

NJ Policyholders Could Still See Recovery For COVID Losses

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To date, New Jersey courts, both state and federal, handling COVID-19 business interruption insurance cases have ruled on at least 32 dispositive motions. Thirty of those motions were resolved favorably to insurers. Yet, policyholders continue to file major COVID-19 business interruption insurance coverage cases in New Jersey and elsewhere.

So, what gives and is there any reason for policyholder optimism? The surprising answer is yes. Depending on the nature of the loss and the precise policy language at issue, there remains a plausible path to policyholder insurance recoveries in response to COVID-19 business interruption losses.

Insurers have relied primarily on two bases for denying coverage in response to COVID-19 business interruption insurance claims: (1) the coronavirus and COVID-19 do not result in direct physical loss of or damage to property; and (2) some form of a virus exclusion bars coverage.

Of the 30 New Jersey cases decided favorably to insurers, a full 28 involved a virus-related exclusion. As a consequence, the federal and state courts sitting in New Jersey have largely not opined on the direct physical loss of or damage to property issue. That is significant because not all insurance policies are created equal and many do not contain a specific virus-related exclusion.

Only six of the 23 federal court decisions going the insurer's way address the direct physical loss of, or damage to, property issue, and all six of those decisions were decided in the U.S. District Court for the District of New Jersey by a single judge, U.S. District Judge Susan Wigenton. No other federal court sitting in New Jersey has addressed the direct physical loss of or damage to property issue.

Further, of the seven New Jersey state court cases resolved favorably to the insurer, six involved the same standard-form virus-related exclusion drafted by the Insurance Services Office Inc. That exclusion provides, in pertinent part:

We will not pay for loss or damage caused by or resulting from any virus, bacterium or other microorganism that induces or is capable of inducing physical distress, illness or disease.

The remaining New Jersey state court case decided favorably to the insurer, *Savage City Strength LLC v. Covington Specialty Insurance Co.* decided on April 8 by the New Jersey Superior Court for Somerset County, contained an exclusion for "pathogenic or poisonous biological or chemical materials" and the court held that the exclusion was applicable to viruses and precluded coverage.

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Only five New Jersey state court opinions directly address the direct physical loss of or damage to property issue.

Those opinions are almost evenly split, with two, *Optical Services USA/JCI v. Franklin Mutual Insurance Co.* and *Westfield Area YMCA v. North River Insurance Co.*, resolved in favor of the policyholder.

In holding for the policyholder in the *Optical Services* matter decided on Aug. 13, 2020, the New Jersey Superior Court for Bergen County reasoned that there was no controlling legal authority on the issue. Ultimately, the *Optical Services* court reached the "inevitable conclusion" that the policyholder

should be afforded the opportunity to develop their case and prove before this Court that the event of the Covid-19 closure may be a covered event under the Coverage C, Loss of Income, when occupancy of the described premises is prohibited by civil authorities.

The court observed further that the requisite physical damage may occur when the policyholder loses the functionality of its property:

There is an interesting argument made before this Court that physical damage occurs where a policy holder loses functionality of their property and by operation of civil authority such as the entry of an executive order results in a change to the property.

As held in *Optical Services*: (1) the insurer was unable to proffer any controlling legal authority for dismissal; (2) the policyholder should be afforded the opportunity to develop its case; and (3) the policyholder made an interesting argument that physical damage occurs when a policyholder loses functionality of its property.

Similarly, on Jan. 8, the New Jersey Superior Court for Union County concluded in *Westfield YMCA* that the policyholder should be permitted to take discovery. In denying the insurers' motions to dismiss, the *Westfield YMCA* court stated: (1) "the pleading is certainly sufficient"; and (2) "there is case law in New Jersey that suggests that the physical damage doesn't have to be physical on the premises."

This is not to say that the path to policyholder recovery — even under insurance policies that contain no virus-related exclusion — will be free of hurdles.

As held by the New Jersey Superior Court for Mercer County on April 16, 2020, in *TMN LLC v. Ohio Security Insurance Co.*, one of the New Jersey state court cases that was decided favorably to the insurer, some courts remain disposed to decide the direct physical loss of or damage to property issue favorably to the insurer even on a motion to dismiss.

In rejecting the *Optical Services* holding, the *TMN* court noted some 23 cases decided favorably to insurers after *Optical Services* was decided. The *TMN* court, however, did not account for whether the insurance policies in those insurer-friendly decisions involved a virus exclusion. Indeed, the *TMN* court would have ruled in favor of the insurer — on the basis of a virus-related exclusion — even if the policyholder had cleared the direct physical loss of or damage to property hurdle.

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Overall, only six of New Jersey's 21 county courts have weighed in on these emerging insurance coverage issues, with no appellate rulings to date. The most that can be said at this point is that trial courts situated in New Jersey have generally enforced virus-related exclusions.

Those holdings, however, say little about those insurance policies that do not contain such exclusions and, at this point, no final conclusion can be drawn regarding the direct physical loss of or damage to property issue.

In all, despite the many decisions, the question of whether business interruption insurance is available for COVID-19 losses remains an open question under New Jersey law. Clarity will come only when appellate courts, and ultimately the New Jersey Supreme Court, weigh in.

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