LOS ANGELES & SAN FRANCISCO
Daily Journal
www.dailyjournal.com
THURSDAY, MAY 11, 2023

GUEST COLUMN

California Supreme Court Review: April 2023

By Andrew S. Ong, Ariel Rogers and Yoona Lee

Shutterstock

This month's column reviews cases related to insurance coverage for losses due to COVID-19. In the past six months, the 9th U.S. Circuit Court of Appeals sent two COVID-19-related cases to the California Supreme Court, asking the Court to answer questions of state law. These upcoming decisions will not only address a split in California authority, they will also impact how lower courts interpret contracts and how insurance providers draft policies for viral contaminations.

The first case before the California Supreme Court is *Another Planet Ent., LLC v. Vigilant Ins. Co.*, 56 F.4th 730 (9th Cir. 2022). The parties in this case disagree whether actual or potential presence of the COVID-19 virus on the insured's premises constitutes "direct physical loss or damage to property" under the insurance policy's provisions for business income, civil authority, and loss prevention expenses. *Id.* at 732. In seeking insurance coverage after being forced to close its venues due to the government's COVID-19 closure orders, Another Planet argued that aerosolized droplets of the COVID-19 virus can "physically alter the air and airspace… and the surfaces of both the real and personal property to which they attach, constituting physical loss or damage." *Id.* The lower court granted Vigilant's motion to dismiss for failure to state a claim, concluding that Another Planet had not sufficiently alleged direct physical loss or damage to property. *Id.* Another Planet appealed.

In considering whether the presence of COVID-19 constitutes "direct physical loss or damage to property" under California law, the 9th Circuit noted a split in California appellate courts. In *United Talent Agency v. Vigilant Ins. Co.*, 77 Cal. App.5th 821 (2022), Division 4 of the 2nd District Court of Appeal reasoned that the "short lived" character of the COVID-19 contamination "that can be addressed by simple cleaning" did not constitute direct physical loss or damage. *Id.* at 835. But in *Marina Pacific Hotel & Suites, LLC v. Fireman's Fund Insurance Co.*, 81 Cal.App.5th 96 (2022), Division 7 of the 2nd District directly questioned the holding in *United Talent Agency*, finding that the insured's argument that the COVID-19 virus "actually bonds and/or adheres to…objects through physico-chemical reactions involving…cells and surface proteins" was a sufficient pleading of direct physical loss or damage to covered property at the demurrer stage. *Id.*at 101. In light of this split in authority, the 9th Circuit requested that the California Supreme Court weigh in to determine which appellate court opinion is most compelling.

Both insurance companies and insurance holders with policies requiring direct physical loss or property damage to trigger coverage will want to watch closely for the Court's decision in Another Planet. If the Court holds that the presence of COVID-19 virus can constitute "direct physical loss or damage to property," then insurers may potentially have to pay out for COVID-19-related claims under relevant provisions, including those for business income, civil authority, and loss prevention expenses. In that scenario, insurance companies may also want to reconsider existing policies to anticipate future viral outbreaks, and redefine what

"direct physical loss or damage to property" may encompass. But in doing so, insurers should take care to not limit the policy so as to render coverage illusory, as high lighted by *French Laundry Partners, LP v. Hartford Fire Ins. Co.*, 58 F.4th 1305 (9th Cir. 2023), the second case certified by the Ninth Circuit for the California Supreme Court.

When French Laundry was forced to close its restaurants in Napa due to COVID-19, it sought coverage under a "Limited Virus Coverage" policy for its economic losses, including loss of business. Denying that French Laundry's losses were covered, Hartford, in a motion to dismiss, pointed to its "Virus Exclusion" provision that states Hartford "will not pay for loss or damage caused directly or indirectly by… [p]resence, growth, proliferation, spread or any activity of…virus." *Id.* at 1306. The district court agreed with Hartford, concluding that the virus exclusion was enforceable. French Laundry appealed, contending that by construing these provisions to preclude COVID-19-related damages, the court rendered the policy's virus coverage illusory. The 9th Circuit subsequently requested that the California Supreme Court resolve this question of state law, as other cases involving virus exclusion clauses in the context of COVID-19 had reached California appellate courts since the district court's dismissal.

With so many businesses having suffered deep losses due to COVID-19, French Laundry offers a potential avenue for insurance holders to get coverage, as indicated by the 9th Circuit's reference to *John's Grill, Inc. v. Hartford Fin. Servs. Grp., Inc.*, 86 Cal.App.5th 1195 (2022). In *John's Grill*, the California Court of Appeal considered similar provisions of Limited Virus Coverage, Virus Exclusion, and Specified Causes Clause as those at issue in French Laundry. *Id.* at 1202-03. The appellate court concluded that, even with a Virus Exclusion provision, the virus endorsement in Hartford's insurance policy should be read broadly to ensure that coverage was not "virtually illusory." *Id.* at 1220.

Should the Court agree with *John's Grill*, French Laundry may recover for COVID-19-related losses under its Limited Virus Coverage despite the Virus Exclusion clauses, signifying a noteworthy win for insurance holders making similar claims of illusory coverage. Given the prevalence and uncertainty surrounding COVID-19 insurance litigation, *Another Planet* and *French Laundry* are cases to follow closely, as the Court's answers to these questions will have important public policy ramifications impacting both state and federal courts, and insurance holders and insurance companies. Meanwhile, insurance companies with similar exclusionary clauses may want to re-evaluate policies to ensure that courts cannot find coverage is illusory, while still carving out the necessary limitations and exclusions.

Andrew S. Ong *is a partner in Goodwin Procter LLP's Intellectual Property practice and a leader of the firm's Trade Secrets, Employee Mobility + Non-Competes group, and* **Ariel Rogers** *and* **Yoona Lee** *are associates at Goodwin Procter LLP.*

Reprinted with permission from the *Daily Journal*. ©2023 Daily Journal Corporation. All rights reserved. Reprinted by ReprintPros 949-702-5390.