ins. Co*. (N.J. 2009) 968 A.2d 724 (reviewing a multitude of cases including *Western Fire Ins. Co. v. First Presbyterian Church* (Colo. 1968) 437 P.2d 52 (accumulation of gasoline around and under church rendered it uninhabitable and constituted direct physical loss as the term is used in the policy); and *Southeast Mental Health Ctr, Inc. v. Pacific Ins. Co*. (W.D. Tenn. 2006) 439 F. Supp.2d 831 (physical damage includes loss of use and loss of functionality). *See also General Mills, Inc. v. Gold Medal Ins. Co*. (Minn. Ct. App. 2001) 622 N.W.2d 147, 152; *Pepsico, Inc. v. Winterthur Int'l Am. Ins. Co*. (2005) 806 N.Y.S.2d 709, 711; and *Dundee Mut. Ins. Co. v. Marifjeren* (N.D. 1998) 587 N.W. 2d 191, 194.

[11] *See, e.g., Murray v. State Farm* (W. Va. 1998) 509 S.E.2d 1 (homes rendered inhabitable or unusable because of threat of future rock fall – unsafe for habitation); and *Manpower Inc. v. ICSOP* (E.D. Wis. Nov. 3, 2009) No. 08C0085, 2009 WL 3738099 (portion of office building in which located collapsed).

[12] *See, e.g., Mangerchine v. Reaves* (La. 2011) 63 So.3d 1049, 1056 ("Physical damage is only one kind of 'physical loss' of property; for example, a person can suffer the physical loss of property through theft, without any actual physical damage to property.") (citing *Corbian v. U.S. Auto. Ass'n* (Miss. 2009) 20 So.3d 601, 612 for the proposition that "loss" includes "deprivation of" property)); *see also*

Applying similar logic, courts in other jurisdictions have found that the presence of COVID-19 can constitute "physical loss of or damage to" property, where its presence renders property useless or unsafe for its intended purpose. (*Studio 417, Inc., et al. v. The Cincinnati Ins. Co.* (W.D. Mo. Aug. 12, 2020) No. 20-cv-03127.) While California courts obviously are not bound by decisions in other jurisdictions, the existence of these decisions demonstrates that Petitioner's interpretation of the policy language is reasonable.[13]

Yet, the appellate cases relied upon by Respondent and other insurers in denying these claims do not reflect California insurance principles much less the issues and facts presented here. (*See, e.g., MRI*, 187 Cal.App.4th 776 (a business personal property policy only covering "loss" — not loss ***or*** "damage" — did not cover an MRI machine's failure to "ramp up" after it was demagnetized); *Ward*, 114 Cal.App.4th at 548 (loss of data following a computer

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Total Intermodal, 2018 WL 3829767 (distinguishing loss from damage — reading them synonymously would render loss surplusage).

[13] *See, e.g.,* RESTATEMENT OF THE LAW, LIABILITY INSURANCE § 4 cmt. a ("An ambiguous policy term is a term that has at least two interpretations to which the language of the term is reasonably susceptible when applied to the facts of the case."); *Thomas v. Mut. Ben. Health & Acc. Ass'n* (S.D.N.Y. 1954) 123 F. Supp. 167, 171; *Walker v. Fireman's Fund Ins. Co.* (D. Mont. 1967) 268 F. Supp. 899, 901. Insurers are hard pressed to object to this principle since they frequently cite it when defending their own conduct in bad faith cases. *See, e.g., Aetna Cas. & Sur. Co. v Super. Ct. of Ariz.* (Ariz. Ct. App. 1989) 778 P.2d 1333, 1336; *Abercrombie & Fitch Co. v. Fed. Ins. Co.* (S.D. Ohio Mar. 30, 2011) No. 2:06-CV-831, 2011 WL 1237611, at *7.

crash could not be a direct physical loss of business personal property, because information is not "physical").)[14]

Until this Court provides an interpretation of the phrase "physical loss of or damage to" property, insurers and policyholders alike will expend considerable resources waging war over the scope of the meaning of that phrase during which time many more thousands of businesses will close with their employees losing their jobs and health insurance. And California courts, already stretched thin by COVID-19, will be further extended by this litigation process. Petitioner asks this Court to grant its petition to transfer so that the Court may resolve the issue — crucial to tens of thousands of small businesses — of whether COVID-19 can cause "physical loss of or damage to" property.

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[14] The claims at issue in both *MRI* and *Ward* were for business personal property. This distinction is important, as courts have found alterations to the air inside a building can constitute "physical loss of or damage to" insured property under a building policy. (*See, e.g., Port Auth.*, 311 F.3d at 236 ("When the presence of large quantities of asbestos in the air of a building is such as to make the structure uninhabitable and unusable, then there has been a distinct loss to its owner."); *Gregory Packaging*, 2014 WL 6675934, at *6 (finding that ammonia "physically transformed the air within [the insured's] facility so that it contained an unsafe amount of ammonia or that the heightened ammonia levels rendered the facility unfit for occupancy until the ammonia could be dissipated" constituted "direct physical loss of or damage to" the facility).) Air, on the other hand, is not generally considered to be part of personal property, like an MRI machine or a database.

CONCLUSION

For the foregoing reasons, Petitioner asks that the Court grant its transfer petition.

Dated: October 16, 2020

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CERTIFICATE OF WORD COUNT

Pursuant to California Rules of Court 8.204(c)(1) and 8.504(d)(1), I certify that the text of this Petition is produced using 13-point or greater Roman type, including footnotes, and contains 3,571 words, which is less than the total words permitted by the rules of Court. Counsel relies on the word count of the computer program used to prepare this Petition.

Dated: October 16, 2020

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