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California Supreme Court Holds That COVID-19 Does Not Create "Direct Physical Loss Or Damage" To Insured Property

Client Alert | May 23, 2024

***Another Planet Ent., LLC v. Vigilant Ins. Co.*, No. S277893** – Decided May 23, 2024

The California Supreme Court held today that commercial property insurance policies that pay for "direct physical loss or damage to property" do not apply to losses resulting from the alleged presence of the coronavirus.

> *"We conclude, consistent with the vast majority of courts nationwide, that allegations of the actual or potential presence of COVID-19 on an insured's premises do not, without more, establish direct physical loss or damage to property within the meaning of a commercial property insurance policy."*

Chief Justice Guerrero writing for the Court

Background:

Most commercial property insurance policies in California insure against the risk of "direct physical loss or damage to property." Following the COVID-19 pandemic, many businesses sought to recover under such policies, claiming losses from the virus and resulting government closure orders. Another Planet, a concert production company with venues across Northern California, was one such business. It claimed that viruses like COVID-19 cause "direct physical damage" when they are present in properties and airspaces and can cause "direct physical loss" to property when they make spaces unfit for their intended use.

As Another Planet recognized in claiming coverage, state and federal appellate courts across the country have overwhelmingly rejected the claim that COVID-19 causes physical loss of or damage to a property. But Another Planet maintained that California insurance policies should be construed more broadly. After briefing and argument, the U.S. Court of Appeals for the Ninth Circuit certified the issue to the California Supreme Court for resolution. The California Supreme Court accepted certification to resolve the issue.

Certified Question:

Can the actual or potential presence of the COVID-19 virus on an insured's premises constitute "direct physical loss or damage to property" for purposes of coverage under a commercial property insurance policy?

Court's Holding:

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No: The COVID-19 virus does not affect the physical characteristics of covered properties, and the fact that a property cannot be used as it was intended does not establish any covered loss.

What It Means:

- The opinion is a significant win for insurers, which have faced a substantial number of claims since the onset of the COVID-19 pandemic. The Court embraced the reasoning of most appellate decisions nationwide and resolved a split that had developed among the California Courts of Appeal on the issue.
- The opinion clarifies that insurance policies covering "direct physical loss or damage to property" require that "the property itself must have been physically harmed or impaired." COVID-19 does not satisfy that requirement because it does not produce any "distinct, demonstrable, physical change" that "result[s] in some injury to or impairment of the property as property."
- The opinion also clarifies that restrictions on the use of property—including those resulting from public health orders issued by the government—likewise do not implicate coverage because they do not constitute "direct physical loss or damage" to the property itself.
- The same analysis applies to physical alterations made "to minimize virus transmission and safely operate": those alterations are preventative and cannot supply the necessary direct physical damage or loss to property.
- The Court distinguished the COVID-19 virus from other invisible or biological substances that become "so connected to the property that the property effectively becomes the source of its own loss or damage"—for instance, when a contaminant damages property and cannot "be easily cleaned or removed."

The Court's opinion is available here.

Gibson Dunn's lawyers are available to assist in addressing any questions you may have regarding developments at the California Supreme Court. Please feel free to contact the following practice group leaders:

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