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Insurance Insolvency

An Overview Of COVID-19 Related Legislative, Regulatory, & Litigation Activity & The Potential Impact On Insurer Solvency

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Commentary

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I. The Coronavirus Pandemic

The coronavirus ("COVID-19") pandemic continues to wreak havoc across the globe and in the United States, bringing with it panic, sickness, and mass mortality. The U.S. health care system is under strain. Fortunately, recent reports suggest that cases may have peaked in several areas of the United States. The pandemic and the resulting emergency declarations and stay at home orders have transformed the American way of life, at least temporarily, and are exacting a major toll on the economy.

At the federal level, the third major relief bill—providing $2.2 trillion in financial relief to individuals and businesses impacted by the virus and injecting an additional $4 trillion in liquidity into the economy—was passed by Congress and signed by the President. The Coronavirus Aid Relief and Economic Security Act known as the CARES Act is the largest economic bill ever enacted. The funds for the paychecks protection program portion of the Act already have been exhausted as a result of loan processing at a record pace. As of the time of preparing this publication, a bill providing nearly $500 billion in additional funding for the paychecks protection program portion of the Act, for health care providers, and for COVID-19 testing has passed the Senate and is awaiting a vote by in the House of Representatives. In addition, discussions are underway regarding a so-called "phase four" of federal relief.

Governmental entities have imposed unprecedented travel, movement, and gathering restrictions, and limited or prohibited for a period of time various activities. Exigent circumstances arm governmental entities with greater powers and legitimately require government action. Yet, impacted constituencies are urged to exercise vigilance to protect their rights and prevent government overreach associated with governmental actions, no matter how well-intended. Protests are breaking out as some Americans are starting to challenge government orders.

For insurers in particular, there has been a recent frenzy of legislative proposals and regulatory activity, some of which give rise to considerable concern. Insurance is an important engine fueling the economy. Short-sighted initiatives that undermine the sanctity of insurance contracts and interfere with the risk assumption and transfer mechanisms pose a threat to the insurance industry. Ultimately, they would also be detrimental to both insureds and the economy.

The activities of legislators in several states to create business interruption insurance by abrogating applicable exclusions and requirements in first-party property policies by legislative fiat, the activities of some state insurance regulators, and the volume of claims notifications and early lawsuits seeking coverage for business interruption claims discussed in this article suggest that the COVID-19 pandemic will further fuel social inflation adversely impacting insurers. *See* S.Seaman, K. Burke, J. Selby, and P. Hernandez, "The Legal Trends Behind 'Social Inflation' In Insurance" Law360 (Portfolio Media Feb. 21, 2020). Further, the state legislative activities, in particular, raises the spectrum of impairing insurer solvency and the ability of insurers to pay other claims.

II. Congressional Appeal To Insurers And Legislative Proposals

In a March 18, 2020 letter to insurance industry and broker associations, a bi-partisan group of United States Congress Members urged commercial property insurers to provide business interruption coverage for COVID-19-related losses. The letter, signed by 18 members of Congress, referenced current and prospective shelter-in-place orders and curfews and stated:

> Business interruption insurance is intended to protect businesses against income losses as a result of disruptions to their operations and recognizing income losses due to COVID-19 will help sustain America's businesses through these turbulent times, keep their doors open, and retain employees on the payroll. During times of crisis, we must all work together. We urge you to work with your member companies and brokers to recognize financial loss due to COVID-19 as part of policyholders' business interruption coverage.

In a joint response, the American Property Casualty Insurance Association, the Council of Insurance Agents and Brokers, the Independent Insurance Agents & Brokers of America, and the National Association of Mutual Insurance Companies stated:

> Standard commercial insurance policies offer coverage and protection against a wide range of risks and threats and are vetted and approved by state regulators. Business interruption policies do not, and were not designed to, provide coverage against communicable diseases such as COVID-19. The U.S. insurance industry remains committed to our consumers and will ensure that prompt payments are made in instances where coverage exists.

President Trump spoke about business interruption insurance during an April 10, 2020 task force press conference, stating he "would like to see the insurance companies pay" if coverage is there. He noted that sometimes there is an exclusion, but urged insurers to promptly pay losses where it is fair to do so. Seven Republican U.S. Senators wrote to President Trump advising that retroactively requiring insurers to cover perils that were not contemplated would imposed significant economic strain on insurers that could result in insurer insolvencies given the magnitude of the estimated claims.

We are not aware of any executive action with respect to existing property policies.

All of this dialogue, standing alone, does not pose an active threat to the insurance industry unless it results in legislative action or executive order.

There are two potential federal pieces of federal legislation that insurers may wish to track in connection with business interruption losses stemming from pandemics – neither of which as currently drafted would apply to the current COVID-19 pandemic.

The first bill circulating in draft form is the so-called "Pandemic Risk Insurance Act of 2020." The proposed legislation, as currently constructed, would establish a federal backstop for pandemic insurance industry losses in excess of $250 million. Specifically, it would create "a Federal program that provides for a system of shared public and private compensation for business interruption losses resulting from a pandemic or outbreak of communicable disease." The bill would have similar features to the Terrorism Risk Insurance Act and losses in excess of an individual insurer's deductible would be shared between the federal government and the individual insurer, with the government paying 95%. The program would be triggered when industry losses exceed the $250 million threshold and aggregate losses would be capped at $500 billion in a calendar year for both insurers and the government. Insurers that participate in the program would be charged an annual premium for reinsurance coverage, "based on the actuarial

cost of providing such reinsurance coverage, including costs of administering the program," the bill states. In return for a federal backstop on pandemic losses, insurers would agree to make available business interruption insurance coverage for insured losses that does not "differ materially from the terms, amounts and other coverage limitations applicable to losses arising from events other than public health emergencies," the proposed bill states. Participation by insurers would be voluntary, but those participating would be required to provide detailed data on their business interruption exposures. Participating insurers would also have to nullify some existing business interruption exclusions and lawmakers would be given powers to extend the scheme to captives and self-insurance arrangements. We understand that multiple versions of the bill are circulating among lawmakers and revisions are being made.

The second active proposal is the "Business Interruption Insurance Coverage Act of 2020," which was announced on April 14, 2020 by United States Representative Mike Thompson (CA-05). He described the purpose of the bill as ensuring businesses that purchase interruption insurance will not get their claims denied because of major events, such as the Coronavirus pandemic, public safety power shutoffs or evacuations.

Section 2 of H.R. 6694 provides that, effective upon the date of the enactment,

> [E]ach insurer that offers or makes available business interruption insurance coverage shall make available, in all of its policies providing business interruption insurance, coverage for losses resulting from (A) any viral pandemic; 10 (B) any forced closure of businesses, or mandatory evacuation, by law or order of any government or governmental officer or agency, including the Federal Government and State and local governments; or (C) any power shutoff conducted for public safety purposes; and (2) shall make available business interruption insurance coverage for losses specified in paragraph (1) that does not differ materially from the terms, amounts, and other coverage limitations applicable to losses arising from events other than those specified in paragraph (1).

Under Section 3, any exclusion in a contract for business interruption insurance that is in force on the date of enactment shall be void to the extent that it excludes losses specified in Section 2. Further, Section 3 purports to preempt state law. It provides that any State approval of any exclusion of losses from a contract for business interruption insurance that is in force on the date of the enactment of this Act shall be void to the extent that it excludes losses specified in section.

The proposed bill provides that an insurer may reinstate a preexisting provision in a contract: (1) if the insurer has received a written statement from the insured that affirmatively authorizes such reinstatement; or (2) if the insured fails to pay any increased premium charged by the insurer for providing such business interruption coverage after receiving notice.

The text of the bill raises several issues, but by its own terms – like the other federal legislative proposal – the bill would not apply to the instant COVID-19 pandemic-related claims.

III. Proposed State Legislation

Legislative bodies in several states are entertaining extraordinary legislation that would force insurers to provide coverage for claims, even where such claims do not meet the terms of coverage or are expressly excluded under insurance policies. Such retroactive nullification of contract represents an unwarranted assault on the insurance industry and on parties' freedom to contract. Additionally, these measures threaten to undermine the insurance regulatory structure as many of these contract provisions were subjected to the regulatory process and approved by insurance regulators. What's more, these proposals fail to account for potential reinsurance ramifications.

Further, such bills, if enacted, could threaten insurer solvency. The Global Federation of Insurance Associations warned that the financial stability of the insurance industry could be at risk if governmental entities ordered policies to be retroactively changed to cover disruption caused by COVID-19 and result in insurers being unable to pay other types of claims. The actual amount of business interruption losses is difficult to calculate. On March 31, the Congressional Research Service ("CRS") issued a report to Congress in which it discussed the issue of business interruption insurance coverage. In the report, CRS noted that some industry sources have estimated the cost of covering business interruption claims for small businesses to range from

$110 billion to $290 billion, monthly. The American Property Casualty Insurance Association estimates that small businesses are losing $255 billion to $431 billion of income monthly from the pandemic as compared to $6 billion in monthly premium received by insurers on commercial property insurance.

It should be noted that A.M. Best revised its outlook for the United States commercial lines insurance industry from stable to negative. A.M. Best appears to be more concerned with the economic slow-down from the COVID-19 pandemic than COVID-19 related claims.

A. The New Jersey Bill

For a variety of reasons, insured entities likely will face an uphill battle when seeking coverage for COVID-19 losses under most commercial insurance policies. Perhaps, in recognition of this reality, the New Jersey legislature is considering extraordinary legislation, Assembly Bill 3844, which would rewrite property insurance policies to provide coverage for COVID-19 business interruption losses—even policies that contain a virus exclusion.

AB 3844, introduced on March 16, 2020, would apply to property policies that were in effect on March 9, 2020 and issued to insureds with less than 100 eligible employees in New Jersey. An eligible employee is a full-time employee who works 25 hours or more in a normal work week. The costs for any paid claims ultimately would be passed on to all insurers operating in New Jersey, except for life and health insurers. The bill is working its way through the legislative process.

B. The Ohio Bill

H.B. No. 589, introduced in the Ohio legislature on March 24, 2020, is intended to require insurers offering business interruption insurance to cover losses attributable to COVID-19. The bill provides: "every policy of insurance insuring against loss or damage to property, which includes the loss of use and occupancy and business interruption, in force in [Ohio] on the effective date of this section, shall be construed to include among the covered perils under that policy, coverage for business interruption due to global virus transmission or pandemic during the state of emergency."

Further, "[t]he coverage required by this section shall indemnify the insured, subject to the limits under the policy, for any loss of business or business interruption for the duration of the state of emergency.

The "state of emergency" refers to Executive Order 2020-01D issued on March 9, 2020.

By its express terms, this bill applies only to policies enforced as of the effective date issued to insureds located in Ohio that employ 100 or fewer eligible employees.

The bill would allow an insurer who pays for applicable COVID-19-related losses to request from the Ohio Superintendent of Insurance "relief and reimbursement from funds collected and made available" for the purpose of the bill. Further, the bill would require the Superintendent to establish procedures for insurers to submit reimbursement claims, and pay the claims either from such funds as are available to the Superintendent and to create a "Business Interruption Fund" and charge an assessment to insurers in the necessary amount required to recover amounts paid to insurers that submit claims for reimbursement.

C. The Massachusetts Bill

Massachusetts bill S.D. 2888 appears to go further than the New Jersey and Ohio bills. It provides: "[E]very policy of insurance insuring against loss or damage to property, notwithstanding the terms of such policy (including any endorsement thereto or exclusions to coverage included therewith) which includes, as of the effective date of this act, the loss of use and occupancy and business interruption in force in the commonwealth, shall be construed to include among the covered perils under such policy coverage for business interruption directly or indirectly resulting from the global pandemic known as COVID-19, including all mutated forms of the COVID-19 virus.

Further, no insurer in Massachusetts: "may deny a claim for the loss of use and occupancy and business interruption on account of (i) COVID-19 being a virus (even if the relevant insurance policy excludes losses resulting from viruses); or (ii) there being no physical damage to the property of the insured or to any other relevant property."

The Massachusetts bill provides that the required coverage shall cover the insured for any loss of business or business interruption until such time as the emergency declaration dated March 10, 2020 and designated as Executive Order 591 is rescinded by the governor.

Insurers would not be liable for any payments beyond the "monetary limits of the policy," and would be subject to "any maximum length of time set forth in the policy for such business interruption coverage."

The Massachusetts bill would apply to insureds with 150 or fewer full-time equivalent employees in Massachusetts. Similar to the New Jersey and Ohio bills, it provides that insurers who are required to pay COVID-19-related losses "may apply to the commissioner of insurance for relief and reimbursement from funds collected and made available for such purpose as provided" in the proposed law. The insurance commissioner would be required to establish procedures for the submission and qualification of claims by insurers for reimbursement and pay those claims with funds collected from "assessments" imposed "against licensed insurers in [Massachusetts] that sell business interruption insurance as may be necessary to recover the amounts paid, or estimated to be paid, to insurers" seeking reimbursement. The bill subjects insurers making these mandatory payments to Mass. Gen. Laws Ch. 176D, which provides a list of acts and omissions by insurance companies that constitute "unfair claim settlement practices."

D. The New York Bill

On March 27, 2020, Assembly Bill No. A10226 was introduced. The bill is similar to the other bills discussed above.

Section 1 of the bill provides, at subsections (a) through (c):

> Notwithstanding any provisions of law, rule or regulation to the contrary, every policy of insurance insuring against loss or damage to property, which includes the loss of use and occupancy and business interruption, shall be construed to include among the covered perils under that policy, coverage for business interruption during a period of a declared state emergency due to the coronavirus disease 2019 (COVID-19) pandemic.
>
> The coverage required by this section shall indemnify the insured, subject to the limits under the policy, for any loss of business or business interruption for the duration of a period of a declared state emergency due to the coronavirus disease 2019 (COVID-19) pandemic.
>
> This section shall apply to policies issued to insureds with less than 100 eligible employees [full time employees working 25 hours a week or more] in force on the effective date of this act.

Sections 2 and 3 provide that an insurer may apply to the superintendent of financial services for reimbursement by the department from funds collected and authorizes the superintendent of financial services to charge insurance and make distributions to insurers for this purpose.

This act purports to take effect immediately and to apply to insurance policies in force on March 7, 2020. The proposed act is hardly a model in draftsmanship and suffers from the same deficiencies as the other proposed bills.

E. The Louisiana Bills

On March 31, 2020, Louisiana became the fifth state to enter the fray of potentially mandating insurance coverage losses due to COVID-19. Bills were introduced in the Louisiana state senate and in the house of representatives to require insurers to pay for COVID-19 related business interruption loss regardless of policy requirements and applicable exclusions. Neither bill contains a funding mechanism like those proposed in other states. While the house bill (H.B. 858) is limited to small businesses (meaning 100 or less full time employees in the state) the senate bill (S.B. 477) is not so limited.

House Bill 858 provides:

> Notwithstanding any other provisions of law to the contrary, every policy of insurance insuring against loss or damage to property, which includes the loss of use and occupancy and business interruption in force in this state on the effective date of this Act, shall be construed to include among the covered perils under such a policy, coverage for business interruption due to global virus transmission or pandemic, as provided in the Emergency Proclamation Number 25 JBE 2020 and the related supplemental proclamations concerning the coronavirus disease 2019 pandemic.

House Bill 858 further provides that its provisions "shall be given prospective and retroactive application

and shall be applied retroactively to March 11, 2020" to relevant insurance policies in force on that date. Senate Bill 477 contains substantially similar provisions.

Additional bills are pending in Louisiana. Proposed Senate Bill 506 would require property insurance policies to cover the cost of disinfecting and fumigation of buildings in which a person who tested positive for COVID-19 works or resides.

Finally, Louisiana Senate Bill 495 would create a business compensation fund with a framework to expedite some property insurance claims. Under this bill, insurers issuing policies in Louisiana would have the option to participate in the fund by depositing the greater of $50 million or 80 percent of the aggregate policy limits for all commercial insurance policies that the insurer has in force in Louisiana on March 11, 2020 or anytime thereafter during the state of emergency. Participating insurers would be immune from claims of bad faith by claimants seeking compensation for losses associated with the COVID-19 pandemic. The bill purports to allow a claimant to seek compensation from the fund if they meet certain criteria, including being insured for commercial loss, the insured sustained loss of commercial income or revenue due to coronavirus, the insured agrees to accept 80 percent of actual losses up to the policy limits, and the application for a claim is received by the commissioner of insurance no more than 90 days after the expiration of the emergency declaration. Insurers would be permitted to challenge claims as fraudulent and challenging the amount claimed.

F. The South Carolina Bill

South Carolina legislators have introduced S.B. 1188. This bill, if enacted, would mandate that "every policy of insurance in force in [South Carolina] insuring against loss or damage to property, notwithstanding the terms of the policy and including any endorsement thereto or exclusions to coverage. . . shall be construed to include, among the covered perils under the policy, coverage for loss of use and occupancy, or business interruption, directly or indirectly resulting from the global pandemic known as COVID-19." Further, the proposed bill also provides that "no insurer in this State may deny a claim for a loss of use and occupancy, or business interruption, with respect to COVID-19." The bill applies to insureds with 150 or fewer full-time equivalent employees.

G. The Pennsylvania Bill

House Bill 2372, the Business Interruption Insurance Act, was introduced by 37 legislators in the Pennsylvania Assembly on April 3, 2020. The bill would require that any insurance policy that insures against loss or damage to property, which includes the loss of use and occupancy and business interruption, in force in the Commonwealth on March 6, 2020, shall be construed to include among the policy's covered perils coverage for business interruption due to global virus transmission or pandemic. Coverage would be subject to "the broadest or greatest limit and lowest deductible afforded to business interruption coverage under the insurance policy." "Property damage" is defined as follows: "In a building, office, retail space, structure, plant, facility, commercial establishment or other area of business activity, the direct physical loss, damage or injury to tangible property, as a result of a covered peril, including, but not limited to: (1) The presence of a person positively identified as having been infected with COVID-19. (2) The presence of at least one person positively identified as having been infected with COVID-19 in the same municipality of this Commonwealth where the property is located. (3) The presence of COVID-19 having otherwise been detected in this Commonwealth." The bill would apply to businesses with fewer than 100 eligible employees, defined as full time employees who work a normal work week of at least 25 hours. Like several of the other state proposals, the Pennsylvania bill would establish a process by which insurers could seek reimbursement for paid claims from funds collected from the Commonwealth's property and casualty insurers.

It is difficult to predict the prospects of such bills becoming law or what amendments may be made to the proposed legislation along the way, but it is important that insurers engage with legislators to ensure they understand the adverse consequences associated with these bills, the troubling precedent they present, the likely unintended consequences should these bills become law, and require coverage for which a premium was not paid. Effective education of legislators and advocacy will be particularly challenging in view of social distancing policies currently in place.

These bills, and their abrogation of express contractual provisions and purported application to policies previously priced and executed present a host of legal and constitutional issues, including challenges on the

grounds that states are precluded from retroactively changing contracts by the Contracts Clause of the United States Constitution. The Contracts Clause provides, "[n]o state shall . . . pass any . . . Law impairing the Obligation of Contracts." Under current jurisprudence to prevail upon a Contracts Clause challenge, a party must show that there is a substantial impairment of a contractual relationship and the impairment does not serve a significant and legitimate public purpose. It would appear that insurers could make a strong showing on both prongs.

As noted, such bills, if enacted, could threaten the solvency of insurers. Chubb Ltd. CEO Evan Greenberg recently warned that forcing insurers to pay for losses not covered by policies would bankrupt the industry.

Requiring insurers to pay claims not covered by insurance policies by government fiat is nether sound nor sustainable public policy. Subjecting insurers to such mandates – even with provisions for reimbursement through pools created through state insurance industries – would not provide an efficient mechanism to respond to the fallout from a pandemic.

H. Other Bills And Orders

It is likely that the attempted contract nullification by state legislative fiat may spread to other jurisdictions. For example, there are reports that legislators in Rhode Island are contemplating proposed legislation.

There are a variety of other legislative acts and executive orders impacting various lines of coverage. For example, the Minnesota state legislature passed legislation designed to allow first responders and health care workers battling the COVID-19 pandemic to qualify for workers compensation. The Governor of Missouri issued an executive order allowing first responders to receive workers' compensation benefits if they are diagnosed with or quarantined because of COVID-19. This removes the requirement that an employee prove that he or she became ill while on the job and creating the presumption that a first responder was exposed to the coronavirus while on duty. The Governor of Kentucky issued an emergency order creating a presumption that removal of workers from work by a physician is due to occupational exposure from COVID-19 if they are in a broad list of occupations including healthcare workers, first responders, corrections officers, military, activated National Guard, domestic violence and child advocacy workers, rape crisis, child care and other community-based services workers, and grocery and postal workers.

Similarly, the Illinois Workers Compensation Commission issued an emergency amendment creating a rebuttable presumption that all front-line workers who are injured or incapacitated as a result of exposure to COVID-19 during a state of emergency are presumed to have been exposed to the disease in the course of their employment. Further, the definition of front-line worker was expanded and the amendment provides the injury will be presumed to be "causally connected." Utah enacted legislation amending its workers' compensation act by establishing, under certain circumstances, a rebuttable presumption that a first responder who contracts COVID-19 contracted the virus by accident during the course of performing the first responder's duties as a first responder. These are just some of the examples of other acts and orders related to COVID-19.

IV. Regulatory Activity

COVID-19 has generated considerable regulatory activity as well. We provide some examples below.

A. The Wisconsin Commissioner

The Wisconsin Commissioner of Insurance encouraged insurers to offer flexibility to insureds experiencing economic hardship because of the public health emergency related to COVID-19, including offering non-cancellation periods, deferring premium payments, instituting premium holidays, and accelerating or waiving underwriting requirements. Further, during this period no insurer form filings will be approved absent express action by the Commissioner of Insurance office.

On March 23, 2020, the Wisconsin Commissioner of Insurance ordered that insurers cannot deny a claim under a personal auto policy solely because the insured was engaged in deliver food on behalf of a restaurant, until restaurants resume normal operations. Further, general liability insurers were required to notify restaurant-insureds that hired and non-owned auto coverage is available and, if requested, insurers must provide this coverage.

B. The California Commissioner

On March 18, 2020, the California Insurance Commissioner sent a notice to admitted and non-admitted insurance companies providing life, health, auto, property, casualty, and other types of insurance in California

requesting they give their insureds at least a 60-day grace period to pay insurance premiums in light of COVID-19 and related response measures. The notice also urged steps to eliminate the need for in-person payments, including that "all insurance agents, brokers, and other licensees who accept premium payments on behalf of insurers take steps to ensure that customers have the ability to make prompt insurance payments," such as through online payments.

On March 26, 2020, the California Department of Insurance issued an "urgent data survey" to all admitted and non-admitted insurance companies, seeking information about coverage for COVID-19 business interruption exposures. In the notice, entitled "Request for Information: Business Interruption and Related Coverage in California," the Department stated that recent events "have left California business and the state facing uncertainties and weighing public policy options." In order to understand "the number and scope of business interruption type coverages in effect, and the approximate number of policies that exclude virus such as COVID-19," the Department posed several questions regarding the number of employees of policyholders to which such policies were issued. Responses were required by April 9, 2020.

On April 9, 2020, the Department released a notice requesting insurers to not deny claims under a personal auto insurance policy solely because the insured was engaged in providing delivery service on behalf of a California essential business impacted by the COVID-19 related closures, so long as the delivery driver was operating within the course and scope of his/her duties on behalf of such essential business. There are several aspects to this request, which insurers should review.

On April 13, 2020, the Department ordered insurers to provide initial premium refunds for the months of March and April for the following lines of insurance: private passenger automobile insurance; commercial automobile insurance; workers' compensation insurance; commercial multiple peril insurance; commercial liability insurance; medical malpractice insurance; and any other line of coverage where the measures of risk have become substantially overstated as a result of the pandemic.

The order is premised upon the Department's determination that projected losses on these lines of insurance are now overstated due to the severe curtailment in the activities of policyholders under these lines (*e.g.*, less miles driven, less business revenue, drop in payroll) and that refunds should be provided to policyholders to reflect this decreased risk of loss. Insurers have 120 days to comply.

On April 14, 2020, California Insurance Commissioner Ricardo Lara issued a notice to insurers regarding "Requirement to Accept, Forward, Acknowledge, and Fairly Investigate All Business Interruption Insurance Claims Caused by the COVID-19 Pandemic." The notice did not take any position of business interruption coverage or purport to alter insurance contract language. The Commissioner noted that, despite the Department's on-going guidance to businesses statewide during the COVID-19 pandemic, it has received complaints from businesses, public officials, and others asserting that certain insurers, agents, brokers, and insurance company representatives are attempting to dissuade policyholders from filing a notice of claim under business interruption insurance coverage, or refusing to open and investigate these claims upon receipt of a notice of claim.

The Commission put insurers on notice that they are required to comply with their contractual, statutory, regulatory, and other legal obligations such as those set forth in the California Fair Claims Settlement Practices Regulations in connection with all California insurance claims, including business interruption, event cancellation, and other related claims filed by California businesses. The commissioner noted the Regulations require all insurers and representatives accept any communication from the policyholder or its representative indicating that the policyholder desires to make a claim against a policy that reasonably suggests that a response is expected as a notice of claim. (Regulations, section 2695.5(b).)

As the notice serves as a useful overview of some applicable claims handling requirements, we quote from it below:

> Upon receipt of a notice of claim, subject to certain exceptions, every insurer is required to acknowledge the notice of claim immediately, but in no event more than 15 calendar days after receipt of the notice of claim. (Regulations, section 2695.5(e).) If the acknowledgment of a

claim is not in writing, a written acknowledgment of the receipt and date of the notice of claim must be made in the claim file of the insurer. (Regulations, section 2695.5(e)(1).) Failure of an insurance agent or claims agent to transmit a notice of claim to the insurer promptly will be imputed to the insurer, except where the subject policy was issued pursuant to the California Automobile Assigned Risk Program. (Regulations, section 2695.5(e)(1).) Upon receipt of a notice of claim, the insurer is required to provide the policyholder with the necessary forms, instructions, and reasonable assistance, including but not limited to, specifying the information the policyholder must provide in connection with the proof of claim and begin any necessary investigation of the claim. (Regulations, section 2695.5(e)(2).) Thereafter, every insurer is required to conduct and diligently pursue a thorough, fair, and objective investigation of the reported claim, and is prohibited from seeking information not reasonably required for or material to the resolution of a claim dispute before determining whether the claim will be accepted or denied, in whole or in part. (Regulations, section 2695.7(d).) After conducting a thorough, fair, and objective investigation of the claim, the insurer must accept or deny the claim, in whole or in part, immediately, but in no event more than 40 days after receipt of the proof of claim. The amount of the claim accepted or denied by the insurer must be clearly documented in the claim file unless the claim has been denied in its entirety. (Regulations, section 2695.7(b).) Notice on Requirement to Accept, Forward, Acknowledge, and Fairly Investigate All Business Interruption Insurance Claims Caused by the COVID-19 Pandemic Page 3 April 14, 2020 If the claim is denied in whole or in part, the insurer is required to communicate the denial in writing to the policyholder listing all the legal and factual bases for such denial. (Regulations, section 2695.7(b)(1).) Where the denial of a first party claim is based on a specific statute, applicable law or policy provision, condition, or exclusion, the written denial must include reference to and provide an explanation of the application of the statute, applicable law, or policy provision, condition, or exclusion to the claim. Lastly, every insurer that denies or rejects a third-party claim, in whole or in part, or disputes liability or damages must do so in writing. (Regulations, section 2695.7(b)(1).) Based on the foregoing, every insurer, insurance agent, broker, insurance company representative, and other Department licensees is required to comply with their contractual, statutory, regulatory, and other legal obligations in connection with all California insurance claims, including but not limited to, Business Interruption insurance claims, event cancellation claims, and other related claims filed by California businesses. Additionally, no insurer, insurance agent, broker, insurance company representative, or other Department licensee shall dissuade policyholders from filing a notice of claim under its Business Interruption insurance coverage, or refuse to open and investigate such claims upon receipt of a notice of claim.

C. The New York Department Of Financial Services

In light of anticipated losses arising from the outbreak of COVID-19, New York State's Department of Financial Services ("NYDFS") instructed property/casualty insurers to prepare explanations for their policyholders concerning "commercial property insurance" written in New York that might be implicated by coronavirus-related losses. NYDFS considers commercial property insurance to include business owners, commercial multiple peril, and specialized multiple peril policies, along with substantially similar insurance.

Insurers were required to provide each policyholder a detailed explanation for each policy type, including business interruption, contingent business interruption, civil authority, and supply chain coverage, and explain whether those coverages are implicated by a contamination-related pandemic. insurers are specifically required to explain what types of damage or loss constitutes "physical loss or damage" under various policy forms and to describe the workings of applicable waiting periods.

NYDFS acknowledged that the coverages implicated by COVID-19 may change as the situation evolves, but noted that it considers insurers' "obligations to policyholders a heightened priority." NYDFS also stated that

it is important for insurers "to continue to assist policyholders with the [required] information as developments concerning COVID-19 unfold."

In responding to this and other requests by regulators and policyholders – and in evaluating their exposures – insurers should carefully consider their analyses and explanations of coverage issues in light of the exact policy wordings at issue as well as the relevant facts and applicable law.

D. Utah

The Utah Insurance Department issued Bulletin 2020-2 to provide "guidance for business interruption claims related to COVID-19." The Bulletin "urges insurers to promptly process and pay claims related to. . .COVID-19 - particularly claims for business interruption losses - to minimize the impact to insureds." The Bulletin points to the Utah state Unfair Trade and Settlement Practices statute, as "offer[ing] additional guidance regarding settlement practices."

The above are just some of the many notices, directives, requests, and orders of insurance from state insurance departments relating to COVID-19 that are impacting insurers.

V. Insurance Commissioner Statements On Business Interruption Coverage for COVID-19 Losses

Several state insurance commissioners have weighed in on the issue of coverage for business interruption loss under property insurance policies. In a recent letter to business owners, for example, North Carolina's insurance commissioner stated:

> [Y]our issue with commercial property insurance, specifically business interruption insurance, presents a more difficult problem. Standard business interruption policies are not designed to provide coverage for viruses, diseases, or pandemic-related losses because of the magnitude of the potential losses. Insurability requires that loss events are due to chance and that potential losses are not too heavily concentrated or catastrophic. This is not possible if everyone in the risk pool is subject to the same loss at the same time. Consider the difference, for example, between losses suffered from a hurricane and the losses resulting from COVID-19. The hurricane losses affect certain areas on the coast where the event occurred but the losses from this pandemic cover the entire nation. Therefore, mandating coverage for this size and type of loss while canceling existing exclusions in the policies would end the very existence of the business interruption insurance market as we know it. Recent estimates show that business continuity losses from COVID-19 just for small businesses of 100 employees or fewer could amount to between $220 billion to $383 billion per month. Meanwhile, the total reserve funds for all of the U.S. home, auto, and business insurers combined to pay all future losses is only $800 billion. This type of loss could cripple the insurance industry causing many companies to fail, which would put the protection of homes, automobiles, and businesses at risk. We can't legally force insurers to cover a risk which they didn't intend to cover and which, in some instances, was specifically excluded in the policy.

In response to Frequently Asked Questions on the District of Columbia's Department of Insurance, Securities, and Banking's website, the acting commissioner stated:

> Likely, business interruption insurance will not provide coverage. Communicable diseases are usually excluded. For a business interruption policy to respond, the following conditions will need to be met: 1. Actual loss of business income 2. Suspension of business operation 3. Direct physical loss or damage at the described premises that is from a covered cause Business interruption insurance does not provide coverage for a slowdown or reduction in operations.

On March 17, 2020, Georgia's insurance commissioner issued Bulletin 20-EX-3, in which he noted that "[f]ollowing September 11, Hurricane Sandy, and other disasters, insurers tightened policy language to make clear that property damage was a requirement" for coverage. He further stated that "[v]iruses and disease are typically not an insured peril unless added by endorsement."

In its response to a question about business interruption coverage for COVID-19, the Kansas Department of

Insurance notes on its website that "it is the Department's understanding that it is unlikely that a business policy would cover losses related to COVID-19, as most business policies have communicable disease exclusions." Louisiana's department of insurance responded on its website to a question about business interruption coverage due to civil authority order by noting that "most commercial business interruption policy forms provide coverage only when . . . the civil authority order is due to a covered peril that causes direct physical damage ('virus' is typically not a covered peril. . .."

Mississippi's insurance commissioner has also stated on the insurance department's website that "[u]nder the business interruption or business income policy, there likely is no coverage [for losses resulting from a business shut down related to COVID-19] as losses occurring as a result of virus or bacteria are typically excluded by admitted companies." North Dakota's insurance department similarly noted on its website that "it's unlikely that you will find coverage through your business disruption coverage. Generally, the triggering event for coverage would include physical damage; a pandemic is not considered physical damage. Also, under business disruption coverage there can be Civil Authority coverage, this too generally is triggered by physical damage."

In Bulletin No. 20-08, West Virginia's insurance commissioner noted:

> A business interruption insurance policy should clearly list or describe the types of events, commonly known as perils, that it covers. Perils that are not listed or described in the policy, or that are specifically excluded in the policy, are generally not covered. These excluded perils are typically risks that are too great to be underwritten at an affordable price. For example, insurance policies generally contain exclusions for loss or damage caused by war, nuclear accident and radiation. The potential loss costs from such perils are so great that providing coverage would jeopardize the financial solvency of insurers and many businesses could not afford the premium costs to cover such catastrophic events even if they were covered perils. Global pandemics like COVID-19 usually fall into this category of risks or perils that are not covered. Business interruption policies were generally not designed or priced to provide coverage against communicable diseases, such as COVID-19, and therefore usually include exclusions for that risk.

On March 18, 2020, Maryland's Insurance Administration stated that global pandemics fall into a category of risks, such as war, nuclear action and radiation, that "are so extreme that providing coverage would jeopardize the financial solvency of property insurers."

VI. National Association Of Insurance Commissioners

On March 20, the National Association of Insurance Commissioners ("NAIC") held a video conference public session during which state insurance regulators, insurance industry members, and consumer representatives discussed insurance issues arising from the COVID-19 pandemic. Insurance industry representatives urged state regulators to coordinate their various requests for information and data to avoid taxing insurer resources in responding. Insurance industry representatives expressed confidence that, due to adequate reserving, insurers will be able to adequately respond both to health and property-casualty insurance claims related to COVID-19. However, they warned that this may not be the case if states mandate that insurers cover virus-related claims, especially for "business interruption" coverages. Regulators and insurer representatives agreed it is important for legislators to include the insurance industry in discussions about insurance-based solutions to the economic effects of the pandemic.

There was discussion about the need for some regulatory and operational deadlines to be adjusted due to the pandemic's widespread impact on operations, such as extending premium payment dates and insurer financial reporting deadliness.

On March 25, the NAIC released a statement opposing any legislative proposals that would require insurers to retroactively pay unfunded COVID-19-related business interruption claims not covered under insurance policies.

VII. Developments In The United Kingdom

Similar developments are taking place in the United Kingdom. For example, the parliamentary Treasury Committee has written to the Association of British

Insurers requesting extensive data on how its members plan to approach claims for losses in connection with COVID-19.

The Treasury Committee has requested detailed data from insurers about their response to the crisis, including how many companies have stopped offering some products during the crisis or changed their terms; how much they expect to pay out in COVID-19-related claims; their approach to addressing claims under policies providing business interruption insurance; details about communications with policyholders regarding the insurance implications of COVID-19. The committee warned insurers it expects a swift response and will be making all data it receives publicly available.

The Association of British Insurers said insurers in Britain could be hit with $329 million in claims over the crisis, the highest pay-out on record for passenger flight cancellations. Britain's Financial Conduct Authority wrote to insurers on Thursday urging them to show fairness and flexibility when assessing claims related to the coronavirus.

Meanwhile, Lloyd's of London reports that it expects coronavirus claims to impact up to 14 different business lines this year.

On April 15, 2020, the Financial Conduct Authority ("FCA") issued guidance to insurers on its expectations with respect to insurers' conduct concerning business interruption. It acknowledged that most policies providing basic coverage, do not cover pandemics, and create no obligation for insurers to pay COVID-19 pandemic business interruption claims. However, under policies where an insurer has an obligation to pay, the insurer must assess and pay valid COVID-19 claims without delay. The FCA urged insurers to make interim payment and, where an insurer does not agree to do so it must communicate its grounds for making that decision directly to the FCA, including details of how its decision represents a fair outcome for customers.

VIII. The Coverage Litigation Begins

Against this remarkable political, legislative, and regulatory backdrop, the first COVID-19 insurance coverage actions have been filed in courts throughout the United States. The early coverage filings have focused on coverage for business income losses under property insurance policies, some of which allegedly provide Business Interruption, Interruption by Civil Authority, Limitations of Ingress/Egress, and Extra Expense coverages.

The plaintiffs in most of the coverage actions have been restaurants, bars, theaters, retailers, and other small businesses that have been adversely impacted by the pandemic and by governmental closure orders. An increasing number of these early cases are proposed class actions. In *Billy Goat Tavern*, one of the first putative class actions, an Illinois restaurant chain seek relief on behalf of a proposed class of all Illinois businesses offering food or beverage for on-premises consumption that were insured by the same insurer under the same all-risk form and were denied coverage for their COVID-19 related business loss claim.

Several lawsuits have been brought by Native American Tribe Nations for losses sustained by "multiple commercial businesses and services." In those complaints, the Nations seek to preempt any attempt to remove the lawsuits to federal court, stating that they "expressly disavow [ ] any federal claim or question as being part" of their lawsuits, and that the "claims are based in contract and insurance laws" of their state.

A number of complaints contain no allegations that the insureds tendered claims to their insurers in advance of filing their lawsuits, and some policyholders have assert bad faith claims even though it appears that their claims have not been denied. In other cases, the carriers' denials of tendered claims have given rise to statutory and common law bad faith allegations.

In *Big Onion*, for example, the plaintiffs alleged that the insurer "issued blanket denials to Plaintiffs for any losses related to Closure Orders – often within hours of receiving Plaintiffs' claims — without first conducting any meaningful coverage investigation, let alone a 'reasonable investigation based on all available information' as required by Illinois law." The *Big Onion* plaintiffs also cited a memorandum from the CEO of the insurer that had been circulated to its "agency partners" prior to some of the claims being tendered, "acknowledging that states, such as Illinois, had 'taken steps to limit operations of certain businesses,' but prospectively concluding that [the insurer's] policies would likely not provide coverage for losses due to a 'governmental imposed shutdown due to COVID-19 (coronavirus).'"

In *Hair Goals Club*, the plaintiff alleged that the insurer's claim denial violated Texas Insurance Code section 541.061, Misrepresentation of Insurance Policy, as well as other Insurance Code sections concerning the Prompt Payment of Claims. The plaintiff also asserted a claim for breach of the common law duty of good faith and fair dealing, and alleged that the insurer's acts were done "knowingly," as that term is defined in the Texas Insurance Code. In addition to seeking coverage for losses under the policy, the plaintiff seeks attorney's fees and interest, calculated at the statutory amount of 18% per annum. The plaintiff also asked the court to order production of the insurer's claim file and communication with agents, adjusters, and other concerning the claim.

In *Mace Marine*, the insured asked the court to rule that COVID-19 contamination constitutes direct physical loss or damage to property, and asserted a bad faith claim based on the insurer's alleged "general business practice of willful, wanton, immoral, unlawful, malicious and/or deceptive claims handling practices." In *Sandy Point Dental*, the insured based a statutory bad faith claim on allegations that the insurer denied coverage without conducting a reasonable investigation and failed to provide reasonable and accurate explanations for the denial of the claim.

In some lawsuits, the plaintiffs seem to allege that the absence of an exclusion for a particular cause of loss means that the loss is covered. In *Cajun Conti*, for instance, the plaintiffs seek a declaration that "because the policy provided by Lloyd's does not contain an exclusion for a viral pandemic, the policy provides coverage to plaintiffs for any future civil authority shutdowns of restaurants in the New Orleans area due to physical loss from Coronavirus contamination." In *French Laundry*, the plaintiffs ask the court to declare that the relevant governmental order "triggers coverage because the policy does not include an exclusion for a viral pandemic and actually extends coverage for loss or damage due to virus." *See also Prime Time* ("Loss of business Income and operating expenses is specifically covered under the policy, and governmental suspension as a result of COVID-19 is not specifically excluded.")

The presence of a virus exclusion in the policies at issue has not prevented some insureds from pursuing coverage litigation. In one action, an insured restaurant has asked a federal district court in Pennsylvania to rule that the policy's virus exclusion does not apply to its claim. The insured is seeking recovery for losses sustained following governmental orders pursuant to coverage for the loss of business income and extra expenses incurred when access to the insured property is prohibited by order of civil authority as the direct result of a covered cause of loss to property in the immediate area of the insured's property. The insured alleges that restaurants such as itself "are more susceptible to being or becoming contaminated, as both respiratory droplets and fomites are more likely to be retained on the Insured Property and remain viable for far longer as compared to a facility with open-air ventilation," the insured's business is "highly susceptible to rapid person-to-property transmission of the virus, and vice-versa, because the service nature of the business places staff and customers in close proximity to the property and to one another," and the virus is "physically impacting" the insured restaurant. As we've seen in other COVID-19 lawsuits, the insured further alleges that "[a]ny effort by the [insurer] to deny the reality that the virus causes physical loss and damage would constitute a false and potentially fraudulent misrepresentation that could endanger the Plaintiff and the public." With regard to the policy's Exclusion of Loss Due to Virus or Bacteria, the insured seems to allege that the exclusion does not apply on the basis that the losses were caused by governmental orders. Similar to a number of earlier COVID-19 lawsuits, there is no indication that the insured tendered the claim to its insurer or that the claim was denied prior to the filing of the coverage action.

In another action the policy issued to the insured bar/restaurant excluded coverage 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 insured alleged, however, that its loss of business income "was not 'caused by or resulting from' a virus as its loss occurred as a result of the Mayor's Order."

In at least one coverage matter, the insured is seeking coverage under an endorsement that covers various identified pandemic events. The Pandemic Event Endorsement in the *SCGM* case is triggered by the occurrence of certain enumerated diseases. Although the insurer did not deny the insured's claim, the insured filed suit and asserted a claim for "Breach of Contract-Anticipatory Breach/Repudiation" based on a statement

by an alleged "agent" of the insurer to the insured's broker, stating that COVID-19 is not a named disease on the endorsement. The insured also asserted a common law bad faith claim, based on an alleged "internal, high-level directive to automatically deny all pandemic-related business interruption claims," as well as a claim for "Gross Negligence and/or Malice."

We already have seen multiple class action suits filed and requests by insureds for multi-district litigation. The number of theories offered in support of coverage claim has broadened and the type of entities bringing coverage actions has expanded already. Lawsuits will continue at a fast and furious pace. The theories and arguments for coverage will continue to evolve and numerous coverage issues and defenses will be presented. *See generally Insurance Coverage & Reinsurance Primer on Coronavirus (COVID-19) Claims* (Hinshaw & Culbertson LLP 2020).

IX. Conclusion

Developments impacting insurers related to COVID-19 continue at a rapid pace. Insurers and their counsel must monitor developments closely and take appropriate steps to protect their interests. We suspect that most insurers will be able to endure COVID-19 related losses that are covered by the terms, conditions, and exclusions of their insurance policies. Social inflation factors and activities of state regulators may impose substantial burdens, but it is the proposed state legislation to nullify terms, conditions, and exclusions of policies that represents the major threat to the industry. ■

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