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Lawyer Insights

Are Courts Ignoring Policy Interpretation Rules in COVID Decisions?

Federal trial courts may be disregarding basic rules of policy interpretation in COVID-19 cases, and policyholder attorneys are not happy about it.

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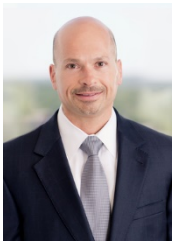


The Northern District of New York recently awarded judgment on the pleadings to insurer Affiliated Factory Mutual Insurance Co. in a COVID-19-related business interruption claim.[1] In doing so, the court followed in the footsteps of other federal courts across the country when it failed to consider all parts of the policy as required by state law and made fact determinations at the Rule 12(c) pleading stage.

Mohawk Gaming Enterprises, a casino and resort operated by the Saint Regis Mohawk Tribe located on the border of New York and Canada, was forced to close its operations due to government orders. It filed a claim with AFM requesting coverage for business interruption under the civil authority section of the policy. AFM ignored the basis of Mohawk Gaming's claim and instead acknowledged the claim as one for communicable disease coverage—a coverage with a low sublimit. Eventually, the insurer denied Mohawk Gaming's claim, and Mohawk sued AFM seeking recovery of business income losses that it incurred when it was forced to close due to the COVID-19 pandemic.

AFM moved for judgment on the pleadings, arguing that the government order closing Mohawk Gaming did not trigger the civil authority provision of the policy. The district court agreed.

In granting the insurer's motion, however, the court made two errors.

The Policy and Facts Alleged, Not the Scoreboard, Controls Coverage.

First, the court failed to consider all parts of the AFM policy as required under New York law. Specifically, it failed to afford meaning to language contained in the policy's two communicable disease clauses – meaning that necessarily applies throughout the policy. Both of those clauses specifically contemplate that "communicable diseases," as defined and covered under the AFM policy, can cause loss and damage to property. Yet, the court did not analyze the meaning of those clauses within the context of this policy. Instead, the court followed other decisions from "numerous courts around the country," each of which is based on different policy wording and their own inherently flawed reasoning to conclude that the presence of virus "is insufficient to trigger coverage when the policy's language requires physical loss or physical damage."

For example, the court relied on *Sharde Harvey DDS, PPLC v. Sentinel Insurance Co., Ltd.*[2] But the policy in *Sharde* did not include any communicable disease coverages. Nor does *Uncork and Create LLC v. Cincinnati Insurance Co.*[3], which the court also relied upon, include a communicable disease coverage.

Thus, the district court looked to the "scorecard" of cases without looking at the differences in coverage under the policy at issue here. That was an error.

In fact, a federal court in Texas recently rejected the very same reasoning employed in *Mohawk Gaming* after recognizing that the FM/AFM policy form "is much broader than [others] and expressly covers loss and damage caused by 'communicable disease.'"[4] In New York, as in Texas, insurance coverage is not determined based on a "scoreboard." It is based on the words and phrases actually used by the parties.

Courts that have performed a proper analysis have concluded that the policy language and the type of claims alleged matter and, in many cases, mandate coverage for COVID-19-related losses (or, at a minimum, present issues of fact that cannot be resolved by early motions practice).[5]

The *Mohawk Gaming* court failed to undertake this critical analysis and wrongly relied on the scoreboard to summarily dismiss the claims.

Courts Should Not Usurp the Jury's Role of Resolving Factual Questions Concerning a Virus's Ability to Physically Alter Property

Second, the district court made a factual determination about whether COVID-19 physically alters property without hearing from scientific experts. Mohawk Gaming was forced to close its casino to the public after an outbreak of COVID-19 was discovered at a college five miles away. The AFM policy provides business interruption coverage for losses caused by "an order of civil or military authority [that] prohibits access to a location" if that order "is the direct result of physical damage of the type insured" at or within five miles of a covered location. Mohawk Gaming contended that COVID-19 caused "physical loss or damage" of the type insured by the policy and that, because COVID-19 was located within five miles of the casino, the business interruption coverage applied.

In its order, the court ruled that the meaning of "physical loss damage" unambiguously does not cover the "mere presence or spread of the novel coronavirus." But it considered no evidence of whether the presence of COVID-19 causes a physical alteration of the property, the true test under New York law (and most other states' laws) for whether physical damage to property has occurred. Whether a certain substance can have a certain type of effect is clearly a question of fact—one that the court decided on its own without the benefit of scientific evidence, or any evidence for that matter.

Mohawk Gaming and Similarly Situated Policyholders May Rectify These Issues On Appeal

The *Mohawk Gaming* decision thus raises significant issues for appeal. As noted, the court failed to afford meaning to the policy's two express acknowledgments that "communicable disease"—a term defined by AFM—can cause "loss or damage" to property. Relatedly, because the *Mohawk Gaming* court missed the express acknowledgment that communicable disease may cause loss or damage to property, the court failed to contemplate that such loss or damage is "loss or damage of the type insured." What's more, the court was wrong to defer to "the great majority of courts that have addressed" the issue because the question is what the meaning of the policy is under New York law, not what other courts think about the language.
Besides, no "great majority" of courts addressed the issue under the uniquely broad FM/AFM policy prior to the court in *Mohawk Gaming* and, to date, only the court in *Cinemark* has squarely reconciled the policy's express communicable disease provisions with the policy's generally used phrase "loss or

damage" to property. The only other decision to squarely analyze policy wording from the FM/AFM policy form (as opposed to merely looking to the scoreboard) is *Thor Equities, LLC v. Factory Mutual Insurance Co.*[6], where a federal court in New York rejected the insurer's strained interpretations of the policy's contamination exclusion, finding that provision to be ambiguous and, thus, not applicable to losses caused by COVID-19.Finally, the court made an inappropriate fact determination at the Rule 12(c) stage of litigation.

Unfortunately, the district court was not alone; federal district courts across the country, faced with the novel and pressing issue of COVID-19-related losses, have made similar errors. Cases are proceeding through the Courts of Appeals now where the intermediate courts will have an opportunity to correct those errors.

Notes

1. *Mohawk Gaming Enterprises, LLC v. Affiliated FM Ins. Co.*, No. 8:20-CV-701, 2021 WL 1419782, at *1(N.D.N.Y. Apr. 15, 2021).

2. *Sharde Harvey, DDS, PLLC v. Sentinel Ins. Co., Ltd.*, No. 20CV3350PGGRWL, 2021 WL 1034259, at *1(S.D.N.Y. Mar. 18, 2021).

3. *Uncork & Create LLC v. Cincinnati Ins. Co.*, 498 F. Supp. 3d 878, 879 (S.D.W. Va. 2020).

4. See *Cinemark Holdings, Inc. v. Factory Mut. Ins. Co.*, No. 4:21-cv-00011 (E.D. Tex. May 5, 2021).

5. Id.; see also *MacMiles LLC v. Erie Ins. Exchange*, No. GD-20-7753, slip op., (Pa. Ct. C.P. May 25, 2021)(granting summary judgment to policyholder and finding that "Plaintiff's loss of use of its property was both'direct' and 'physical'"); *Choctaw Nation of Okla. v. Lexington Ins. Co.*, No. CV-20-42, slip op., (Okla. Dist. Ct.Feb. 15, 2021) (granting summary judgment to policyholder because "direct physical loss occurs whencovered property is rendered unusable for its intended purpose" (quotation omitted)).

6. No. 20 Civ. 3380 (AT), 2021 WL 1226983 (S.D.N.Y. Mar. 31, 2021).

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