

# ANDERSON KILL NEW JERSEY

# ALERT

## Michigan Court Issues First Insurance Coverage Decision Regarding COVID-19 Business Interruption

By Robert D. Chesler, Nicholas M. Insua, and John P. Lacey, Jr.

The first court directly to address insurance coverage for COVID-19 business interruption has ruled against coverage. In ruling from the bench, the *Gavrilides v. Michigan* court held that COVID-19 did not constitute physical loss or damage, the requisite trigger for business interruption coverage.<sup>1</sup> This decision is consistent with dicta from *Social Life Magazine, Inc. v. Sentinel Ins. Co.*<sup>2</sup> where the court, in ruling that injunctive relief was not available to the policyholder, opined that physical loss or damage had not occurred. Policyholders have several takeaways from these decisions.

First, New Jersey law, and the law in several other jurisdictions, is different. The New Jersey appellate division's decision in *Wakefern*<sup>3</sup> found business interruption coverage where there was no physical alteration of property. In that case, the northeastern grid shut itself down to prevent any damage. The members of the policyholder, a supermarket cooperative, experienced food spoilage and business interruption. Despite the lack of a physical, tangible injury that altered property, the court found in favor of coverage. Specifically, the court held that the loss of functionality of the system constituted physical loss or damage as a matter of law. The court grounded its decision in fundamental precepts of New Jersey law regarding insurance policy construction, relying on the doctrines of ambiguity and reasonable expectations.

Thereafter, *Gregory Packaging*<sup>4</sup> stayed the course. In *Gregory Packaging v. Travelers*<sup>5</sup> a release of ammonia inside a facility led to the evacuation, and loss of use, of the facility. The insurance company specifically argued that physical loss or damage must involve a physical change or alteration to insured property requiring its repair or replacement.

The court disagreed. It held that

... the ammonia discharge inflicted "direct physical loss or damage to" Gregory Packaging's facility as that phrase would be construed under New Jersey law by the New Jersey Supreme Court, because the ammonia physically rendered the facility unusable for a period of time.

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Thus, New Jersey policyholders have important case law support for the proposition that loss of functionality and use constitutes physical loss or damage.

A second takeaway is that the war over insurance coverage for COVID-19 business interruption is far from over. In fact, the war is in its infancy, and almost all courts have yet to determine whether COVID-19 constitutes direct physical loss. Insurance coverage law is state law, and each of the 50 states will have its own coverage analysis. Ultimately, the highest court in each state may need to rule on these issues. Policyholders must expect a protracted fight with the insurance industry over coverage for COVID-19 business interruption. Policyholders will see victories and losses as this process unfolds, and should not read too much into preliminary rulings.

Third, it is estimated that policyholders have filed over 200 COVID-19 business interruption complaints to date. Attorneys inexperienced in insurance coverage have filed the majority of these complaints, and many of them have not presented their cases well. For example, it is imperative for policyholders to emphasize the physical nature of the coronavirus, such as the way it travels from person to person, stays on surfaces for several days, and remains airborne for hours. The policyholders in *Gavrilides* and *Social Life* apparently failed to sufficiently plead any insured property damage, making their complaints ripe for motions to dismiss.

As noted, law on insurance coverage for COVID-19 business interruption loss is only beginning to develop. Every company suffering such a loss should file a claim with its property insurance company. After receiving a denial, the policyholder need not make a decision on whether to litigate its claim immediately. Rather, it can wait to see how courts in its jurisdiction are treating such claims. However, companies that decide to wait must be cognizant that most property policies contain enforceable contractual limitations periods, typically two years (but variable), that override statutes of limitations and reduce the period in which the policyholder can sue. Policyholders should also consider whether they want to get ahead of the curve, and not leave others to make bad precedents for them.

Finally, although the court in *Gavrilides* ruled against coverage, courts in other jurisdictions will not be bound by that decision. Insurance coverage for COVID-19 business interruption will be a highly contested source of litigation for years to come. Given the amount of COVID-19 complaints filed, it is likely that at some point courts in each state will have an opportunity to weigh in, and decide whether COVID-19 constitutes a direct physical loss. Therefore, as the insurance coverage battle over COVID-19 business



interruption continues, it is critical that policyholders keep abreast of developments in their respective jurisdictions to better understand how courts are deciding these issues . ▲

## ENDNOTES

1 *Gavrilides Mgmt. Co. v. Michigan Ins. Co.*, (Mich. Co. Ct. July 1, 2020).

2 *1:20-cv-03311-VEC* (S.D.N.Y. May 14, 2020).

3 *Wakefern Food Corp. v. Liberty Mut. Fire Ins. Co.*, 406 N.J. Super. 524 (App. Div. 2009).

4 *Anderson Kill represented Gregory Packaging in this case.*

5 *Gregory Packaging, Inc. v. Travelers Prop. Cas. Co. of America*, 2014 U.S. Dist. Ct. Lexis 165232 (D.N.J. 2014).

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