COVID-19 COMMERCIAL INSURANCE
CONSIDERATIONS AND STRATEGIES FOR PROPERTY OWNERS
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The real estate industry is facing significant disruption due to the COVID-19 outbreak. In response to mandatory “shelter-in-place,” “safer-at-home,” and other government orders, many commercial tenants — including bars, restaurants, sports venues, movie theaters, hotels, and manufacturers — have been forced to completely or partially shut down their business operations. Many of these tenants are therefore unable to meet their rent obligations, resulting in a significant and ongoing loss of income to property owners.

In response, many property owners are turning to business interruption insurance to cover their losses. On the surface, business interruption insurance appears to be a good candidate to cover losses stemming from COVID-19. Unfortunately, there are several obstacles that will prevent many property owners from obtaining coverage for COVID-19-related losses from business interruption insurance.

While all policyholders should carefully consider their business interruption policy terms for COVID-19-related losses and continue to submit potential claims to their insurers, they should also carefully consider other important policy terms and strategies to mitigate their losses and protect their assets during these unprecedented times.

Business Interruption Insurance and Potential COVID-19 Coverage Limitations

Business interruption insurance compensates a business for its lost profit and certain continuing operating expenses when operations are affected by damage to property that impairs or prevents normal operations. These policies may also provide contingent business interruption insurance that reimburses lost income and certain continuing operating expenses resulting from an interruption of business at the premises of a customer or supplier of the insured.

Many business interruption policies, however, contain specific limitations and exclusions to the scope of coverage that are applicable to the COVID-19 crisis.

- **Virus and Other Applicable Exclusions.** Some policies contain a specific exclusion for losses related to a virus or other communicable diseases like COVID-19. As one example, ISO form CP 01 40 07 06 is titled “Exclusion for Loss Due To Virus Or Bacteria” and excludes “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 exclusion goes on to specifically state that it applies to, among other things, “business income,” i.e., business interruption.
- **Direct Physical Loss or Damage.** Business interruption policies only provide insurance for “direct physical loss of or damage to” the covered property. In the context of COVID-19, the vast majority of businesses will not sustain a “direct physical loss” to their property. Therefore, where a business’s property is still inhabitable and undamaged, COVID-19-related losses are unlikely to be covered.

- **Civil Authority Coverage.** The “direct physical loss” requirement also applies to “civil authority” coverage. This coverage applies where a “covered cause of loss” causes damage to property other than the insured’s property, resulting in lost business income because a civil authority prohibits access to the insured’s property. In response to COVID-19-related government-ordered shutdowns, property owners may have a basis to argue that “civil authority” coverage has been triggered. In most cases, a direct physical loss to an adjacent or nearby property is required in order for civil authority coverage to kick in. Consequently, most civil authority clauses will not apply to losses stemming from most COVID-19-related government-ordered shutdowns.

**Business Interruption Insurance and Potential Coverage Opportunities**

Despite these obstacles, there are occasions where losses from COVID-19 could arguably be covered by business interruption insurance (assuming the policy does not contain a virus or other applicable exclusion).

- **COVID-19 Causes Physical Loss or Damage.** In circumstances where COVID-19 is shown to be within the confines of a covered property, there could be precedent to argue that the property is contaminated and has therefore sustained a “direct physical loss,” thereby triggering coverage. Courts across the country are currently split, however, as to whether the presence of a harmful substance constitutes damage to or destruction of property.
  - Litigation has already commenced in several states relating to whether COVID-19 contamination constitutes “physical damage” under a business interruption policy. Therefore, the answer to this question is likely to vary state-by-state and will be hotly contested by insurers nationwide as they seek to reign in their exposure from the worldwide pandemic.

- **Potential Government Intervention.** As the economic fallout of the global COVID-19 pandemic continues, state and federal legislatures and regulators are coming under increasing pressure to shift the resulting economic losses onto the insurance industry. One of the major issues that legislatures and regulators are focusing on in this respect is whether business losses related to the virus might implicate business interruption coverage. To that end, several state legislatures – including New Jersey, Massachusetts, and Ohio – have introduced legislation that would retroactively expand coverage under existing business interruption insurance policies to cover losses due to the COVID-19 outbreak.
In light of these fact-specific coverage issues, and the growing possibility of government intervention related to COVID-19-related business income losses, all policyholders should carefully consider their business interruption policy terms for COVID-19-related losses on a case-by-case basis. Furthermore, policyholders should continue to document their lost profits and ongoing operating expenses and submit business interruption claims to their insurers.

A list of best practices for COVID-19-related business interruption claims can be found here or at the following URL: https://www.m3ins.com/sites/default/files/COVID-19%20Business%20Interruption%20Best%20Practices.pdf

**Reviewing Vacancy Clauses**

In the wake of “shelter-in-place” and other government orders that have forced many tenants to temporarily or permanently vacate their leased property, owners should pay close attention to the vacancy provisions in their commercial property insurance policies.

Most property policies contain a vacancy provision that severely restricts coverage in connection with buildings that have been vacant for a specified number of days (typically, 60 days). Some forms also restrict coverage in connection with buildings that have been unoccupied for a specified number of days.

As one example, some policies provide that the covered property will be considered vacant “unless at least 31% of its total square footage is: (i) rented to a lessee or sublessee to conduct its customary operations; and/or (ii) used by the building owner to conduct customary operations.” In the event that a property is considered vacant under this definition for more than 60 consecutive days before a loss occurs, these policies will not cover any loss or damage for certain perils like vandalism, water damage, or theft, and will reduce the amount that the policy will cover for loss or damage caused by other covered causes of loss by 15%.

While most vacancy clauses will not be an immediate concern for COVID-19-related closures for several more weeks, owners should begin working with their insurance advisors now to determine how, if at all, their policies will respond in the event of a loss if their properties were partially or completely vacant or unoccupied. Furthermore, if owners suspect that the vacancy clause in their policy could be triggered in the event of a loss, they should begin a dialogue with their insurer to determine whether it will agree to temporarily suspend the vacancy provision in their policy given the unprecedented disruption that the COVID-19 pandemic and resulting economic turmoil has caused.

Alternatively, if the insurer is unwilling to voluntarily waive the vacancy provision, owners should request a “vacancy permit endorsement” that suspends the exclusions outlined above, which ordinarily requires additional premium. Either way, owners should take steps to ensure that their assets are protected as tenants permanently or temporarily vacate their properties.
Financial Considerations and Strategies

Owners experiencing cash flow constraints or other financial concerns should consult with their insurance advisor to discuss their options to ease the burden of insurance premium payments. Many carriers are voluntarily suspending cancellation for non-payment of premiums until the “shelter-in-place” and “safer-at-home” mandates are lifted. Others are allowing special payment plans for financially-strained policyholders that, among other things, allow insurance payments to be delayed for an agreed number of billing cycles without penalty.

Another option to consider for owners with other cash flow priorities is premium financing. Premium finance is a process by which a lender pays the insurance premium to a carrier on behalf of an insured. The insured repays the Lender for the amount of the loan (principal) plus interest over an agreed upon time period (typically between 9-12 months). This option allows insureds to have their policies paid in full so that they may use their remaining cash-on-hand to reinvest back into their businesses to sustain and grow it. Notably, the loan will not appear on any credit checks (D&B, Trans-Union, Equifax, etc.) as an unpaid balance/outstanding loan. As a result, the loan balance will not negatively affect any lending decisions by other financial institutions.

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These are only some of the insurance issues affecting property owners stemming from the COVID-19 pandemic and resulting economic uncertainty. If you have any questions about the issues addressed in this article or otherwise, please do not hesitate to reach out to your M3 Account Executive.