To be Argued by:
ORRIE LEVY
(Time Requested: 15 Minutes)

New York Supreme Court

Appellate Division—First Department

CONSOLIDATED RESTAURANT OPERATIONS, INC.,

Plaintiff-Appellant,

Appellate Case Nos.: 2021-02971 2021-04034

– against –

WESTPORT INSURANCE CORPORATION,

Defendant-Respondent.

REPLY BRIEF FOR PLAINTIFF-APPELLANT

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Appellant Consolidated Restaurant Operations, Inc. ("CRO") respectfully submits this reply brief in further support of its appeal from the New York State Supreme Court, New York County's Decision and Order dated August 4, 2021, granting the Motion to Dismiss of Defendant Westport Insurance Corporation ("Westport"), and the Decision and Order dated September 23, 2021, denying its Motion for Reargument and, in the Alternative, to Amend Its Complaint.

PRELIMINARY STATEMENT

Westport's arguments that CRO has not sufficiently alleged "physical loss or damage" is premised on a strawman – that CRO is seeking insurance coverage for a mere "loss of use," untethered to any physical impact to its insured properties. Based on this false premise, CRO asserts that *Roundabout Theatre Co. v. Continental Casualty Co*., 302 A.D.2d 1 (1st Dep't 2002), is "plainly applicable." Westport, however, does not dispute that *Roundabout* had nothing to do with whether a dangerous, physical substance on insured property can cause physical loss or damage. It cannot dispute that for decades, courts across the country, including in New York, have found that invisible or intangible substances can cause physical loss or damage, even if they do not structurally alter property, if they seriously impair the functionality of the property. It cannot dispute that based on the Policy[1] as a whole,

[1] Capitalized words not defined shall have the same meaning as in CRO's Opening Brief ("Opening Br.").

a reasonable insured could interpret the term "physical loss or damage" to encompass the physical impacts to CRO's property by the coronavirus. And Westport cannot dispute that CRO has alleged, in detail, that the physical presence and imminent threat of the coronavirus on and in its properties caused it to close dozens of Restaurants and eliminated the functionality of the dining areas within the Restaurants for their intended purpose. Thus, Westport does not dispute the key facts and law that warrant reversal here. Indeed, as CRO noted in its opening brief, a ruling in Westport's favor would require the Court to reject CRO's well-pled allegations and improperly resolve hotly contested factual issues in favor of Westport, in direct contravention of the motion to dismiss standard.

Westport's reliance on a laundry list of inapplicable exclusions to make up for its failure to include a widely available virus exclusion in the Policy is equally misplaced. Westport relies on a contamination exclusion that only applies to traditional environmental pollutants, not a naturally occurring virus. It relies on a "microorganism" exclusion, even though scientists and lay people alike understand that a virus is not a microorganism. It relies on a "loss of market" exclusion, which narrowly excludes coverage where marketplace trends make the insured's products less popular, not where a physical loss or damage to insured property interrupts CRO's business, as CRO has alleged here. And it relies on a "reasons not covered" exclusion, which does not apply when a policyholder has suffered losses as a result

of physical loss or damage to property. At the very least, for each of these exclusions, CRO has posited a reasonable interpretation of the exclusion that results in coverage and, thus, controls as a matter of law.

Finally, Westport asserts that CRO's motion to amend should be denied because the amended complaint was palpably insufficient. To the contrary, that complaint included detailed allegations regarding the physical characteristics, nature, and modes of transmission of the virus, and its presence and impact on CRO's Restaurants and business operations. Thus, the crux of Westport's position is that COVID-19 cannot cause physical loss or damage as a categorical matter, irrespective of the fact that it is a physical particle with physical characteristics that impacts property. That position flies in the face of the plain terms of the Policy and decades of case law from New York and courts across the country.

ARGUMENT

I. CRO SUFFICIENTLY ALLEGED PHYSICAL LOSS OR DAMAGE TO PROPERTY UNDER NEW YORK LAW BASED ON THE PHYSICAL PRESENCE OF THE CORONAVIRUS ON AND IN THE RESTAURANTS

A. Westport Misstates New York Law Regarding Physical Loss or Damage

Westport does not meaningfully rebut the many cases CRO cited from across the country, including *Pepsico* from the Second Department, holding that the physical presence of a noxious substance on insured property can cause physical loss

or damage if it nearly eliminates the functionality of insured property; let alone the numerous cases that have reached this conclusion based on the physical presence and impact of the coronavirus on insured property. *See* Opening Br. at 27-36. And Westport does not meaningfully contest that a reasonable insured, reading the Policy as a whole, would consider CRO's allegations to fall squarely within the undefined term "physical loss or damage." Rather, the crux of Westport's argument is that, under New York law, the presence of a deadly, physical substance rendering property unusable for its intended function cannot "constitute direct physical loss or damage" as a matter of law. Resp't's Br. ("Op. Br.") at 5-7. This position should be rejected.

Westport cannot cite a single New York appellate case involving similar facts that supports this categorical position. Instead, it selectively cites to an insurance treatise, but glaringly omits the "supplement" to that treatise which discusses "direct physical loss or damage to insured property" from invisible agents:

> contamination by persistent chemical or biological agent, not otherwise excluded from coverage, may cause "direct physical loss" if it renders insured property unusable, even though contamination may be gaseous, microscopic, or invisible; covered losses are not confined to obvious physical changes to building caused by fire or bad weather.

See Steven Plitt et al., *Generally; "Physical" loss or damage*, *10A Couch on Insurance* § 148:46 (3d ed. 2021).[2]

Westport then asserts that *Roundabout* is "plainly applicable here" because it interpreted the term "physical loss or damage" to require "actual" damage. Op. Br. at 8-10. Yet, Westport does not dispute that, in *Roundabout*, the policyholder did not allege any physical impairment or detriment (much less a lethal virus) rendering its property unusable for its intended function. On the contrary, Westport concedes that the holding of *Roundabout* was that "losses resulting from off-site property damage do not constitute covered perils under the Policy" – a proposition that is both uncontested and irrelevant here. *Id.* at 10. Thus, the court in *Roundabout* was never asked to resolve the type of claim at issue in this case.

Similarly, Westport's assertion that CRO's position is that "50 New York State and Federal jurists have gotten *Roundabout* wrong" is false and misstates CRO's argument. *Id.* Specifically, *Roundabout* is the applicable authority when an insured has alleged a mere "loss of use" untethered to a physical impact to insured property. Therefore, *Roundabout* may apply where a policyholder failed to allege the physical presence or imminent risk of the coronavirus on insured property. But

[2] Notably, even the portion of this treatise Westport cites in support of this proposition has been seriously called into question by recent scholarship. *See* Richard P. Lewis et al., *Couch's "Physical Alteration" Fallacy: Its Origins and Consequences*, 56 Tort, Trial & Ins. L.J. 621 (2021).

that is not the case here.[3] CRO's argument is thus limited to the far smaller number of New York trial courts that have erroneously extended *Roundabout* to a situation in which a policyholder's losses resulted from the actual presence of a dangerous, physical substance on its property – a situation *Roundabout* does not encompass.

Roundabout's inapplicability here is even reflected in the very cases applying it. For example, in *Kim-Chee LLC v. Philadelphia Indemnity Insurance Co.*, a federal court distinguished *Roundabout* as inapplicable in the COVID-19 context for the exact reasons CRO has argued here:

> In *Roundabout*, there was no dispute that physical loss or damage had caused the business interruption. The claim failed because the incident damaged the neighboring property, not the insured property. This case concerns allegations that the virus contaminated the insured property itself (as well as everywhere else.) The court turns to cases around the country which consider whether contamination is itself a direct physical loss.
>
> Contamination of a structure that seriously impairs or destroys its function may qualify as direct physical loss.

535 F. Supp. 3d 152, 160 (W.D.N.Y. 2021).[4] Thus, certain New York courts have misapplied *Roundabout* to devastating effect in the COVID-19 context in

[3] CRO listed many examples of these cases in footnote 13 to its opening brief. Nevertheless, Westport relies on these very cases in support of its position that New York state and federal courts have uniformly agreed with its position.

[4] *Kim-Chee* ultimately found in favor of the insurer not because a viral substance cannot cause physical loss or damage but, rather, because the Court found, based on the pleadings in that particular case, that COVID-19 is more akin to dust that can be easily cleaned. That finding, however, cannot be made here, where CRO has alleged in detail that COVID-19 is not susceptible to routine cleaning, pervaded the air in addition to attaching to property, and would be continuously reintroduced into the property had CRO opened its doors.

contravention of the plain terms of the policies and persuasive authority from both New York and elsewhere. This Court should correct that doctrinal error.

Westport's erroneous "50 New York Courts" argument, however, does not end there – Westport also asserts that these 50 cases have "unanimously held COVID-19 losses are not due to direct physical loss or damage to insured property." Op. Br. at 19. Yet, as stated, Westport ignores the many New York cases where the policyholder did not even allege the presence of the coronavirus on insured property. Indeed, the very first case Westport cites, *VMSB, LLC v. Zurich American Insurance Co*, No. 650590/2021, 2021 WL 5359032 (Sup. Ct., N.Y. Cty. Nov. 10, 2021), is bereft of a single citation – let alone an appellate citation – supporting its conclusion. The second case Westport cites relies on a single authority, *Roundabout*, without any explanation. *See Raymours Furniture Co. v. Lexington Ins. Co.*, No. 655167/2020, 2021 WL 4789148, at *1 (Sup. Ct., N.Y. Cty. Oct. 14, 2021).

The other trial court cases Westport highlights suffer from these same flaws. *See Sportime Clubs LLC v. Am. Home Assur. Co.*, No. 614493/2020, 2021 WL 4027887, at *4 (Sup. Ct., Suffolk Cty. June 30, 2021) (citing *Roundabout* for the proposition that "New York law requires some form of actual, physical damage to the insured premises if the claimant seeks to recover loss of business income and extra expenses"); *Jeffrey M. Dressel, D.D.S., P.C. v. Hartford Ins. Co. of the Midwest, Inc.*, No. 20-CV-2777(KAM)(VMS), 2021 WL 1091711, at *5 (E.D.N.Y.

Mar. 22, 2021) (failing to cite a single New York state authority in support of its holding under New York law); *Northwell Health, Inc. v. Lexington Ins. Co*., No. 21-cv-1104, 2021 WL 3139991 (S.D.N.Y. July 26, 2021) (relying on *Roundabout*); *Social Life Magazine, Inc.* v. *Sentinel Ins. Co.*, No. 20 Civ. 3311(VEC), 2020 WL 2904834 (S.D.N.Y. May 14, 2020) (explaining insurer's argument was that "*Roundabout* controls").

Westport's reliance on *Cytopath Biopsy Laboratory, Inc. v. U.S. Fidelity & Guaranty Co.*, 6 A.D.3d 300 (1st Dep't 2004), fares no better. Westport does not dispute that in *Cytopath*, the governmental order shutting down a laboratory was not based on the dangerous presence of noxious fumes on the property, which was quickly remedied. Rather, the laboratory was shut down until it could obtain legal permits necessary to install a proper ventilation system. That bears no resemblance to the situation here, where the Restaurants were closed for months because of the presence of the virus, the ongoing and imminent threat of the presence of the virus, and by Orders that were expressly issued, in part, because of the propensity of the virus to create physical hazards on property and damage property. Indeed, unlike in *Cytopath*, CRO would have been unable to use the Restaurants for in-person dining irrespective of the Orders because of the presence of the virus. *See Throgs Neck Bagels, Inc. v. GA Ins. Co. of N.Y.*, 241 A.D.2d 66 (1st Dep't 1998) (policy excluding loss by order of civil authority nevertheless provided coverage where government

ordered restaurant to be closed due to smoke damage; the physical loss by smoke damage, not the government order that highlighted its severity, was the cause of the loss). Further, the policy in *Cytopath* "specifically disclaimed coverage for losses occasioned . . . by 'Acts or decisions[,] including the failure to act or decide, of any person, group, organization or governmental body.'" 6 A.D.3d at 301. The Policy here contains no such exclusion.

Moreover, Westport's reliance on three federal, pre-pandemic cases for the proposition that physical loss or damage under New York law must be "demonstrable" (Op. Br. at 16) simply reflects the lack of any appellate authority in New York supporting Westport's position. In any case, these cases support CRO's position. In *United Airlines, Inc. v. Insurance Co. of the State of Pennsylvania*, the policy only covered "damage," rather than "physical loss or damage" and, thus, was far narrower than the policy here, and reflects that "physical loss or damage" must mean something different and broader than physical "damage." 385 F. Supp. 2d 343, 348 (S.D.N.Y. 2005), *aff'd sub nom. United Air Lines, Inc. v. Ins. Co. of State of PA*, 439 F.3d 128 (2d Cir. 2006). In *Satispie, LLC v. Travelers Property Casualty Co. of America*, the plaintiff sought coverage for pies it had disposed of even though the pies were not contaminated and were edible. 448 F. Supp. 3d 287, 293 (W.D.N.Y. 2020). The court found this did not constitute physical loss or damage. The court observed that "according to Plaintiff's logic, the loss was caused by its

disposal of product that was not contaminated—but if that is the case, it constitutes a loss that is not covered by the Policy." *Id.* Said otherwise, if the pies were contaminated—as the surfaces here were, that would have constituted physical loss or damage, "demonstrable" alteration or not. And in *Philadelphia Parking Authority v. Federal Insurance Co.*, 385 F. Supp. 2d 280, 288 (S.D.N.Y. 2005), the insured suffered economic losses untethered to any physical impact to its property. In that context, the court noted that there must be "some physical problem with the covered property," which is exactly what CRO has alleged here.

Westport's attempts to distinguish New York authority that supports CRO's position also fails. Westport cannot dispute that, in *Pepsico*, the Second Department expressly rejected the notion that "to prove 'physical damages' the [insured] must prove that 'there has been a distinct demonstrable alteration of [the] physical structure [of the insured's products] by an external force.'" *Pepsico, Inc. v. Winterthur Int'l Am. Ins. Co*., 806 N.Y.S.2d 709, 711 (2d Dep't 2005). And Westport does not dispute that the Second Department only required that the introduction of an invisible substance "seriously impaired" the "function and value" of the product. Instead, Westport attempts to distinguish *Pepsico* on the ground that, there, the "soda was permanently destroyed," a fact that does not appear to have played any role in the court's decision. Indeed, that argument speaks only to the duration or extent of a loss, not to the availability of coverage in the first instance.

Indeed, the Policy does not, as Westport suggests, require a "complete loss." Put simply, like the soda in *Pepsico*, an invisible substance invaded CRO's insured properties and rendered them unusable, resulting in losses. Moreover, *Pepsico* is far more analogous to the present circumstances than *Roundabout.*

Westport's efforts to distinguish *Schlamm Stone & Dolan, LLP v. Seneca Insurance Co.*, 800 N.Y.S.2d 356, 2005 WL 600021 (Sup. Ct., N.Y. Cty. 2005) also fall flat. Westport ignores that the court faulted the policyholder for not alleging that "its offices were so damaged that, even if the order had not been in place, it would not have been able to return to business," when that is exactly what CRO has alleged here. *Id.* at *3. And, contrary to Westport's argument, there is nothing in *Schlamm Stone* suggesting that the presence of the noxious substance was "permanent." Rather, a small number of more recent trial court cases have attempted to distinguish *Schlamm Stone* on that ground without basis. Indeed, *Schlamm Stone* made clear that "the presence of noxious particles, both in the air and on surfaces in plaintiff's premises, would constitute property damage under the terms of the policy." *Id.* at *5. This strongly supports CRO's position.[5]

[5] Westport's reliance on appellate authority from other states is similarly misplaced. Westport fails to rebut CRO's argument that both the Eighth and Ninth Circuit Courts have tacitly recognized that the actual presence of COVID-19 on insured property can constitute physical loss or damage. *See* Opening Br. at 33. And in Westport's remaining cases the policyholder did not allege the physical presence of the virus on insured property. *See Nail Nook, Inc. v. Hiscox Ins. Co.*, No. 110341, 2021 WL 5709971, at *3 (Ohio Ct. App., Cuyahoga Cty. Dec. 2, 2021) (policyholder's alleged losses were "all due to the coronavirus" without specific allegations of the

Finally, Westport's efforts to distinguish persuasive authority from other jurisdictions interpreting similar policy language should be rejected. Westport seeks to distinguish *Gregory Packaging, Inc. v. Travelers Property Casualty Co. of America*, No. 2:12-cv-04418, 2014 WL 6675934 (D.N.J. Nov. 25, 2014) – which found physical loss or damage based on temporary ammonia contamination in the air of the facility – on the ground that, there, the property was rendered unfit for human occupancy, whereas "[h]azmat suits were not required for entry into CRO's restaurants." Op. Br. at 35. Yet, Westport ignores that CRO's dining areas were rendered functionless by the coronavirus and that the small number of people who could enter CRO's properties likely did so wearing protective masks. The dining areas were not habitable for in-person dining, which was their insured and intended function.

Similarly, Westport attempts to distinguish *Motorists Mutual Insurance Co. v. Hardinger*, 131 F. App'x 823 (3d Cir. 2005) – a case involving E. coli in a water well – because there, the applicable standard was supposedly "complete uninhabitability," which Westport argues CRO cannot satisfy here. But the standard

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actual presence of virus on the property and policy contained standard-form virus exclusion); *Santo's Italian Cafe LLC v. Acuity Ins. Co.*, 15 F.4th 398, 402 (6th Cir. 2021) (policyholder generally alleged losses resulting from the pandemic and shut-down orders); *Gilreath Fam. & Cosm. Dentistry, Inc. v. Cincinnati Ins. Co.*, No. 21-11046, 2021 WL 3870697, at *2 (11th Cir. Aug. 31, 2021) ("Here, the shelter-in-place order that Gilreath cites did not damage or change the property in a way that required its repair or precluded its future use for dental procedures.").

in *Hardinger* was not "complete uninhabitability" – it was whether the presence of E. coli had "nearly" eliminated the functionality of the property as a home, even though individuals could ostensibly have entered and used the property for other purposes. The Third Circuit, in *Port Authority of New York & New Jersey v. Affiliated FM Insurance Co*., 311 F.3d 226 (3d Cir. 2002), applied a similar standard. CRO's allegations fall squarely into this well-established line of authority and easily satisfy this standard at the motion to dismiss stage. R-59-60, ¶¶ 29-33; R-1938-40, ¶¶ 32-39.

Thus, Westport's assertion that CRO was required to show that its property was "completely useless or uninhabitable" as a result of the virus has no basis in the law or Policy. Rather, this Court should apply the standard historically utilized by courts in New York, the Third Circuit, and courts across the country to evaluate whether and when noxious substances constitute physical loss or damage. Because CRO's allegations easily satisfy this standard, this Court should reverse the trial court's decision granting Westport's motion to dismiss.

B. Westport Fails to Rebut That, Under the Plain Language of the Policies, CRO Has Sufficiently Alleged Physical Loss or Damage

Westport's misapplication of *Roundabout* and its misstatement of New York law reflects its inability to rebut the sufficiency of CRO's allegations under the applicable standard and the plain terms of the Policy. CRO alleged in detail that the actual presence of COVID-19 – a deadly, resilient, physical substance that attaches

to and alters air and property – impaired the physical function of the Restaurants for their intended purpose, in-person dining. R-54-56, 59-60 ¶¶ 12-21, 29-33; R-1932-40, ¶¶ 13-39. In its opening brief, CRO explained that these allegations fall squarely into the plain and ordinary meaning of the undefined terms "physical loss or damage" based on basic dictionary definitions and the reasonable expectations of the average insured – which is the guiding principle of insurance policy interpretation in New York. *See* Opening Br. at 20-22; *Dean v. Tower Ins. Co. of N.Y.*, 19 N.Y.3d 704, 708 (2012). Further, CRO cited many well-reasoned cases spanning decades and from across the country, including numerous recent cases in the COVID-19 context, supporting this conclusion.

Nevertheless, and despite conceding the applicability of these interpretative standards under New York law, Westport's opposition glosses over this threshold argument entirely and largely ignores CRO's cases. Similarly, Westport ignores CRO's argument that an insurance policy must be interpreted as a whole and that, here, the Policy expressly covers physical loss or damage resulting from invisible substances such as "radioactive contamination," which makes clear that "physical loss or damage" under this Policy does not require a visible alteration or tangible damage to property.

Instead, Westport argues that this Court should ignore that Westport included exclusions in the Policy which expressly refer to certain invisible contaminants as

types of "loss or damage" – exclusions which would be superfluous given Westport's current interpretation of that term. Op. Br. at 30-31. Indeed, contrary to Westport's position, CRO is not arguing that this Court should create coverage based on some purported negative inference. Rather, the terms and conditions of the Policy when read as a whole, including its exclusions, inform the interpretation of the undefined term "physical loss or damage." Here, those exclusions would be pointless unless the Policy covered physical loss and damage from on-site viruses and viral diseases of the type that CRO has alleged. Accordingly, a reasonable policyholder would conclude that the physical presence of a virus in and on insured property can result in physical loss or damage under the Policy.

Westport's failure to grapple with these threshold principles of insurance policy interpretation reveals a simple truth: Westport has no retort to the conclusion that a reasonable insured reading the terms and conditions of this Policy would construe the undefined phrase "physical loss or damage" to encompass a circumstance where, as here, the insured has lost the ability to physically utilize some or all of its property due to the actual presence of a dangerous, physical substance.

C. Westport Misstates CRO's Arguments, Mischaracterizes CRO's Allegations, and Ignores Critical Policy Language Undermining Westport's Position

i. Westport Misstates CRO's Arguments and Allegations Regarding Physical Loss or Damage

To support its heavy reliance on *Roundabout* – a case that involved purely economic losses – Westport mischaracterizes CRO's position as being that "direct physical loss or damage to property . . . can be reasonably interpreted to include the loss of use of property." Op. Br. at 13. Based on this false premise, Westport analogizes CRO's claim to where an insured has suffered economic losses because a city has changed its maximum occupancy for restaurants, or where a city issues an ordinance requiring a restaurant to cease operations at an earlier time of day. *Id.* at 14. But in Westport's examples, the "loss of use" of property is untethered to any physical impact to insured property. Here, in contrast, CRO has alleged the physical presence and impact of a dangerous substance in and on its properties, which resulted in a loss of functionality. R-59, 60, ¶¶ 31, 35; R-1941, 1943, ¶¶ 41-42, 49-50. The fact that Westport is forced to misstate CRO's position to try to shoehorn it into *Roundabout* and into examples where coverage would not be available reflects that Westport cannot overcome CRO's actual allegations as pled.

Seemingly anticipating this weakness in its argument, Westport further asserts that CRO's losses were "not because of any internal, physical impact to its property." Op. Br. at 10-11. Rather, Westport contends that CRO's losses resulted from governmental orders. *Id.* This argument, however, is contrary to CRO's allegations, both in its original complaint and its proposed amended complaint, that its losses resulted from the physical presence of the virus on its properties, and that CRO

operated its restaurants with severe limitations even after those orders were relaxed or lifted. R-59-60, ¶¶ 29-33; R-1938-40, ¶¶ 32-39. Indeed, CRO alleged, in detail, that the virus physically attached to and altered the Restaurants, as well as the air within the Restaurants. R-60, 68, ¶¶ 36, 61; R-1942-43, ¶¶ 46-47.

Further, Westport fails to even mention, let alone rebut, CRO's argument that whether its losses stem from governmental orders or the physical presence of the virus is a quintessential fact question that cannot be resolved at the motion to dismiss stage. Opening Br. at 49-50. *See Molycorp, Inc. v. Aetna Cas. & Sur. Co.*, 78 A.D.2d 510, 510 (1st Dep't 1980) ("[W]here two causes lead to a loss…the relevant inquiry is to determine which of the two was the dominant and efficient cause of the loss, generally a factual issue to be determined by the trier of the facts."). And, even if CRO's losses were caused by the governmental orders alone, numerous of those orders expressly state that they were issued, in part, because of the virus's propensity to impact property. R-51, ¶ 3; R-1929, 1940, ¶¶ 3, 38.

Westport also argues that CRO is asking this Court to accept the allegations in its complaint "as true, regardless of their implausibility." Op. Br. at 33. It further asserts that CRO's "conclusory claims" are "too vague, too unsubstantiated, and too implausible to establish, by itself, the necessary conditions for coverage." *Id.* The Court should reject Westport's casual assertions that allegations with which it disagrees are "vague" or "implausible." Indeed, CRO supported its allegations with

considerable detail regarding the nature, presence and impact of the coronavirus, and supported these allegations by citation to scientific sources, even though such citations are not even required at the pleading stage. R-54-56, ¶¶ 12-21; R-1932-38, ¶¶ 13-31.

Westport's only retort is to point to a single allegation from CRO's initial complaint that the "virus might not be actually present at the Restaurants." Op. Br. at 33. As CRO explained, however, Westport misconstrues the intent of that allegation, which was to (1) acknowledge that CRO's Restaurants, which operate across the country, may have had different amounts of COVID-19 exposure at different times, and (2) show why CRO was not limited to coverage under the Policy's "communicable disease" coverage grant, rather than to allege that the virus was never present at its properties. R-59, 60, ¶¶ 31, 35; R-1941, 1943, ¶¶ 41-42, 49-50. To avoid any confusion, CRO removed that allegation from its proposed amended complaint. That Westport continues to cite this provision as the sole example of its "implausibility" argument – a provision that would not even be included in the operative complaint had the court properly granted CRO's motion to amend – is telling.

Finally, Westport accuses CRO of "wrongly complain[ing] that the Supreme Court erred because it did not receive or consider any scientific evidence." Op. Br. at 32. This is incorrect. CRO's argument is that the trial court erred because it

effectively invented its own scientific record *sua sponte* at a hearing on a motion to dismiss, and then improperly assessed the sufficiency of CRO's allegations against that record. Indeed, it is telling that Westport does not even attempt to defend the trial court's baseless suggestions that CRO could have easily cleaned COVID-19 from its properties in minutes, or could have avoided the impact of the virus by simply closing its doors or testing every would-be patron. That is because the trial court erred in resolving hotly disputed factual and scientific issues against CRO at the motion to dismiss stage.

ii. Westport Ignores or Misconstrues Key Policy Terms

Westport asserts that CRO cannot show physical loss or damage because "its employees were allowed in the restaurants in order to serve customers for drive-through, takeout, and delivery." Op. Br. at 36. Indeed, Westport asserts that COVID-19 cannot cause physical loss or damage because numerous locations, such as hospitals and police stations, remained open throughout the pandemic. *Id.* at 17, 38. These arguments fundamentally misconstrue the coverage afforded by the Policy.

The Policy covers every part of the insured properties, not simply certain parts. Thus, for example, if the dining area of CRO's Restaurants was destroyed in a fire, CRO would be entitled to coverage for resulting losses, including business interruption losses from reduced sales, even if it could still use its kitchen to provide

take-out orders. The result is no different here, where CRO's dining areas were rendered unusable by the presence of the virus, but certain of its kitchen spaces could still be used to prepare take-out orders by a limited number of individuals wearing appropriate protective gear. Indeed, the Policy's business interruption coverage expressly applies when an insured is "partially prevented from…continuing business operations or services." R-62, ¶ 46; R-1946, ¶ 63. Similarly, the Policy covers business interruption losses resulting from a "partial" prohibition on access as a result of a civil authority. R-66, ¶ 54; R-1949, ¶ 71. That is precisely what CRO experienced here.

Moreover, certain locations, such as hospitals and police stations, remained open during the pandemic despite the mortal risk of remaining open because of their essential nature, not because those locations were somehow safe for human presence. The best evidence of this is that the employees in those locations wore protective gear just to enter, something a patron trying to eat in CRO's Restaurants could not do. The extraordinary burden shouldered by those essential workers and those close to them should be praised, not used as a yardstick to deny coverage to other "non-essential" businesses. Put differently, the fact that a doctor could enter a hospital wearing an N-95 mask and a plastic shield to perform emergency care in March 2020, does not mean that the dining rooms of CRO's Restaurants were habitable for casual dining during that same period. On the contrary, the fact that

only certain locations were permitted to remain open despite the considerable risk to human life from the presence of the virus is persuasive evidence of why CRO's dining areas were rendered useless by the presence of the virus.

Finally, Westport argues that the Policy's "period of liability" shows that there was no physical loss or damage because property impacted by COVID-19 is not "repaired or replaced" with "current materials of like size, kind and quality." Op. Br. at 28. This argument, however, ignores that CRO's efforts to sanitize its property, and to clean the air with filtration systems, clearly constitutes efforts to repair its properties with current materials of like size, kind and quality. Indeed, Westport's reliance on this provision to inform the meaning of physical loss or damage is particularly questionable given that Westport asks this Court to ignore other Policy provisions, such as coverage for radiation contamination, and exclusions for invisible contaminants that the Policy considers "loss or damage," which would make no sense if the "period of liability" is interpreted to limit coverage as Westport suggests.

Westport's proposed reading also turns the "period of liability" provision upside down. That provision narrows the period of time during which Westport must pay a business interruption loss if the affected property can reasonably be repaired or replaced. But that does not mean, as Westport's proposed reading implies, that the Policy excludes coverage if the property cannot reasonably be

repaired or replaced. Rather, in such a circumstance, the property still would suffer a "physical loss or damage," and Westport would be obligated to pay associated business interruption losses up to the limits of liability of the Policy.

II. NO EXCLUSION BARS COVERAGE AT THE MOTION TO DISMISS STAGE

A. The Contamination Exclusion Does Not Apply

Westport does not dispute that the contamination exclusion in the Policy is subject to the following lead-in language: "loss or damage due to the discharge, dispersal, seepage, migration, release or escape of . . . materials that may be harmful to human health." And Westport cannot dispute that the New York Court of Appeals has interpreted this type of lead in language to limit the exclusion to traditional environmental pollutants. *See Belt Painting Corp. v. TIG Ins. Co*., 100 N.Y.2d 377 (2003). Indeed, a New Jersey court recently found a similar contamination exclusion inapplicable, holding that this type of exclusion only applies to "traditional environmental and industrial damage," and not to a naturally occurring virus. *See Ocean Walk, LLC v. American Guarantee and Liability Ins. Co., et. al*., ATL-L-0703-21 (N.J. Sup. Ct. Dec. 22, 2021) (attached as addendum).

Even without *Belt Painting* as a backdrop, a reasonable insured could read this exclusion as only applying to contaminants in the context of traditional pollution. *See JGB Retail Lessee, LLC v. Starr Surplus Lines Ins. Co.,* No. A-20-816628-B, 2020 WL 7190023, at *3 (D. Nev. Nov. 30, 2020) (insurer "has not

shown that it is unreasonable to interpret the Pollution and Contamination Exclusion to apply only to instances of traditional environmental and industrial pollution and contamination that is not at issue here"); *Seifert v. IMT Ins. Co.*, 495 F. Supp. 3d 747, 752 n.6 (D. Minn. 2020) (holding an insurer's attempt to place the coronavirus within a pollution exclusion was "unavailing").

Nevertheless, Westport argues that this Court should effectively ignore this lead-in language. To support this argument, it cites *Nguyen v. Travelers Casualty Insurance Co. of America*, No. 20-cv-00597, 2021 WL 2184878, at *15 (W.D. Wash. May 28, 2021) and *Rhonda Hill Wilson v. Hartford Casualty Co.*, 492 F. Supp. 3d 417, 427 (E.D. Pa. 2020), neither of which contained the critical lead-in language at issue here. It also cites to *Broome County v. Travelers Indemnity Co.*, 125 A.D.3d 1241 (3d Dep't 2015), which does not reflect the law in the First Department, which does not limit *Belt Painting* to third-party policies, but extends it to first-party policies as well. *See Vigilant Ins. Co. v. V.I. Techs., Inc.*, 676 N.Y.S.2d 596, 597 (1st Dep't 1998) ("The commonly understood meaning of the language in question should not be held to be different depending on whether it is used in a 'first-party' or 'third-party' policy.").

Next, Westport cites *Northwell*, in which a federal trial court found that a naturally occurring virus fits within this exclusion because a "sneeze" is a type of "discharge" or "dispersal." 2021 WL 3139991, at *9. This conclusion is contrary

to *Belt Painting* and to the reasonable interpretation of the average insured reading this language, who would not consider a "sneeze" to fall into the category of "discharge, dispersal, seepage, migration, release or escape of materials." Put differently, CRO is not treating the word "virus" as if it is not in the exclusion – rather, the exclusion can be reasonably interpreted to be limited to instances where, for example, a virus is discharged or released through biomedical waste pollution, or leaked from a research laboratory. If Westport wanted to exclude coverage for a naturally occurring virus it was required to do so clearly and unambiguously (Opening Br. at 42-43), such as by using the standard-form virus exclusion widely available in the insurance marketplace, not by sticking the word "virus" in exclusionary language that, on its face and as interpreted by the New York Court of Appeals, would not apply here.

B. The Microorganism Exclusion Does Not Apply

Westport fails to rebut that there is a split of authority regarding whether a virus constitutes a microorganism. Opening Br. at 45-47. Instead, it pretends that authority undercutting its position simply does not exist. Further, it cites no cases supporting its position that this exclusion would bar coverage here; nor does it make any effort to distinguish authority holding otherwise. *See id.* at 45-46; *Schleicher & Stebbins Hotels, LLC v. Starr Surplus Lines Ins. Co.*, No. 217-2020-CV-00309, 2021 WL 4029204, at *11 (N.H. Super. Ct. June 15, 2021) ("The Microorganism

Exclusion is not applicable to SARS-CoV-2, because a virus is not unambiguously understood to be a 'microorganism.'"). Thus, Westport fails to establish that this exclusion is subject to no reasonable interpretation that results in coverage. As such, Westport's argument fails as a matter of law. *See Sincoff v. Liberty Mut. Fire Ins. Co.*, 11 N.Y.2d 386, 390 (1962) (holding that where experts "disagree as to the meaning of [a] word, and the dictionaries contain varying connotations" the term "is capable of more than one meaning" and therefore, its meaning "must be resolved in favor of the insured"); *Chang v. Gen. Accident Ins. Co. of Am.*, 598 N.Y.S.2d 178, 180 (1st Dep't 1993) (ambiguity in an insurance provision "which is subject to more than one reasonable interpretation, must be construed most favorably to the insured and strictly against the insurer").

Moreover, this exclusion expressly references mold, mildew, fungus and spores – which are four strikingly specific microorganisms that fall within the kingdom of fungus. The omission of viruses from this list is thus particularly notable and would lead a reasonable insured to conclude that a virus does not fall within the exclusion. Thus, the exclusion does not apply for this reason as well.

C. The Loss-of-Market Exclusion Does Not Apply

Westport does not dispute that the "Loss-of-Market" exclusion is limited to purely economic losses untethered to physical impacts to property, such as a circumstance where a policyholder's products become less popular in the

marketplace, rather than losses stemming from physical loss or damage. It does not mention, let alone rebut, CRO's argument that Westport's interpretation of this exclusion would render coverage illusory. And it cannot rebut that CRO pleads various causes of loss, including the actual presence of the virus. R-52, 59-61, ¶¶ 4, 29-38; R-1930, 1941-1944 ¶¶ 4, 41-53. Thus, its argument that this exclusion applies because the Orders, rather than any physical loss or damage, caused CRO's losses, would require this Court to reject CRO's allegations, and resolve the quintessential fact question of causation in favor of Westport at the motion to dismiss stage. *See Duane Reade, Inc. v. St. Paul Fire & Marine Ins. Co*., 411 F.3d 384, 398-99 (2d Cir. 2005) (noting that the insurer's "assertion that the 'loss of market' exclusion applies to Duane Reade's claim" because its losses were caused by a loss of market due to the collapse of the World Trade Center, rather than the physical loss or damage caused by the collapse, "creates, at most, a factual issue concerning the amount of loss Duane Reade may recover"). Westport cites no authority to support this proposition.

D. The Reasons Not Covered Exclusion Does Not Apply

Westport's continued insistence that the "Reasons-Not-Covered" exclusion is applicable to CRO's claim should be rejected. This exclusion only applies to exclude those time-element losses that are not due to physical loss or damage. CRO has robustly pled physical loss or damage as a basis for its time element recovery –

and does not seek time-element recovery for other reasons not covered – making this exclusion inapplicable.

III. THE COURT ERRED IN DENYING CRO'S MOTION FOR LEAVE TO AMEND ITS COMPLAINT

Westport defends the trial court's denial of CRO's motion to amend its complaint on three grounds, none of which survive scrutiny.

First, Westport argues that the proposed amended complaint would not impact the result of the motion to dismiss and, thus, is palpably insufficient. This argument, however, presupposes that COVID-19 categorically cannot cause physical loss or damage under any circumstances. Indeed, although CRO's original complaint was sufficient, its amended complaint added considerable details regarding the nature and impact of COVID-19 on CRO and its Restaurants. These allegations leave no doubt that CRO suffered losses as a result of the physical presence of a deadly, physical substance on and in its properties, which constitutes "physical loss or damage."

Second, Westport asserts that the trial court already addressed all of the "proposed factual allegations CRO seeks to add." Not so. At the August 4, 2021 hearing, the trial court asked a series of questions that revealed that the court was not accepting CRO's allegations as true, as required, and was not drawing reasonable inferences in CRO's favor, as required. The trial court also inquired into the physicality of the virus, the nature of its impact on property, and certain of CRO's

allegations regarding whether and how the virus was present on insured property because in the court's view they were absent from the complaint. Thus, CRO sought leave to file an amended complaint that would address those perceived gaps and make its position abundantly clear. To the extent Westport now asserts that even that amended complaint would not be enough, this simply reveals that Westport's denial of coverage is divorced from the facts.

Third, Westport argues that CRO's proposed amendment deleted a key factual allegation from its original complaint that "no restaurant had access limited due to a government order due to the presence of the SARS-Co-V-2 virus" and accuses CRO of pleading alternative facts. The reason CRO removed this allegation from the amended complaint, however, is precisely because Westport had misinterpreted its intent, which was to make clear that the virus was not present at every Restaurant at all times such that CRO was not limited to the Policy's communicable disease coverage; it was not to allege that the virus was not present on any of the properties. In fact, the original complaint made clear the virus was present on the Restaurants. R-60, ¶ 36. Thus, the amended complaint sought to clarify that point. In any case, this has no bearing on whether the proposed amended complaint was insufficient.

CONCLUSION

For the foregoing reasons, the trial court's decisions granting Westport's motion to dismiss and denying CRO's motion for leave to file an amended complaint should be reversed.

Dated: December 23, 2021

By: Robin L. Cohen

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I hereby certify pursuant to 22 NYCRR 1250.8(j) that the foregoing brief was prepared on a computer using Microsoft Word.

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UNPUBLISHED DECISION

BY THE COURT:

SUPERIOR COURT OF NEW JERSEY
LAW DIVISION
ATLANTIC COUNTY
DOCKET NO.: ATL-L-0703-21

Civil Action

ORDER

AC OCEAN WALK, LLC :

Plaintiff, :

vs. :

AMERICAN GUARANTEE AND LIABILITY INSURANCE COMPANY; AIG SPECIALTY INSURANCE COMPANY; NATIONAL FIRE & MARINE INSURANCE COMPANY; and INTERSTATE FIRE AND CASUALTY COMPANY, :

Defendants. :

THIS MATTER having been brought before the court by defendants by way of a joint motion seeking an order dismissing the complaint pursuant to Rule 4:6-2(e) of the New Jersey Court Rules, and the court having read and reviewed the moving and opposition papers and having heard oral argument; and it appearing to the court that good cause has been shown; and for the reasons set forth by the court in its written decision of this date;

IT IS on this 22 day of December, 2021, **ORDERED** as follows:

1. As to defendant National Fire and Marine Insurance Company, the motion is granted and the complaint is dismissed.

2. The motion is denied as to the remaining defendants American Guarantee and Liability Insurance Company, AIG Specialty Insurance Company and Interstate Fire and Casualty Company.

3. A copy of this order shall be deemed served upon all counsel of record upon being uploaded to eCourts.

HON. MICHAEL WINKELSTEIN, J.A.D.
(retired and temporarily assigned on recall)

MOTION:

_X_. Opposed
____ Unopposed

NOT FOR PUBLICATION WITHOUT
THE APPROVAL OF THE COMMITTEE ON OPINIONS

AC OCEAN WALK, LLC, Plaintiff, vs. AMERICAN GUARANTEE AND LIABILITY INSURANCE COMPANY AIG SPECIALTY INSURANCE COMPANY, NATIONAL FIRE & MARINE INSURANCE COMPANY; AND INTERSTATE FIRE & CASUALTY COMPANY, Defendants.	SUPERIOR COURT OF NEW JERSEY LAW DIVISION ATLANTIC COUNTY DOCKET NO.: ATL-L-0703-21 Civil Action DECISION RE: R.4:6-2(e) MOTION

Decided: December 22, 2021

Stephen M. Orlofsky, Esquire (BLANK ROME) for plaintiff, AC Ocean Walk, LLC.

Edward M. Pinter, Esquire (FORD MARRIN ESPOSITO WITMEYER AND GLESER, LLP) for defendant, American Guarantee and Liability Insurance Company.

Peter E. Kanaris, Esquire (Pro Hac Vice) (HINSHAW AND CULBERSTON, LLP) for defendant, National Fire and Marine Insurance Company.

Michael D. Hynes, Esquire (DLA PIPER LLP) for defendant, Interstate Fire and Casualty Company.

Shawn L. Kelly, Esquire (DENTONS US LLP) for defendant, AIG Specialty Insurance Company.

MICHAEL WINKELSTEIN, J.A.D. (retired and temporarily assigned on recall).

AC Ocean Walk, LLC, the Ocean Casino, has filed suit against multiple insurance carriers seeking coverage for COVID-19 related losses under the quota-share insurance policies Ocean purchased from the insurers. The defendants are the American Guarantee and Liability Insurance

Company (the Zurich policy), the AIG Specialty Insurance Company (the AIG policy), the National Fire and Marine Insurance Company (the National Fire policy), and the Interstate Fire and Casualty Company (the Interstate policy). The insurers have declined coverage. They now move pursuant to R. 4:6-2(e) for dismissal of Ocean's complaint.

The insurance carriers make two primary and one secondary argument. First, they allege that to establish coverage, the policies require actual physical damage to the property, and the COVID-19 did not create any actual physical damage to Ocean's property. In policy terms, the carriers claim Ocean sustained no "direct physical loss of, or damage to, the insured property" and consequently the insurers are not required to provide coverage. The carriers also assert that even if plaintiff could meet its burden to establish direct physical loss of, or damage to, the property, the policies contain contamination exclusions, which explicitly exclude coverage for any loss due to a "virus."

The secondary argument applies only to the National Fire policy. That policy contains an endorsement that excludes coverage for damages in any way related to pathogenic or poisonous biological or chemical substances. National Fire asserts that the endorsement precludes coverage for damage caused by the COVID-19 virus.

Ocean asserts it is entitled to coverage. It claims that the COVID-19 virus caused a direct physical loss of plaintiff's property: that loss being the loss of use of the Ocean Casino, when the risk of damage to the health and property that accompanied the COVID-19 became imminent and the casino was forced to close. Ocean argues that direct physical loss is satisfied when the property is unable to be used for its intended purpose.

Plaintiff further asserts that the property did in fact suffer direct physical loss of its property because of the actual presence of the COVID-19 on the premises, which fundamentally altered and

damaged the surfaces and the air space within the casino, preventing Ocean's use of the property. Also, Ocean submits that the insurance policies included broad language insuring against "risks of" direct physical loss or damage to the property. Ocean asserts that these risks ultimately came to pass and resulted in the closure of the casino. In addressing the contamination exclusion, plaintiff maintains that as written, it is unenforceable under New Jersey law because the purpose of the exclusion is to preclude traditional environmental pollution, not a communicable disease such as the COVID-19 virus.

The legal standard under R.4:6-2(e)

Rule 4:6-2(e), requires the complaint be searched in depth with liberality to determine if a cause of action can be gleaned even from an obscure statement, particularly if further discovery will be taken. Every reasonable inference is consequently accorded a plaintiff and the motion should be granted only in rare instances and ordinarily without prejudice. Printing Mart-Morristown v. Sharp Electronics, 116 N.J. 739, 746 (1989). Nevertheless, if the complaint states no basis for relief and discovery would not provide one, dismissal of the complaint is appropriate. Camden County Energy Recovery Associates v. NJ Department of Environmental Protection, 320 N.J. Super. 59, 64 (App. Div. 1999), aff'd o.b., 170 N.J. 246 (2001). Simply making non-particularized allegations does not satisfy New Jersey's pleading requirements. Lederman v. Prudential Life Ins. Co., 385 N.J. Super. 324, 349 (App. Div. 2006).

The legal standard for insurance contract construction

The law addressing the construction of insurance policies in this state is well-settled. Insurance policies are contracts of adhesion. Longobardi v. Chubb Ins. Co., 121 N.J. 530, 537 (1990). The interpretation of an insurance policy, like any contract, is a question of law. Sosa v. Massachusetts Bay Ins. Co., 458 N.J. Super 639, 646-47 (App. Div. 2019). In performing its

interpretative task, the court looks first to the plain language of the policy, and if it is unambiguous, the court will not strain to provide a better policy than the one obtained. Ibid. The court is guided by general principles: "coverage provisions are to be read broadly, exclusions are to be read narrowly, potential ambiguities must be resolved in favor of the insured, and the policy is to be read in a manner that fulfills the insured's reasonable expectations." Id. at 646. The insurer bears the burden to establish that an exclusion applies. Ibid. In determining whether there is an ambiguity, the court "considers whether an average policyholder could reasonably understand the scope of coverage, and whether better drafting could put the issue beyond debate." Ibid. "If there is more than one possible interpretation of the language, courts apply the meaning that supports coverage rather than the one that limits it." Id. at 646-47.

The Policies

Plaintiff purchased four all-risk insurance policies, all insuring the Ocean property, a casino, in Atlantic City. The first policy provision in dispute is the insuring agreement. The specific question is: what is the meaning of "direct physical loss or damage?" The policies do not define that term. The insuring agreement substantially reads the same in each policy. It says:

> This policy insures against direct physical loss of, or damage caused by, a covered cause of loss to covered property, at an insured location [the casino] . . . subject to the terms, conditions and exclusions stated in this policy.

The next issue addresses the pollution exclusions. The question there is: does the inclusion of the term "virus" in the exclusions preclude coverage for COVID-19? "Virus" is included in the definition of contamination but is not listed as a contaminant. A **Contaminant(s)** is defined to include:

> Any solid, liquid, gaseous, thermal, or other irritant, pollutant, or contaminant, including but not limited to smoke, vapor, soot, fumes, acids, alkalis, chemicals,

> waste including material to be recycled, reconditioned, or reclaimed, asbestos, ammonia, other hazardous substances, **Fungus** or **Spores**.[1]
>
> **Contamination (Contaminated)**, includes:
>
> Any condition of property due to the actual presence of any foreign substance, impurity, pollutant, hazardous material, poison, toxin, pathogen or pathogenic organism, bacteria, virus, disease causing or illness causing agent, **Fungus**, mold or mildew.

The Interstate and National fire policies have an exclusion section referred to as a "Pollution Contamination Exclusion." They are substantially the same and read as follows:

> There will be no payment for "loss, damage, cost or expense caused directly or indirectly by . . . the release, migration, discharge, escape or dispersal of Contaminants . . . Contaminants means materials that may be harmful to human health, and include any impurity, pollutant, poison, toxin, pathogen or pathogenic organism, disease-causing or illness-causing agent, asbestos, dioxin, polychlorinated biphenyls, agricultural smoke, agricultural soot, vapor, fumes, acids, alkalis, bacteria, virus, and hazardous substances listed in the Federal Water Pollution control Act, Clean Air Act, Resource Conservation and Recovery Act of 1976, Toxic Substances Control Act, or as designated by the United States Environmental Protection Agency or any other local governmental agency . . . .

National Fire has an additional exclusion that the three other carriers do not. It is the Biological or Chemical Substances Exclusion Endorsement. The court will later address whether that exclusion precludes coverage for COVID-19. It states:

> This policy does not provide coverage for any loss, cost, expense or damage of any nature, however caused, directly or indirectly arising out of, resulting from, or in any way related to the actual or suspected presence or threat of any pathogenic or poisonous biological or chemical substance or material of any kind, including but not limited to, any malicious use of such substance or material, whether isolated or widespread, regardless of any other cause or event contributing at the same time or in any sequence.

Discussion

The Insuring Agreement

The insuring agreement provides coverage for <u>direct physical loss of, or damage caused by, a covered loss to covered property</u>. The carriers assert that this standard requires some type

[1] The terms Fungus and Spores are highlighted in the originals.

of physical alteration to the property, which, according to the carriers, plaintiff is unable to show. The Ocean, on the other hand, puts forth two primary arguments to show that it is entitled to coverage under the insuring agreements. It argues that the facts as pleaded in the complaint sufficiently show a physical alteration to the property to defeat a R.4:6-2(e) motion. Plaintiff also asserts that the insuring agreements language of "direct physical loss" is satisfied by a loss that renders the property unusable for its intended purpose; that a physical alteration to the property is not necessary to meet the policy standard of a direct physical loss.

The court's discussion begins with whether the complaint was sufficiently pleaded to articulate enough facts to state a claim for relief. Bell Atl. Corp. v. Twombly, 550 U.S. 544, 570 (2007). In the complaint, at paragraphs 106-122, plaintiff alleged that the COVID-19 virus, which is transmitted through physical particles in the air and on surfaces, presented an imminent threat to Ocean's facilities, its customers and employees, rendering the casino unsafe. Para. 106-107. The complaint asserts that the respiratory droplets expelled from individuals land on, attach, and adhere to surfaces and objects, which renders physical changes to the property and its surface by becoming part of its surface; and as a result of that physical alteration, contact with those previously inert surfaces [the property] was made unsafe. Para. 113. Plaintiff further pleaded that numerous scientific studies documented that COVID-19 can physically remain on and alter property for extended periods of time. Para. 114. Ocean claims that the chain of events caused by the Pandemic created both actual direct physical loss or damage to Ocean's property, and a continued threat of direct physical loss or damage. Para. 120.

These claims constitute fact-based pleadings from which a cause of action that the COVID-19 damaged Ocean's physical premises may be gleaned. The facts may be in dispute, but that is an issue for another day. It is this court's opinion that the pleadings are sufficient to show that the

COVID-19 damaged the Ocean's premises; this meets the requirements for coverage pursuant to the insuring agreements, and, accordingly, the complaint satisfies the Printing-Mart criteria to survive a R.4:6-2(e) motion.

The court is also satisfied that the insuring agreement language that requires a "direct physical loss" to warrant coverage may be satisfied if the property becomes unusable for its intended purpose, whether or not the property is altered by the COVID-19 virus. Here is why.

In Wakefern Food Corp. v. Liberty Mutual Fire Insurance Co, 406 N.J. Super 524, 529 (App. Div. 2009), problems developed with the North America power system and electrical grids, which resulted in an electrical blackout over the Northeastern United States and portions of Canada. Wakefern is a group of supermarkets that suffered losses due to food spoilage during the blackout and sought coverage from its carrier, Liberty Mutual. The policy covered, among other things, damage due to the loss of electrical power. Id. at 530-31. The policy applied only in case of "physical damage to off-premises electrical plant and equipment." Id. at 531-32. Although the power grid was physically incapable of supplying power for four days, the transmission lines, connections and supply pipes suffered no "physical damage." Id. at 538. As a result, Liberty Mutual denied coverage. Id. at 538. "Physical damage" was an undefined term under the policy. Id. at 540.

Wakefern filed suit and the carrier moved to dismiss. The trial court agreed with the carrier and dismissed the complaint. The Appellate Division reversed. Id. at 524. The appellate court found that the term "physical damage" was ambiguous, and the trial court should not have construed the term so narrowly in favor of the insurance carrier in a motion to dismiss; rather, the court observed that the policy should be construed in a manner favoring the insured, rather than the insurer, in determining what was a reasonable expectation of the insured. Id. at 540. See

Flomerfelt v. Cardiello, 202 N.J. 432, 441 (2009) (if terms of insurance policy are not clear, but are ambiguous, they are to be construed against insurer not the insured, so as to give effect to insured's reasonable expectations).

The Wakefern court found that the electrical grid was "physically damaged" because, due to a series of incidents that occurred outside of the plaintiff's insured properties, the grid and its component generators and transmission lines were "physically incapable of performing their essential function of providing electricity." Id. at 540. And that failure resulted in damages to the supermarkets, which could not function without electricity. The court said that the loss of function was akin to direct physical damage under the terms of the policy. Id. at 541.

Similarly, here, Ocean argues its entitlement to coverage because of its inability to operate its gaming floor and hotel rooms as a result of the virus – a loss of the casino's function. Put simply, Ocean asserts that it was unable to operate according to its essential functions by the imminent risk of damage that would be caused by the COVID-19.

Plaintiff submits, and for purposes of this R.4:6-2(e) motion the court accepts as true, that the primary source of the property's revenue was its casino floor and guest accommodations, which were eliminated and destroyed by the presence and imminent threat of the COVID-19, in the air space and on the surfaces, rendering those parts of the property functionally useless and not fit for their intended purpose. That position is consistent with the principles discussed in Wakefern and supports Ocean's claim for coverage. The insurers here did not define the term "physical damage." The policy language is ambiguous. It can be construed to support Ocean's, as well as the carriers', positions as to the meaning of the insuring agreements. "[I]f there is more than one possible interpretation of the language, courts apply the meaning that supports coverage rather than the one that limits it." Sosa, 458 N.J. Super at 646-47.

Wakefern is not the only New Jersey decision that does not require physical alteration of the property to constitute direct physical loss for insurance coverage purposes. The case of Customized Distribution Services v. Zurich Ins. Co., 373 N.J. Super. 480 (App. Div. 2004) can similarly be read to support plaintiff's arguments. There, the Campbell Soup Company filed a complaint against Customized Distribution Services (CDS), which operated a warehouse in New Jersey. Id. at 483. In warehousing a Campbell beverage product named "Splash," CDS failed to locate and ship the beverage in a timely manner and as a result Campbell claimed damages. Ibid. CDS sought insurance coverage from the defendant Zurich, under an all-risk policy. Id. at 484. The claim by Campbell was that CDS failed to properly distribute the product. Id. at 485. The policy said: "covered causes of loss means risks of direct, physical loss to covered property." Id. at 486. Zurich contended there was no coverage because there was no "direct physical loss" as required by the policy.

The appellate court found that for coverage to apply, it was not necessary that the product's material or chemical composition be altered. Id. at 488. It explained that the term "risk" as in risk of direct, physical loss, supported the view that the policy did not require that there be any actual physical damage to or alteration of the material composition of the property or its packaging. Ibid. In considering the parties reasonable expectations and understanding that the Splash beverage did not undergo a change in material composition, but rather how the product was perceived by Campbell's customers as a result of an undue passage time, the court found that such a change was the "functional equivalent" of damage of a material nature or an alteration in physical composition. Id. at 490. The court found that coverage can exist without a product's material alteration or packaging alteration. Id. at 491. The court stated that the term "physical" can mean more than material alteration or damage, and it would have been incumbent upon the insurer to rule out

coverage clearly and specifically under the circumstances where material damage did not occur. Ibid.

Two federal cases support the same analysis. In Port Authority v. Affiliated FM Insurance Co., 311 Fed. 3d 226, 230 (3d Cir 2002), the plaintiff sought recovery from its insurance carrier for the abatement of asbestos contamination. The District Court held "that unless asbestos in a building was of such quantity and condition as to make the structure unusable, the expense of correcting the situation was not within the scope of a first party insurance policy covering physical loss or damage." Ibid. The Third Circuit affirmed. It agreed with the District Court's articulation of the proper standard for "physical loss" for asbestos contamination, accepting the proposition that "[w]hen the presence of large quantities of asbestos in the air of a building is such as to make the structure uninhabitable and unusable, there has been a distinct loss to its owner. Id. at 236. And if there is a release of asbestos-containing materials that contaminates the property to the extent "such that the function is nearly eliminated or destroyed, or the structure is made useless or uninhabitable, that would cause such a loss of utility." Ibid. Thus, asbestos in the air could, without actual damage to the building, be considered a physical loss or damage if the asbestos was of sufficient quantity to render the building unusable.

Said another way, though the structure in Port Authority, the World Trade Center, continued to function, had the asbestos contamination been sufficiently severe as to render the structure unusable, coverage would have been afforded under the policy. That is essentially the position Ocean takes here vis-a-vis the COVID-19 virus and its effect on the Ocean – the COVID-19 rendered the property unfit for its intended purpose, causing the property to lose is essential function.

In Gregory Packaging Co., Inc. v. Traveler's Property Casualty Company of America, 2014 Dist. Lexis 165232 (Dist. Of N.J. Nov. 25, 2014), ammonia had been physically released into the air in the plaintiff's packaging facility in Newark. Id. at 3. Those heightened ammonia levels rendered the facility unfit for occupancy until the ammonia dissipated. Id. at 5. The building was not otherwise physically damaged. The New Jersey District Court observed that under New Jersey law, physical loss or damage is provable without experiencing structural alterations. Id. at 13. Resting its decision in part on Wakefern and Port Authority, the court found that the ammonia release "physically transformed the air within the [packaging] facility so that it contained an unsafe amount of ammonia or that the ammonia levels rendered the facility unfit for occupancy until the ammonia could be dissipated." Id. at 16. And, significantly, the court concluded that the ammonia discharge inflicted "direct physical loss of or damage to" the packaging facility. Id. at 17. This fully supports plaintiff's position here.

Accordingly, the court concludes that the term "direct physical damage" in the carriers' policies in this case could support either plaintiff's or defendants' positions of what constitutes a direct physical loss; in other words, it is ambiguous. The carriers could have defined the term physical damage but declined to do so. Id. at 20-21. Consequently, construing the language against the insurance carriers and in favor of the insured as is required under New Jersey law, see, inter alia, Flomerfelt, 202 N.J. at 441, the court concludes that plaintiff has sufficiently pleaded a cause of action as to the insuring agreements entitling plaintiff to coverage for COVID-19 damages.

The Pollution Exclusion

In that the court has concluded that the COVID-19 infiltration satisfies the insuring agreement of direct physical loss or damage caused by a covered cause of loss, the court now turns to exclusionary language in the policies. The four policies contain language that the carriers claim

excludes a virus, such as COVID-19, from coverage, regardless of how the insuring agreement is construed. No doubt, however, that the insurer has the burden to prove the applicability of the exclusion. Flomerfelt, 202 N.J. at 442.

In the Zurich and AIG policies, a contaminant is defined to include:

> Any solid, liquid, gaseous, thermal, or other irritant, pollutant, or contaminant, including but not limited to smoke, vapor, soot, fumes, acids, alkalis, chemicals, waste including material to be recycled, reconditioned, or reclaimed, asbestos, ammonia, or hazardous substances, **Fungus** or **Spores**.

It is of note that this latter section, which listed contaminants, does not include viruses. Virus is, however, included in the policy provision that is headed Contamination (Contaminated). That definition reads as follows:

> Any condition of property due to the actual presence of any foreign substance, impurity, pollutant, hazardous material, poison, toxin, pathogen or pathogenic organism, bacteria, virus, disease causing or illness causing agent, **Fungus**, mold or mildew.

The Interstate and National Fire policies have exclusion sections referred to in each as the Pollution Contamination Exclusion. They are substantially the same in each policy and read as follows:

> There will be no payment for "loss, damage, cost or expense caused directly or indirectly by . . . the release, migration, discharge, escape or dispersal of Contaminants . . . Contaminants means materials that may be harmful to human health, and include any impurity, pollutant, poison, toxin, pathogen or pathogenic organism, disease-causing or illness-causing agent, asbestos, dioxin, polychlorinated biphenyls, agricultural smoke, agricultural soot, vapor, fumes, acids, alkalis, bacteria, virus, and hazardous substances listed in the Federal Water Pollution control Act, Clean Air Act, Resource Conservation and Recovery Act of 1976, Toxic Substances Control Act, or as designated by the United States Environmental Protection Agency or any other local governmental agency . . . .

These types of exclusion clauses were addressed in depth by the New Jersey Supreme Court in Nav-Its, Inc. v. Selective Ins. Co. of America, 183 N.J. 110 (2005). In Nav-Its, the insured brought a claim against a commercial liability insurer for declaratory judgment, seeking indemnity

in a lawsuit arising out of exposure to fumes from a floor coating sealant. Id. at 113. The policy contained a pollution exclusion endorsement, which defined pollutants as "any solid, liquid, gaseous or thermal irritant or contaminant, including smoke, vapor, soot, fumes, acids, alkalis, chemicals and waste." Id. at 115.

The policy also defined "Pollution Hazard" to mean an "actual exposure or threat of exposure to the corrosive, toxic or other harmful properties of any pollutants arriving out of the discharge, disposal, seepage, migration, release or escape of such pollutants." Ibid. The issue arose as to whether these exclusions were applicable, in that the exclusions are generally applied only to traditional environmental pollution claims. Id. at 113-14. The Appellate Division found that the pollution exclusion clauses were not necessarily limited to the cleanup of traditional environmental damage. Id. at 114. The New Jersey Supreme Court reversed. Id. at 127.

The Court characterized the issue as follows: "The central question presented in this case is whether we should limit the applicability of the pollution exclusion clause to traditional environmental pollution claims." Id. at 118. The answer was yes. Id. at 126. The Court observed that important to its analysis was the principle that "exclusions in the insurance policy should be narrowly construed." Id. at 119. In evaluating claims of coverage for environmental pollution, the Court was guided by Morton International, Inc., v. General Accident Ins. Co. of America, 134 N.J. 1 (1993). Id. at 119. The Nav-Its Court concluded, "applying the doctrine of reasonable expectations, . . . the common understanding of state regulators was that the 'overriding purpose [of the pollution clause] was to deny coverage to intentional polluters.'" Id. at 121, quoting Morton, 134 N.J. at 77. The Court said that the evidence suggested strongly that the pollution exclusion "was designed to serve the twin purposes of eliminating coverage for gradual environmental degradation, and government-mandated cleanup such as superfund response cost

reimbursement. Nav-Its, 183 N.J. at 122-23. Neither purpose is served by the pollution exclusions in this case.

The Court subsequently found that the purpose of the pollution exclusion clause in "various forms" was "to have a broad exclusion for traditional environmentally related damages." Id. at 123. The Court noted that if read literally, the exclusion "would require its application to all instances of injury or damage to persons or property caused by 'any pollutants arising out of the discharge, dispersal, seepage, migration, release or escape of . . . any solid, liquid, gaseous, or thermal irritant or contaminant, including smoke, vapor, soot, fumes, acids, alkalis, chemicals and waste.'" Id. at 123. Accepting such an interpretation of the pollution exclusion would essentially exclude all pollution hazards except those falling within a limited exception within the selected policy. Ibid. The Court consequently rejected the insurer's interpretation, finding the exclusions overly broad, unfair, and contrary to the objectively reasonable expectations of the New Jersey and other state regulatory authorities that were presented with an opportunity to disapprove the clause. Id. at 123-24, citing Morton, 134 N.J. at 30.

Significantly, the Court observed that it was the insurer's obligation to come forth with compelling evidence that the pollution exclusion clause in the subject case was approved by the Department of Insurance as intended to be read as broadly as the insurance company urged. Id. at 123. And the Court received no such compelling evidence to support that position. Ibid. Nor has this court.

The Appellate Division, in Birch v. Hanover Ins. Co., Docket No. A-2490, 221 N.J. Super, Unpub. Lexis 453, (App. Div. March 19, 2021), is also instructive. The case involved insurance coverage for a home inspection company policy. Id. at 1-2. The home inspector did not raise any problems with the propane tanks' connection to the house's hot water heater in his report. Id. at 1.

The homeowners purchased the house, hired a vendor to replace the propane tank, and the replacement tank subsequently exploded through a leaky valve. Ibid.

The homeowners sought coverage under their policy with Hanover, which contained an exclusion for claims "arising out of or based upon . . . flammable materials." Ibid. Hanover argued that the policy did not cover the property damage claim as it excluded coverage for escape of a "pollutant." Id. at 12.

In addressing the particular exclusion of damages caused by pollutants, the Appellate Division agreed with the plaintiffs that the exclusionary provisions in the professional liability policy did not pertain. Id. at 13. Citing to Nav-Its, the appellate court stated: "The scope of the pollution exclusion should be limited to injury or property damage arising from activity commonly thought of as traditional environmental pollution," thus reflecting "the exclusion's historical objective-avoidance of liability for environmental catastrophe related to intentional industrial pollution." Id. at 13-14.

The same scrutiny is warranted here. In the Zurich and AIG policies, contaminants include: "Any solid, liquid, gaseous, thermal, or other irritant, pollutant, or contaminant, including but not limited to smoke, vapor, soot, fumes, acids, alkalis, chemicals, waste including material to be recycled, reconditioned, or reclaimed, asbestos, ammonia, other hazardous substances, **Fungus** or **Spores**." Contamination includes: "Any condition of property due to the actual presence of any foreign substance, impurity, pollutant, hazardous material, poison, toxin, pathogen or pathogenic organism, bacteria, virus, disease causing or illness causing agent, **Fungus**, mold or mildew." For the most part the contaminants are associated with traditional environmental pollution damages, not reasonably related to the damages in this case, which are derived from a communicable disease.

The Interstate Fire and National Fire pollution exclusion provisions state: "There will be no payment for "loss, damage, cost or expense caused directly or indirectly by . . . the release, migration, discharge, escape or dispersal of Contaminants . . . Contaminants means materials that may be harmful to human health, and include any impurity, pollutant, poison, toxin, pathogen or pathogenic organism, disease-causing or illness-causing agent, asbestos, dioxin, polychlorinated biphenyls, agricultural smoke, agricultural soot, vapor, fumes, acids, alkalis, bacteria, virus, and hazardous substances listed in the Federal Water Pollution control Act, Clean Air Act, Resource Conservation and Recovery Act of 1976, Toxic Substances Control Act, or as designated by the United States Environmental Protection Agency or any other local governmental agency." This provision overwhelmingly refers to environmental and industrial pollution contaminants.

Applying an analysis like that articulated by Justice Wallace in Nav-Its, 183 N.J. at 123, these pollution exclusions are overly broad, unfair, and are without doubt contrary to objectively reasonable expectations of the insured. Inserting the term "virus" in the section defining contamination does not change the substance of the exemption. When read as a whole, the exclusion remains applicable to more traditional environmental-related damages and as such will not fulfill the insured's reasonable expectations. The insurers, who have the burden to do so, have not presented the court with compelling evidence to show that the pollution exclusion clause in the present case should be construed as broadly as the insurers suggest.

A similar result was reached in JDG Vegas Retail v. Starr Surplus Lines, 2020 Nev. Dist. Lexis 1512, (Eighth Judicial District of the Court of Nevada, Clarke County, Nov. 30, 2020). In JDG, the court was faced with the same issues that are present here. The court was caused to decide whether the pollutant or contaminate exemption in its property insurance policy, which was similar, though not identical, to the exclusions claimed here, was applicable to preclude coverage

for direct physical loss of its property for loss of business as a result of the coronavirus. Id. at 3. And as is the case here, the word "virus, was added to what was otherwise language that the court attributed to pollution caused by traditional environmental and industrial pollution. Id. at 9. The court found that the defense had not demonstrated it would be unreasonable to interpret the pollution and contamination exclusion to apply only to instances of traditional environmental and industrial pollution. Accordingly, the court found that the pollution and contamination exclusion would not exclude the plaintiff's claims. Id. at 11.

New Jersey has a strong public policy that insurance policy coverage provisions are to be read broadly, and exclusions are to be read narrowly. Sosa, 458 N.J. Super at 647. Consistent with that public policy, it is not unreasonable to conclude that pollution exclusions in an all-risk policy that are substantially directed at traditional environmental and industrial damages do not pertain to damages for a virus such as COVID-19, which damages are the result of naturally occurring communicable diseases. Accordingly, the pollution exclusions in this case may not be used to preclude coverage.

That said, one more issue remains to be addressed: whether the National Fire Insurance Biological or Chemical Substance Exclusion bars coverage under that policy. The court finds that it does. The exclusion reads as follows:

> This policy does not provide any coverage for any loss, cost, expense or damage of any nature, however caused, directly or indirectly arising out of, resulting from, or in any way related to the actual or suspected presence or threat of any pathogenic or poisonous biological or chemical substance or material of any kind, including but not limited to, any malicious use of such substance or material, whether isolated or widespread, regardless of any other cause or events contributing at that same time or in any sequence.

This exclusion applies to damages directly or indirectly arising out of, resulting from, or in any way related to actual or suspected presence "of any pathogenic or poisonous biological or

chemical substance, . . . including, but not limited to, any malicious use of such substance." The exclusion is clear and unambiguous. The endorsement, in bold print, indicates that it "changes the policy."

COVID-19 falls within the category of pathogens covered by the endorsement. Pathogenic and biological substances include COVID-19. See 42 USCS 262, Regulation of Biological Products, Subsection (I)(1), (the term biological product includes a virus); Attorney's Dictionary of Medicine, 55d ed. 2021, defining pathogen as to include any microorganism (bacterium) capable of causing disease; the Interim Laboratory Biosafety Guideline for handling and processing specimens associated with Coronavirus disease 2019 (COVID-19) issued by the CDC (updated December 13, 2021) notes, as a key point, that suspected and confirmed SARS-CoV-2 positive clinical specimens, cultures, or isolates should be packed and shipped as [a] Biological Substance.

Counsel for Ocean suggested that this endorsement is to protect the casino against terrorism. Perhaps it could be viewed in that respect. But that would not affect its application to the COVID-19 virus. In all respects the clear focus of this endorsement is on pathogenic contaminants, such as COVID-19. And given that the National Fire's BH-1 endorsement is specifically directed to war risk and terrorism, the reasonable expectations of the insured would be consistent with an understanding that this pathogenic/biological endorsement affects pathogens, not terrorism.

Nor does the subject endorsement contain the language, as that previously discussed, which is derived from environmental or industrial pollution. The language substantially mirrors a virus such as COVID-19. Consequently, the court concludes that the endorsement precludes coverage under the National Fire policy.

Conclusion

In sum, the court denies the R. 4:6-2(e) motion for dismissal of the complaint by American Guarantee and Liability Insurance Company (Zurich policy), AIG Specialty Insurance Company, and Interstate Fire and Casualty Company. The court grants the motion by National Fire and Marine Insurance Company because of the Biological or Chemical Substances Exclusion endorsement and dismisses the complaint as to that carrier.