

Two State Supreme Courts Rule That COVID-19-Related Business Losses Do Not Allege Physical Loss Or Damage (Insurance Law Alert)

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The highest courts in Iowa and Massachusetts have ruled that pandemic-related business losses are not covered by all risk property policies, concluding that allegations relating to the COVID-19 virus do not allege physical loss or damage.

In *Verveine Corp. v. Stratmore Ins. Co.*, 2022 WL 1180061 (Mass. Apr. 21, 2022), the Supreme Judicial Court of Massachusetts ruled that losses incurred by restaurants in the wake of government shutdown orders were not covered by all risk property policies because there was no “direct physical loss of or damage to” property. In so ruling, the court emphasized that the relevant inquiry is “not whether the virus is physical, but rather if it has direct physical effect *on property* that can be fairly characterized as ‘loss or damage.’” (Emphasis in original). Noting that every federal appellate court in the nation has required some “distinct, demonstrable, physical alteration of the property,” the court concluded that no such loss or damage is alleged in the context of COVID-19-related business losses stemming from government restrictions.

Further, the court held that allegations of viral “presence” do not amount to physical loss or damage, stating: “Evanescence of a harmful airborne substance that will quickly dissipate on its own, or surface-level contamination that can be removed by simple cleaning, does not physically alter or affect property.” Having reached this conclusion, the court also held that civil authority coverage was unavailable because there was no damage to properties located nearby to the insured premises.

Finally, the court rejected the policyholder’s contention that the inclusion of a virus exclusion in one policy but not in others created “a clear negative implication” that the policies without the exclusion were intended to cover COVID-19-related claims.

In *Wakonda Club v. Selective Ins. Co. of Am.*, 2022 WL 1194012 (Iowa Apr. 22, 2022), the Iowa Supreme Court granted an all-risk property insurer’s motion for summary judgment, finding that losses suffered as a result of government closure orders were not covered by Business Income and Extra Expense provisions. Addressing this matter of first impression under Iowa law, the court held that a policyholder’s loss of use of its property, without more, cannot satisfy the policy’s “direct physical loss of” property requirement. Because the policyholder disavowed any knowledge that the COVID-19 virus was present at its premises, the court held there was no potential physical element that could implicate coverage.

The court rejected the policyholder’s assertion that coverage was available pursuant to Iowa’s reasonable expectations doctrine, which turns on an ordinary layperson’s understanding of policy coverage, regardless of ambiguity. The court explained that even if a layperson would not understand the difference between “loss” and “damage,” the “physical” requirement “defeats any expectation that the policy provided coverage for any business interruption untethered from a physical loss of the property.”

On the same day that *Wakonda Club* was decided, the Iowa Supreme Court also dismissed a policyholder’s complaint in *Jesse’s Embers, LLC v. Western Agricultural Ins. Co.*, 2022 WL 1194006 (Iowa Apr. 22, 2022). There, the court rejected a claim for business interruption coverage for the same reasons set forth in *Wakonda Club*, and also upheld the insurer’s denial of coverage under a civil authority policy provision. The court reasoned that the government orders were not issued in response to physical loss or damage to nearby property, but rather in order to reduce the spread of the virus.

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