Cassels

Business Interruption Insurance Issues

April 6, 2020

The COVID-19 pandemic has created uncertainty for every corporation, industry, individual, governmental authority and enterprise. Various announcements, describing the extraordinary steps all levels of government are prepared to implement to mitigate the harms COVID-19 poses to the health of individuals and the various components of the economy on which those individuals rely, are constant.

These announcements, in most instances, are proactive, in that governments are announcing measures that are intended to assure us that potential economic outcomes caused by factors that are beyond the control of an individual, enterprise, business or non-governmental organization (such as a government-mandated closure of a business) will be delayed until we have the opportunity to correct once the crisis of the pandemic has passed.

These proactive steps, in large measure, appear to recognize there is no one industry or group that can possibly mitigate the unprecedented havoc COVID-19 is wreaking on the local, national and international economy. The economic harm caused by shelter-in-place or ‘stay at home' orders will be so broadly based that no single set of market or industry participants can possibly fashion the type of solution that will right the economy. For this reason, certain commentaries, addressing the recently released Ontario Superior Court of Justice decision *MDS Inc. v. Factory Mutual Insurance Company* [2020 ONSC 1924], raised eyebrows when they suggested Insurers would be the industry participants expected to mitigate many of the COVID-19 harms companies or enterprises suffered due to "business interruption." A careful read of the *MDS Inc.* decision indicates that those commentaries, to the extent they attempt to draw a parallel between the *MDS Inc.* decision and the current COVID-19 pandemic, have overstated the court's ruling.

The facts giving rise to the *MDS Inc.* decision occurred more than a decade ago, when an unanticipated leak of heavy water caused a shutdown of a nuclear reactor at Chalk River, Ontario. ***MDS Inc.* is not a case that resulted from or in any way addresses the COVID-19 pandemic or its impacts.** The determinations of the trial judge are fact-specific, and result from the court's analysis of nine separate experts' reports and the evaluation of the work and opinion of an additional court-appointed expert. The specific language of the worldwide All-Risks policy on which MDS Inc. relied, which the court determined contained ambiguities, is central to the various determinations the court reached. Great care should be applied when reviewing how the court resolved questions such as the applicability of the Corrosion Exclusion under the policy, what treatment was to be given to the Resulting Physical Damage Exemption term of the policy, what was meant by the Idle Period Exclusion listed in the Time Element Exclusions Clause and how ambiguities in those terms, and terms such as the Nuclear Radiation Exclusion were resolved.

Nothing in the *MDS Inc.* decision should be understood or interpreted to mean that clear exclusions for

pandemics or the actual terms of insurance policies limiting the basis for coverage due to business interruption are abridged or abrogated because of the impact of COVID-19. However, the court in the *MDS Inc.* decision, relying on the specific facts before it, interpreted the term "physical damage" in a manner that included the loss of the use of property, even in the absence of actual physical damage.

The court reasoned that such an interpretation was appropriate given the unique factual context of the case, and the "purpose of all-risks property insurance, which is to provide broad coverage." Other portions of the decision, however, are not centred on larger policy-based arguments for coverage, but rather, on very particular findings that the Insurer had knowledge of the unique facts of Chalk River, and its reactor, as well as the "vulnerability" of MDS Inc. The court's findings in this respect included the observation that the Insurer was also the Insurer of the Chalk River facility, and was aware that coverage for the reactor itself had been deleted from coverage for Chalk River in their last renewal – a fact the court indicated was not known by MDS. Inc.

The court's reliance on a prior Canadian decision, which found that fumes resulting from a spill of petroleum products under the plaintiff's business resulted in "physical damage," merits close scrutiny (paragraphs 472 to 474):

"The only case that squarely considers the meaning of physical damage in the context of an all-risks policy in a similar factual context to this case is *Jessy's Pizza*: a Small Claims Court decision in Nova Scotia.

In *Jessy's Pizza*, a vandalized oil line caused an oil spill under the plaintiffs' business. This in turn caused an overpowering smell of oil in the store. The plaintiffs tried to mitigate this problem by leaving open windows and doors, to no avail. They were forced to close. The floor of the restaurant was removed and the contaminated soil beneath was dug out.

Adjudicator Johnston looked at the facts in a pragmatic fashion, confirming that the physical damage coverage applied to both the tangible direct damage to the floor, as well as to the fumes in the restaurant as 'the fumes physically damaged the contents of the business' as the continued operation of the restaurant business was untenable."

There is a strong counter argument that *tangible* direct damages are the more appropriate beginning and end point for what constitutes "physical damage," even in the context of an all-risks policy. Insurers, intermediaries and Insureds have long understood the term "physical damage" to be confined to actual corporal damage which is proximate to a harm – "physical damage" does not extend to impairment of use or function of the whole because of an intangible harm. In the paragraphs immediately before the review of the *Jessy's Pizza* case, the court identifies "…two very different interpretations of the meaning of physical damage in the various cases…," as a basis to suggest that the meaning of "resulting physical damage" is "ambiguous." However, in the next paragraphs, the court seems to make an alternative finding, observing "[a] review of the cases confirms that there is no bright line or a single case that is dispositive of the

meaning of resulting physical damage for this case." In this respect, the *MDS Inc.* decision should not be read as the court enunciating an expansion of the definition of "physical damage" across all policies of insurance, or even those that are all-risks policies. Rather, this decision considered the unique facts the case presented, and interpreted the policy language in that fact-specific context.

The *MDS Inc.* decision is receiving significant attention as Insurers and Insureds consider the proper interpretation of insurance coverages during the unprecedented period of uncertainty created by COVID-19. The *MDS Inc.* decision, however, should not be viewed as a precedent that binds subsequent courts hearing such cases during the COVID-19 era. Rather it, and some of the commentaries about it, should be viewed as a warning sign that courts may be implored (and possibly tempted) to become more sympathetic to intervention or public policy arguments regarding the interpretation of insurance policy language. In effect, courts may see an influx of legal arguments and positions which seek to have the courts extend coverage as a form of social benefit, even in the face of clear policy language. Demands that courts fashion societal-enhancing remedies in cases where clear policy language would exclude relief to Insured claimants, notwithstanding the crisis conditions resulting from the COVID-19 pandemic, will be made.

Concerns of many Insurers that courts will signal a change in approach to interpreting the coverages under insurance polices are also growing. California's courts may be the first to consider COVID-19 related business interruption coverage disputes. Renowned Chef Thomas Keller and owner of world-famous Yountville restaurants the French Laundry and Bouchon Bistro, which have been adversely impacted by the shelter-in-place order issued in California, filed suit in Napa County Superior Court against Hartford Fire Insurance Company seeking a declaration in favor of coverage for the plaintiffs' business interruption losses. (*French Laundry Partners, LP dba The French Laundry, a Limited Partnership; KRM, Inc. dba Thomas Keller Restaurant Group, a Corporation; Yountville Food Emporium, LLC dba Bouchon Bistro, a Limited Liability Company v. Hartford Fire Ins. Co., a Corporation; Trumbull Ins. Co., a Corporation, Karen Relucio, an Individual, and; DOES 1 to 25*, inclusive; case number not immediately available, in the Superior Court for the State of California, County of Napa; filed March 25, 2020.) In Canada, a Regina-based law firm has issued a national class action against indemnity Insurers in Canada that are not paying business owners for losses accumulated due to the COVID-19 pandemic. Beyond the courts, Massachusetts, Ohio and New Jersey have each introduced bills that purport to rewrite existing insurance policies to cover businesses' economic losses arising from Covid-19 work stoppages. In addition, many US state Insurance Commissioners (who are often elected rather than appointed) have started to advocate that Insurers take a liberal approach to paying any COVID-19 related claims. A similar pattern of judicial and regulatory intervention has been seen in the past with other catastrophic events. As an example, in the aftermath of Hurricane Katrina, the Louisiana Commissioner of Insurance ordered Insurers to pay homeowners' claims notwithstanding a clear flood exclusion in most polices.

It is clear that COVID-19 is creating an entirely new set of health, economic and social problems for everyone. Insurers must be responsible partners in the fight against COVID-19. It is important that their service levels to the public, particularly with respect to claims, remain as uninterrupted as possible. It is also

important that they show flexibility in areas such as grace periods for failure to renew polices on time or for late payment of premiums. However, industry participants should never become vehicles by which courts transfer to Insurers COVID-19 burdens that were never contemplated in the contract of insurance

The Insurance Bureau of Canada has indicated that the Canadian insurance industry wrote in total $59.6 billion in Gross Written Premium in 2018 for home, automobile and business insurance. The Canadian government has announced relief payments to the Canadian taxpayer well in excess of that amount. The ultimate responsibility to fairly allocate what will be the extremely high costs of COVID-19 must belong to the legislative branch of government. Any invocation to the courts to create remedies for claimants, despite clear policy language, represents an exponentially greater harm for all participants and stakeholders of the insurance industry than can be justified by any individual result, no matter how equitable such a result may seem.
