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COVID-19 has prompted businesses to contemplate the type of protection their insurance policies may offer them in this time of uncertainty. Perhaps your business has had to close, and you can no longer pay rent. Perhaps you failed to take steps to protect employees or customers from the virus, and now they are threatening legal action against you. On the other side of the equation, insurers may see an influx of claims dealing with losses associated with COVID-19, and they will need to be determined what losses, if any, the insurer is obligated to cover.

Whether an insurer will cover losses will ultimately come down to whether losses suffered during the pandemic are losses caused by a “covered peril” that are not otherwise excluded under the policy. Some policies are “all risk” policies, which offer a broad range of coverage, whereas other insurance policies may only cover those perils named in the policy. Commercial insurance policies typically contain two streams of coverage – property insurance and liability insurance. This article will discuss coverage within both the property context as well as the liability context.

Property Loss

Property insurance for businesses is meant to protect the physical assets of a business against loss and/or damage, such as the building you operate out of, stock, merchandise, computers, equipment, etc. Whether an insurer will be obligated to cover those losses will come down to whether there was a direct physical loss to insured property, whether that damage was caused by a covered peril, and whether the loss is otherwise excluded by the policy.

Arguments about whether losses are a “direct physical loss” are frequently argued in court. We anticipate such arguments will also likely occur in the context of policy claims for losses to an insured’s business due to the impact of COVID-19. There are thus two issues facing insureds in that context: (a) many businesses will not have suffered actual physical damage to their property; and (b) even if they did, the physical damage may be an indirect consequence of the peril. Some losses may not be physical or direct, such as lost revenues.

Take a loss of stock, for example: a greenhouse is forced to close due to a government order to protect the public from COVID-19. As a result of the closing, the plants meant to be sold perish. The loss would translate into a loss of property for the business owner, but is it a “direct and physical loss of property”? Probably not. The plants perished because they were not being tended to – not because the virus destroyed them. It could, therefore, be argued that the loss was “indirect.”

Let’s say a business’s stock is “contaminated” by the virus and cannot be sold. In this instance, the loss may be direct from the virus, but is it truly a “physical loss”? In assessing that question, one of the primary



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considerations will be whether the stock was altered sufficiently to fall under the definition of “physical loss.” Since the virus does not impact the appearance of the contaminated items, it might be assumed they would not. By way of analogy, though, there are circumstances where insurers have paid to clean or replace goods damaged by smoke in a fire even though they do not look physically damaged. Could it be argued that an item contaminated by the virus is a similar situation, thus warranting coverage? Recent court cases suggest it may be possible, but it is yet to be seen within the specific context of COVID-19.

While the comparative example may hold true, there could be several other hurdles to establishing coverage under a policy. In both the case of the greenhouse and contaminated stock, the insured would still need to establish that damage caused by the virus is a covered peril if they do not have an “all risks” policy. Even if considered as such, other provisions of the policy may exclude coverage. The answers, therefore, ultimately depend on the individual terms of the insurance policy.

If an insured is able to establish the loss or damage is a direct physical loss or damage caused by a covered peril not otherwise excluded, the general property provisions of the insurance policy would cover the cost to repair or replace the property. Often times, though, there can be other “indirect” losses experienced as a result of the loss or damage to the property itself. Lost revenues are one clear example of such “indirect loss,” and insureds would have to look to business interruption coverage to be indemnified for these types of losses.

Business Interruption

Business interruption insurance is a form of property insurance that, by its nature, is meant to cover indirect losses. It is meant to indemnify insureds for lost revenues resulting from property damage or loss yet still typically requires physical damage to that property before a loss will be considered to fall within coverage. Not all policies contain coverage for business interruption.

Insureds and insurers alike will need to think about whether physical damage to property has, in fact, occurred. An obvious example is where your business has been interrupted due to an accidental fire at your building. Let’s say you operate a gym, and the fire caused physical damage to most of the gym equipment in the building. You can’t operate your gym until your equipment has been repaired or replaced. Your property insurance would respond to repair or replace your equipment, and business interruption insurance would respond to cover lost revenues during this time. Depending on the scope of the business interruption insurance, it may also cover extra costs associated with getting the business back up and running or setting up an alternative business site in the meantime.

Most common commercial insurance policies are meant to cover traditional, known risks such as the fire example. The situation is quite different where a business cannot operate due to a government order related to COVID-19 or contamination from the virus itself. While the insured property may not be physically damaged at all, your business has nonetheless still been interrupted. Another example may be where property is discarded because it might be contaminated; perhaps a truck driver has just delivered goods to a business but has also just tested positive for COVID-19. Those delivered goods may be contaminated and cannot be used in the business, which may then translate to lost revenues or extra costs.

In the circumstances of either example, there will likely be arguments about the meaning of “physical damage” generally and whether contamination of property can be considered to fall within that meaning such that coverage exists. There may also be issues about whether the property was actually contaminated or assumed contaminated and discarded for safety purposes.

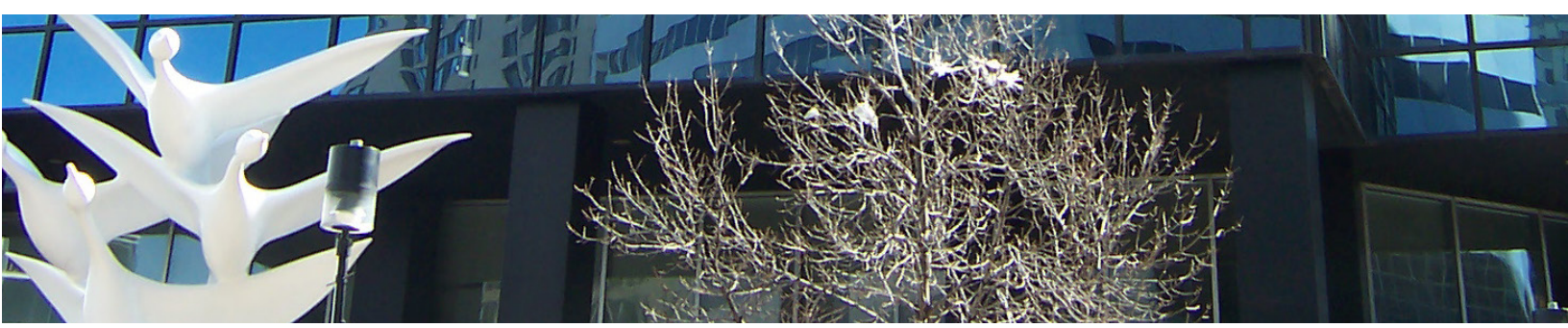
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Liability Insurance

It is possible some businesses could inadvertently expose themselves to third party liability that might not otherwise arise but for the COVID-19 pandemic. An interesting example of how certain businesses dealt with such potential liability are those that banned the use of personal re-usable cups following the World Health Organizations' classification of COVID-19 as a pandemic. Presumably, this step was taken to attempt to limit or avoid employees potentially falling ill or even critically ill as a result of exposure to the virus on cup rims that had been in customer's mouths. In the ordinary course, the use of re-useable cups may be completely acceptable from a liability perspective. In light of COVID-19, though, what if an employee or customer was exposed to the virus and became ill as a result of a business not changing its "ordinary course" practices? Could that business be held liable, and would its insurer be required to indemnify under a policy of liability insurance? Allegations of negligence causing loss or damage typically fall within coverage under those types of policies, but any applicable exclusions would still need to be considered.

Exclusions

Insurance considerations in light of COVID-19 are not completely uncharted territory. The industry responded to several millions of dollars in losses following the SARS epidemic in 2002 and 2003. As a result, many insurers adjusted their business interruption policies to contemplate and exclude the risks associated with epidemics or communicable diseases.[1]

General commercial insurance policies also contain "pollution exclusions" that broadly exclude losses arising out of the discharge or escape of pollutants. Pollutants are commonly defined as "any solid, liquid, gaseous or thermal irritant or contaminant, including smoke, vapour, soot, fumes, acids, alkalis, chemicals and waste." The term "contamination" is often used when discussing COVID-19; therefore, the more general question of whether a virus can be a "pollutant" may become a point of issue.

Manuscript Policies and Endorsements

Traditional commercial insurance policies contain general wording and exclusions meant to apply to a wide variety of business endeavours. Depending on the nature of a business, a traditional commercial insurance policy may not suitably protect against the unique risks of that business. Some insurers may offer manuscript policies customized to a certain area of business and losses not typically covered in traditional policies. Many insurers also offer endorsements or "add ons" to commercial insurance. For example, some insurers may offer endorsements for:

- **Loss of Attraction** – This product is meant to protect businesses that lose customer traffic due to an external event. The best example is a hurricane hits the city and damages the street in front of the business, making it difficult or impossible for customers to visit. This branch of coverage does not require physical damage to the insured property, but physical damage to external property is still a requirement.
- **Prevention of Access** – This product is meant to protect a business that has been prevented access to its building. Some endorsements are specific enough to offer cover where the prevention of access is due to a government order. These coverages need to be analyzed carefully as physical damage of some sort may still be required.

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- **Infectious diseases** – This product would be part of a manuscript policy for businesses that risk losses due to infectious diseases. There are special policies for laboratories or hospitals that come in contact with infectious diseases on a more regular basis.
- **Event cancellation insurance** – This product is meant to protect insureds when their event (concert, conference, sporting event) needs to be cancelled or postponed. The insurance should be read carefully, as it often contains an exclusion for losses caused by communicable diseases.
- **Contingent Business Interruption** – This product is meant to protect a business's supply chain in the event its supplier has suffered a loss and cannot deliver. This branch of coverage still requires physical damage to the supplier's property.

This is only a broad overview of additional coverages available. These coverages may still come with strict restrictions and should be evaluated carefully.

Recent Developments: Courts Broadening the Definition of “Physical Damage” and Class Actions Against Insurers

A recent decision out of the Ontario Superior Court of Justice from March 30, 2020, suggests that, at least in Ontario, courts may interpret the definition of “physical damage” broadly, especially for “all risk” policies already meant to cast a broad net of coverage. Although the Superior Court's decision could still be appealed, it may nevertheless provide some interim guidance on the types of “COVID-19 losses” that could potentially be found to fall within coverage.

In the case, a nuclear reactor plant was shut down due to a water leak in the facility. The leak did not damage the reactor, but the business lost the use of it for a period of time, which caused supply chain issues for their customers that were trying to purchase radioactive isotopes. One of those customers made an insurance claim under their contingent business interruption insurance, which was denied by the insurer. The Court concluded the costs incurred due to “loss of use” following the shut down should be covered even though there was no physical damage to the reactor itself. While not dealing specifically with COVID-19 or any other type of virus, the decision broadens the definition of “physical damage” to include the “loss of use” of property. In rendering its decision, the Court referenced a prior court case that accepted fumes from an oil spill constituted “physical damage” (similar to the smoke damage analogy).

At first glance, the reasoning seems to support a parallel argument of coverage for COVID-19 losses. Like most cases, though, the Ontario decision was given within the specific context of contingent business interruption coverage in an “all risks” policy that did not specifically deal with communicable diseases or potential exclusions. As such, whether any one “COVID-19 loss” will fall within coverage will still very much depend on the individual terms of each insurance policy and the context of the loss.

Although no class action has yet been certified, such lawsuits are being commenced in Saskatchewan for business interruption coverage for COVID-19 losses. If the Court approves the actions, any subsequent reported decisions will hopefully clarify and further elucidate the circumstances in which coverage might be found to exist for such losses.

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Conclusion

The short answer is that, since the SARS epidemic, most business interruption insurance policies are now built to exclude losses due to communicable diseases. If damaged or lost property is a “direct physical loss” caused by a “covered peril” not otherwise excluded, basic

property coverage under a commercial insurance policy should provide coverage limited to the cost of that property.

If you are a business that put your mind to the possible risks of a future epidemic and you purchased special insurance to cover you, such as a manuscript policy or endorsement, then you may be in a better position. Even then, though, many of those endorsements still exclude communicable diseases. Each insurance claim will need to be assessed on an individual basis based on the terms of the policy, which will necessarily include an assessment of the coverages, exclusions, and any endorsements added to the policy.

Whether coverage will be granted will be based on a combination of many factors, some of which could be:

- Is the policy an “all-risk” policy?;
- Can “contamination” be considered a “physical loss” to property?;
- Is the direct cause of the loss COVID-19 or otherwise?;
- Does the policy contain an exclusion for epidemics and, if so, does that exclusion apply?;
- Would any other exclusions, such as a pollution exclusion, apply?; and
- Have any endorsements or specialized insurance products designed for losses during an epidemic been purchased?

[1] “Insurers Are Immunized Against Virus Costs”, Yang, Jing, Dow Jones News Service, February 22, 2020 at www.advisen.com/tools/fpnproc/fpns/articles_new_12/P/360544271.html?rid=360544271&list_id=12

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About McKercher LLP:

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