PLUNKETT COONEY

Direct Physical Loss, Physical Loss, Known Loss Coverage Update

June 15, 2022

Direct Physical Loss or Physical Damage – Wisconsin

Colectivo Coffee Roasters, Inc. v. Soc'y Ins.
--- N.W.2d ---, No. 2021AP463, 2022 WL 1758674 (Wis. June 1, 2022)

The Supreme Court of Wisconsin unanimously held that state-mandated closures of in-person dining did not amount to direct physical "loss" of or "damage" to insureds' properties.

A group of insured bars and restaurants brought a putative class action against their insurer for declaratory and injunctive relief and damages for breach of contract, after claiming that state-mandated restrictions on in-person dining due to the COVID-19 pandemic were compensable losses under their respective policies. The trial court denied the insurer's motion to dismiss, and the Wisconsin Supreme Court granted the insurer's petition to bypass the Court of Appeals.

The Supreme Court of Wisconsin disagreed with the trial court's denial of the insurer's motion to dismiss, finding that no direct physical "loss" or "damage" occurred. The Supreme Court held that an insured suffers physical "loss" of its property when the property is destroyed or affected to such an extent that it cannot be repaired. Moreover, physical "damage" is harm to tangible characteristics of the property that does not rise to the level of physical loss.

The Supreme Court held that the state-mandated closures due to the COVID-19 pandemic did not amount to direct physical "loss" of or "damage" to the property of the insureds' bars and restaurants. The Supreme Court reasoned that the presence of the virus did not alter the appearance, shape, color, structure or other material dimension of the property; the virus was not a physical peril that made merely entering the structure hazardous; and the policies made a clear distinction between loss of use and physical loss of or damage to property. Therefore, the Supreme Court reversed the trial court's order and remanded the case with instructions to grant the insurer's motion to dismiss.

By: Michael Hanchett

Known Loss and Impaired Property Exclusions – Ninth Circuit (California Law)

Monterey Prop. Assocs. Anaheim, LLC v. Travelers Prop. Cas. Co. of Am.
No. 21-55541, 2022 WL 2062909 (9th Cir. June 8, 2022)

Monterey Property Associates Anaheim, LLC (MPAA) was sued by its tenant, Fitness International, LLC, d/b/a LA Fitness (LA Fitness) based on MPAA's refusal to repair a defective roof over LA Fitness's swimming pool. In failing to do so, LA Fitness was forced to permanently close its pool because of dangers posed by the roof. LA Fitness subsequently sued MPAA, which tendered the action to its commercial liability insurer, Travelers Property Casualty Company of America (Travelers). Travelers denied coverage because of (1) a "policy exclusion for 'property damage' to property that [the insured] own[s] or rent[s]" and (2) lack of coverage "for 'property damage' that was known prior to the policy period." MPAA then initiated a lawsuit against Travelers in the U.S. District Court for the Southern District of California. The trial court granted summary judgment in favor of Travelers, finding that MPAA knew of the defective roof prior to the inception of the policy. MPAA appealed.

The U.S. Court of Appeals for the Ninth Circuit agreed with the trial court's ruling, adding that Travelers was also entitled to deny coverage under the policy's "impaired property" exclusion. The appellate court explained that under the Travelers policy, property damage is not covered to the extent that an insured knew that the damage had already occurred before the policy period started. The appellate court recognized that there was "ample evidence in the record to support" that MPAA knew of the damage to LA Fitness's roof before the Travelers policy period began. MPAA did not dispute this finding, however, it argued that LA Fitness's pool closure was not a continuation of the roof damage, but a different type of loss. The appellate court rejected this argument, reasoning that the roof damage was the only proffered reason for the pool closure, and as such, it constitutes a known loss.

The appellate court additionally held that the Travelers policy excluded coverage under the "impaired property" exclusion, which excludes damage to "property that has not been physically injured, arising out of ... [a] delay or failure by [the insured] or anyone acting on [the insured's] behalf to perform a contract or agreement in accordance with its terms." The appellate court held that the impaired property provision applied because MPAA did not dispute that LA Fitness's pool closure was caused by its own delay in performing its duties under its lease contract with LA Fitness. As such, the appellate court concluded that MPAA's arguments on waiver, estoppel, and ambiguity were without merit and that the trial court did not err by granting summary judgment on MPAA's remaining claims for breach of the implied covenant of good faith and fair dealing or declaratory relief.

By: Danielle Chidiac

Direct Physical Loss or Physical Damage – Sixth Circuit (Ohio Law)

Troy Stacy Enter. Inc. v. Cincinnati Ins. Co.
No. 21-4008, 2022 WL 2062001 (6th Cir. June 8, 2022)

The U.S. Court of Appeals for the Sixth Circuit upheld the federal district court's dismissal in favor of defendant Cincinnati Insurance Company (Cincinnati) and against Troy Stacy Enterprises Inc. and six

other businesses (plaintiffs) in a case in which plaintiffs sought to recoup economic losses attributable to the COVID-19 pandemic. The appellate court ruled that plaintiffs failed to state a claim because they had not plausibly alleged either "physical loss" or "physical damage" as required under their policies.

Plaintiffs held property insurance policies with Cincinnati. After the COVID-19 pandemic broke out in March 2020, civil orders were issued in the home states of the businesses, which included Ohio, West Virginia, Minnesota, Illinois, and Pennsylvania. The plaintiffs alleged that they lost income and incurred other expenses to comply with the orders. Cincinnati denied the plaintiffs' claims for reimbursement for "direct physical loss or damage" to property. Four separate suits were filed against Cincinnati, which were eventually consolidated. Cincinnati moved to dismiss the consolidated suit, and the district court granted the motion, concluding that "whether the 'loss' comes by way of the virus, the disease, or government closure orders, under every applicable state's law, [plaintiffs'] reading asks too much of the policy language."

On appeal, the appellate court affirmed the district court's ruling, and in so doing explained that under Ohio law, plaintiffs were entitled to business income coverage only if the presence of the COVID-19 virus on insured property or the civil authority orders constitutes "direct accidental physical loss or accidental physical damage." Plaintiffs argued that the virus met this standard by "corrupting, attaching to, and physically ... altering [their] surfaces" and by "necessitating remedial measures" such as cleaning. The appellate court disagreed and concluded that "physical loss or damage contemplated by the policy is not the same as a loss of use due to the temporary, surface-level presence of a virus."

By: Joshua LaBar