

IN THE SUPREME COURT OF THE STATE OF NEVADA

STARR SURPLUS LINES
INSURANCE CO.,

Petitioner,

vs.

THE EIGHTH JUDICIAL DISTRICT
COURT OF THE STATE OF
NEVADA in and for the County of
Clark and THE HONORABLE MARK
DENTON, District Judge,

Respondents,

and

JGB VEGAS RETAIL LESSEE, LLC,

Real Party in Interest.

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Case No.: 84986

Eighth Judicial District Court
Case No.: A-20-816628-B

**REAL PARTY IN INTEREST'S (1) NOTICE OF SUPPLEMENTAL
AUTHORITIES IN SUPPORT OF ITS ANSWER TO PETITION FOR
WRIT OF MANDAMUS OR, IN THE ALTERNATIVE, PROHIBITION,
AND (2) RESPONSE TO PETITIONER'S NOTICE OF
SUPPLEMENTAL AUTHORITIES**

ROBERT L. EISENBERG, ESQ., Nevada Bar No. 0950
LEMONS, GRUNDY & EISENBERG
6005 Plumas Street, Third Floor
Reno, Nevada 89519

Attorney for Real Party in Interest

Pursuant to NRAP 31(e), Real Party in Interest JGB Vegas Retail Lessee, LLC (“JGB”) respectfully submits this Notice of Supplemental Authorities to bring to the Court’s attention two recent decisions issued after the close of briefing, styled *Shusha, Inc. v. Century-National Insurance Company*, 2022 WL 18110247 (Cal. Ct. App. Dec. 14, 2022) (*publication request granted* Jan. 5, 2023), and *Another Planet Entertainment, LLC v. Vigilant Insurance Company*, 2022 WL 17972557, at *9 (9th Cir. Dec. 28, 2022). JGB also hereby submits its Response to Petitioner Starr Surplus Lines Insurance Co.’s (“Starr”) Notice of Supplemental Authorities, filed January 3, 2023 (“Starr Notice”), as allowed by NRAP 31(e).

I. JGB’S NOTICE OF SUPPLEMENTAL AUTHORITIES

As set forth in JGB’s Answer, the phrase “direct physical loss or damage” in an “all-risks” property insurance policy provides coverage “when a deadly physical substance like SARS-CoV-2/COVID-19 either (1) is present on or around covered property, rendering it partially or wholly unusable, unsafe or unfit for its intended purpose (‘physical loss’) *or* (2) alters the surfaces or air of covered property (‘physical damage’).” *See* JGB’s Answer at 1, 13-17. Petitioner argues to the contrary, purporting to rely in part on California caselaw. *See* Starr’s Petition at 13-21. Two recent decisions summarize the current state of California law as to the meaning of “direct physical loss or damage.”

A. *Shusha Inc. v. Century-National Ins. Co.*

Shusha stands for the legal proposition that a policyholder “unquestionably plead[s] direct physical loss or damage to covered property” by alleging that SARS-CoV-2 and/or COVID-19 was present on and around insured property, rendering the property “dangerous and unusable for [its] intended purposes,” resulting in business income losses. 2022 WL 18110247, at *6, *8-9 (attached as Exhibit A). *Shusha* reaffirmed *Marina Pacific Hotel & Suites, LLC v. Fireman's Fund Ins. Co.*, 296 Cal. Rptr. 3d 777 (Ct. App. 2022).¹ The Court also clarified that *Marina Pacific* and *Shusha* are wholesale rejections of—not merely “narrow, limited departure[s]” from—*United Talent Agency v. Vigilant Ins. Co.*, 293 Cal. Rptr. 3d 65 (Ct. App. 2022), which held COVID-19 cannot cause physical loss or damage to property as a matter of law. *Id.* at *7-9.

Shusha also distinguished *Inns-by-the-Sea v. California Mutual Insurance Company*, 286 Cal. Rptr. 3d 576 (Ct. App. 2021)—a case which Starr cites repeatedly²—holding that *Inns* “involved only allegations of loss of use of the insured property as a result of government-ordered closures to limit the spread of COVID-19.” *Id.* at *6. In contrast, just like JGB, the *Shusha* policyholder

¹ JGB cites *Marina Pacific* throughout its answering brief. See Answer at 4, 20, 24, 30.

² See Petition at 13-14, 16, 21; Reply at 13-14, 16-17.

“expressly alleged [that] the presence of the virus on the insured premises[:]” (1) rendered property and surfaces “dangerous and unusable for their intended purposes;” and (2) “caused physical damage to covered property,” both of which “in turn led to business losses.” *Id.* at *6 & n.6.

The policy at issue in *Shusha* is nearly identical in relevant part to JGB’s policy (providing coverage for “direct physical loss of or damage to property”). Like JGB, the plaintiff in *Shusha* alleged business interruption losses resulting from direct physical loss or damage caused by the actual presence of COVID-19 at their respective insured properties. Further, the defendant insurer in *Shusha* advanced virtually identical arguments to what Starr does here. Thus, like *Shusha*, JGB respectfully submits that this Court should hold direct physical loss or damage occurs, *inter alia*, where the presence of SARS-CoV-2 and/or COVID-19 on and around insured property renders the property “dangerous and unusable for [its] intended purposes,” resulting in business income losses.

B. Another Planet Entertainment, LLC v. Vigilant Ins. Co.

On December 28, 2022, the United States Court of Appeals for the Ninth Circuit certified the following question to the California Supreme Court regarding a COVID-19 business interruption insurance dispute similar to JGB’s:

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?

Another Planet, 2022 WL 17972557, at *3 (attached as Exhibit B). Thus, *Another Planet* stands for the proposition that, as the Ninth Circuit now recognizes, the meaning of the phrase “direct physical loss or damage to property” is an open and disputed question under California law.

Notably, and in contrast, Starr’s Petition cites early COVID-19 coverage decisions out of the Ninth Circuit which had simply assumed that the California Supreme Court would hold SARS-CoV-2/COVID-19 could not cause physical loss or damage as a matter of law.³ The Ninth Circuit relied on its own decisions which *predicted California law* as its basis to then dismiss COVID-19 insurance coverage cases *under Nevada law*, and refused to seek this Court’s guidance regarding the meaning of the phrase “physical loss or damage” in all-risks policies.⁴ At least two of these Ninth Circuit decisions purporting to declare Nevada law based on

³ Starr relies heavily on California state and federal case law in its briefing, including the *Another Planet* federal district court decision preceding the Ninth Circuit’s certified question. See Petition at 13-14, 16-17, 19-21, 23-24; Reply at 10, 13-17, 20.

⁴ See *Circus Circus LV, LP v. AIG Specialty Ins. Co.*, 2022 WL 1125663, at *2 & n.2 (9th Cir. Apr. 15, 2022) (citing *Mudpie, Inc. v. Travelers Cas. Ins. Co. of Am.*, 15 F.4th 885 (9th Cir. 2021) (predicting California law) to reject coverage under Nevada law and “deny[ing] Circus Circus’s request that we certify two questions to the Nevada Supreme Court as unnecessary”); *Levy Ad Group, Inc. v. Fed. Ins. Co.*, 2022 WL 816927, at *1 (9th Cir. Mar. 17, 2022) (citing *Mudpie* and opining “there is no reason to think a Nevada court would interpret the contract language differently”).

predictions of California law (*Circus Circus* and *Levy Ad*) feature prominently in Starr's Petition.⁵

Multiple California Court of Appeal decisions, including *Marina Pacific* and *Shusha*, have now rejected or distinguished these early Ninth Circuit decisions, and instead held that a policyholder with allegations similar to JGB's properly alleges physical loss or damage to property and business interruption losses caused by SARS-CoV-2/COVID-19.⁶ As a result, the Ninth Circuit has now acknowledged that its earlier predictions regarding California law may have been premature or misplaced, and invited the California Supreme Court to provide its pronouncement of California law.

JGB respectfully submits that the Court should consider these other rulings, all involving, in pertinent part, similar or nearly identical policy language at issue in this matter.

⁵ See Petition at 13, 20, 22 (relying principally on *Levy Ad* and *Circus Circus* as pronouncements of Nevada law); Reply at 18-19, 27 (same). Starr also relies on *Project Lion LLC v. Badger Mut. Ins. Co.*, 2021 WL 2389885, at *2 (D. Nev. May 19, 2021), which in turn relies on the Ninth Circuit's pronouncement of California law in *Mudpie* and other California federal district courts as its basis to interpret Nevada law. See Petition at 13, 19-20.

⁶ See, e.g., *Shusha*, 2022 WL 18110247, at *5-*7 (citing *Marina Pacific* and distinguishing *Mudpie*).

II. RESPONSE TO STARR'S NOTICE

Starr's Notice advises the Court of two out-of-state rulings: (1) *Neuro-Communication Services, Inc. v. Cincinnati Insurance Co.*, 2022 WL 17573883 (Ohio Dec. 12, 2022); and (2) *Tapestry, Inc. v. Factory Mut. Ins. Co.*, (Misc. No. 1) 2022 WL 17685594 (Md. Dec. 15, 2022). Like nearly all of the cases Starr cited in its briefing, the policyholders in *Neuro-Communication Services* and *Tapestry* failed to allege either that SARS-CoV-2 was present on and rendered insured property unusable for its intended purpose, or that SARS-CoV-2 physically altered and damaged insured property. *See* Answer at 25-26 (explaining the same defect in nearly all of Starr's cited cases). Thus, *Neuro-Communication Services* and *Tapestry* should not be instructive here.

Specifically, the policyholder in *Neuro-Communication Services*, unlike JGB, did **not** allege that on-site SARS-CoV-2 rendered its property dangerous and unusable for its intended purpose, nor that the virus physically attached to and damaged its property. Rather, the policyholder only claimed lost income due to governmental orders limiting its operations. *See* 2022 WL 17573883, at *2-3. And though Starr points to *Neuro-Communication Services*' interpretation of the phrase "direct physical loss or damage to property," that "language does not appear in the policy" at issue there. *Id.* at *3 (acknowledging that the certified question asked the court to answer "three factual scenarios [concerning] 'direct physical loss or

damage” even though the policy at issue did not contain that phrase).⁷ The *Neuro-Communication Services* policy is further distinguished from the Starr policy at issue, as that policy *defined* loss as “accidental physical loss or accidental physical damage.” *Id.* As JGB explained in its briefing, JGB’s policy contains no such definition. Answer at 2 (“The Policy covers ‘all risks of direct physical loss or damage,’ but does not define these terms.”).

As to *Tapestry*, the Court there expressly did *not* rule on the question Starr put before this Court: whether SARS-CoV-2/COVID-19 did or could cause physical loss or damage. *See* 2022 WL 17685594, at *12 (“[W]e decide today neither that Coronavirus does not, nor that it cannot, cause “physical loss or damage” as that phrase is used in the Policies.”). Moreover, this Court previously has diverged from the Maryland Supreme Court on significant insurance coverage interpretive issues. *Compare Jackson v. State Farm Fire & Cas. Co.*, 108 Nev. 504, 507-08, 835 P.2d 786, 789 (1992) (insurance coverage case involving general liability policies and applying the manifestation rule as the trigger of coverage), *with Maryland Cas. Co. v. Lloyd E. Mitchell*, 595 A.2d 469, 478 (Md. 1991) (instead applying the injury-in-fact trigger). *Tapestry* is distinguishable and should not be followed.

⁷ Instead, the policy in *Neuro-Communication Services* covered “direct ‘loss’ to Covered Property at the ‘premises’ caused by or resulting from any Covered Cause of Loss.” *Id.* “‘Covered Causes of Loss’ is defined [in the policy] as direct ‘loss’ unless the ‘loss’ is excluded or limited in that part of the policy.” *Id.*

JGB respectfully submits that this Court adhere to long-standing principles of Nevada law and define the phrase “physical loss or damage” in favor of coverage and thereby uphold JGB’s reasonable expectations.

Dated this 17th day of January, 2023.

LEMONS, GRUNDY & EISENBERG

By: Robert L. Eisenberg

ROBERT L. EISENBERG, ESQ., Nevada Bar No. 0950

rle@lge.net

6005 Plumas Street, Third Floor

Reno, Nevada 89519

(775) 786-6868 / Fax: (775) 786-9716

Attorney for Real Party in Interest

CERTIFICATE OF SERVICE

I certify that on January 17, 2023, I submitted the foregoing “Real Party In Interest’s Notice of Supplemental Authorities and Response to Petitioner’s Notice of Supplemental Authorities” for filing via the Court’s eflex electronic filing system.

Electronic notification will be sent to the following:

**LEWIS ROCA ROTHGERBER
CHRISTIE LLP**

Daniel F. Polsenberg
Joel D. Henriod
Abraham G. Smith
3993 Howard Hughes Parkway,
Suite 600
Las Vegas, Nevada 89169

CLYDE & CO US LLP

Lee H. Gorlin
Amy M. Samberg
7251 W. Lake Mead Boulevard,
Suite 430
Las Vegas, Nevada 89128

Attorneys for Petitioner

I further certify that I served a copy of this document by emailing a true and correct copy thereof, as follows:

The Honorable Mark Denton
DISTRICT COURT JUDGE – DEPT. 13
200 Lewis Avenue
Las Vegas, Nevada 89155
Dept13LC@ClarkCountyCourts.us

Respondent

By: /s/ Margie Nevin
Margie Nevin

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EXHIBIT A

Shusha v. Century-National Ins. Co., 2022 WL 18110247

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Shusha v. Century-National Ins. Co., 2022 WL 18110247

2022 WL 18110247

Only the Westlaw citation is currently available.
Court of Appeal, Second District, Division 7, California.

SHUSHA, INC., Plaintiff and Appellant,

v.

CENTURY-NATIONAL INSURANCE
COMPANY, Defendant and Respondent.

B313907

I

Filed December 14, 2022

Synopsis

Background: Restaurant brought action against insurer under “commercial package” insurance policy, alleging claims for breach of contract, bad faith, and violation of the unfair competition law after insurer denied coverage for lost business income as a result of the COVID-19 pandemic. The Superior Court, Los Angeles County, No. 20STCV25769, Daniel J. Buckley, J., sustained insurer's demurrer without leave to amend, and restaurant appealed.

Holdings: The Court of Appeal, Feuer, J., held that:

[1] restaurant sufficiently pleaded direct physical loss or damage to its property caused by the COVID-19 virus to trigger coverage, and

[2] restaurant adequately alleged causes of action for bad faith and violation of the unfair competition law.

Reversed and remanded.

Procedural Posture(s): On Appeal; Demurrer to Complaint.

West Headnotes (16)

[1] Appeal and Error

In reviewing an order sustaining a demurrer, Court of Appeal examines the operative complaint de novo to determine whether it alleges facts sufficient to state a cause of action under any legal theory.

[2] Appeal and Error

When evaluating a complaint, Court of Appeal reviewing an order sustaining a demurrer assumes the truth of the allegations.

[3] Appeal and Error

Court of Appeal is not required to accept the truth of the factual or legal conclusions pleaded in the complaint when reviewing an order sustaining a demurrer.

[4] Insurance

In general, interpretation of an insurance policy is a question of law that is decided under settled rules of contract interpretation.

[5] Insurance

Goal in construing insurance contracts, as with contracts generally, is to give effect to the parties' mutual intentions.

[6] Insurance

If contractual language of an insurance policy is clear and explicit, it governs, and if the insurance policy terms are ambiguous, i.e., susceptible of more than one reasonable interpretation, the court interprets them to protect the objectively reasonable expectations of the insured; only if these rules do not resolve a claimed ambiguity does the court resort to the rule that ambiguities are to be resolved against the insurer.

[7] Insurance

To ensure that coverage conforms fully to the objectively reasonable expectations of the insured, in cases of ambiguity, basic coverage provisions are construed broadly in favor of affording protection, but clauses setting forth specific exclusions from coverage are interpreted narrowly against the insurer.

[8] Insurance ☞

Insured has burden of establishing that claim, unless specifically excluded, is within basic coverage, while insurer has burden of establishing that specific exclusion applies.

[9] Insurance ☞

Restaurant sufficiently pleaded direct physical loss or damage to its property caused by the COVID-19 virus to trigger coverage under commercial package insurance policy, which included commercial property insurance and general liability coverage; complaint alleged the virus was certain to have been present at restaurant at various times, including "in the form of virus matter present on walls, floors, tables, chairs, silverware, dishes, and other surfaces," that routine cleaning was insufficient to eliminate virus, and thus that the presence of droplets containing the virus led to restaurant closure and constituted covered physical damage to the premises and that restaurant lost business revenues and incurred substantial costs to mitigate the damage by reconfiguring its property and increasing its sanitization procedures.

[10] Contracts ☞

Elements of cause of action for breach of contract are (1) existence of contract, (2) plaintiff's performance or excuse for nonperformance, (3) defendant's breach, and (4) resulting damages to plaintiff.

[11] Insurance ☞

In a claim against an insurance carrier, there are at least two separate requirements to establish breach of the implied covenant of good faith and fair dealing: (1) benefits due under the policy must have been withheld; and (2) the reason for withholding benefits must have been unreasonable or without proper cause.

[12] Insurance ☞

An insurer denying or delaying the payment of policy benefits due to the existence of a genuine dispute with its insured as to the existence of coverage liability or the amount of the insured's coverage claim is not liable in bad faith even though it might be liable for breach of contract.

[13] Insurance ☞

Genuine dispute rule, precluding a finding of bad faith, does not relieve an insurer from its obligation to thoroughly and fairly investigate, process and evaluate the insured's claim.

[14] Insurance ☞

A genuine dispute, precluding a bad faith claim, exists only where the insurer's position is maintained in good faith and on reasonable grounds.

[15] Insurance ☞

The reasonableness of an insurer's claims-handling conduct is ordinarily a question of fact in a bad faith action, but becomes a question of law where the evidence is undisputed and only one reasonable inference can be drawn from the evidence.

[16] Insurance ☞

Restaurant adequately alleged causes of action for bad faith and violation of the unfair competition law, based on insurer's summary denial of restaurant's claim for coverage under commercial package insurance policy, which included commercial property insurance and general liability coverage, arising out COVID-19 pandemic, to survive demurrer; insurer's denial of coverage came just three weeks after restaurant tendered its claim and in the earliest days of the understanding of the novel COVID-19 virus, it was settled law

that environmental contamination that resulted in physical damage could trigger business income coverage, restaurant alleged COVID-19 was present and physically damaged its restaurant, and insurer allegedly did not take any steps to determine whether COVID-19 caused physical damage to the premises before denying coverage. Cal. Bus. & Prof. Code § 17200 et seq.

APPEAL from a judgment of the Superior Court of Los Angeles County, Daniel J. Buckley, Judge. Reversed. (Los Angeles County Super. Ct. No. 20STCV25769)

Attorneys and Law Firms

Hecht Partners, Katheryn Lee Boyd, Kristen L. Nelson, Los Angeles; Law Offices of Jonathan A. Sorkowitz and Jonathan A. Sorkowitz for Plaintiff and Appellant.

Berman Berman Berman Schneider & Lowary, Spencer A. Schneider and Karen E. Adelman, Los Angeles, for Defendant and Respondent.

Opinion

FEUER, J.

*1 Shusha, Inc., dba La Cava (La Cava) appeals from the judgment of dismissal entered after the trial court sustained without leave to amend the demurrer filed by Century-National Insurance Company (Century-National) to La Cava's first amended complaint. La Cava sued Century-National for breach of an insurance contract and related claims after Century-National denied coverage for La Cava's lost business income as a result of its suspension of restaurant operations in March 2020 due to the COVID-19¹ pandemic and associated government shutdowns.

¹ For ease of reference, we refer, as do the parties, to the SARS-CoV-2 virus, its variants, and the coronavirus disease caused by them as COVID-19.

On appeal, La Cava contends the trial court erred in concluding the alleged presence of the COVID-19 virus in its restaurant did not constitute “direct physical loss of or damage to” the restaurant necessary for coverage under the terms of the policy at issue. La Cava also argues Century-National acted in bad faith by summarily denying coverage without

investigating La Cava's claim. We agree La Cava's allegations that contamination by the COVID-19 virus physically altered its restaurant premises were sufficient to withstand demurrer, and we reverse.

FACTUAL AND PROCEDURAL BACKGROUND

A. The Century-National Insurance Policy

As alleged in the operative first amended complaint (complaint), La Cava purchased from Century-National a “commercial package” insurance policy, including commercial property insurance and general liability coverage for a one-year period beginning November 22, 2019 (the policy). A copy of the policy was attached to the complaint.

Section A.1 of the “Business Income (and Extra Expense) Coverage Form” provided in relevant part, “We will pay for the actual loss of business income you sustain due to the necessary ‘suspension’ of your ‘operations’ during the ‘period of restoration’.” The ‘suspension’ must be caused by *direct physical loss of or damage to property* at premises which are described in the declarations and for which a business income limit of insurance is shown in the declarations” (Capitalization omitted and italics added.) “Suspension” was defined to mean, in pertinent part, “[t]he slowdown or cessation of your business activities.” The “period of restoration” was defined in part as the period that “begins with the date of direct physical loss or damage caused by or resulting from any covered cause of loss at the described premises” and ends on the earlier of “the date when the property at the described premises should be repaired, rebuilt or replaced with reasonable speed and similar quality” or “one year immediately following the date of direct physical loss or damage caused by a covered cause of loss.” (Capitalization omitted.)

Section A.5.a of the business income coverage form also included civil authority coverage. This provision provided, “We will pay for the actual loss of business income you sustain and necessary extra expense caused by action of civil authority that prohibits access to the described premises *due to direct physical loss of or damage to property, other than at the described premises*, caused by or resulting from any covered cause of loss.” (Capitalization omitted and italics added.)

B. The Complaint

*2 La Cava filed this action on July 7, 2020. The first amended complaint alleged causes of action for declaratory judgment, breach of contract, breach of the implied covenant of good faith and fair dealing, and unfair business practices in violation of the Unfair Competition Law (UCL; Bus. & Prof. Code, § 17200 et seq.). Each cause of action was premised on Century-National's denial of coverage for business income losses claimed by La Cava as a result of the COVID-19 pandemic.

La Cava is a restaurant in the Sherman Oaks neighborhood of Los Angeles. As alleged, La Cava "promptly shut down operations" on or around March 16, 2020, "[o]nce the La Cava management was made aware by [pandemic-related government orders] of the clear and present danger of the virus and its existence everywhere in LA County, including on the surfaces and in the air in and around La Cava's premises." On April 1, 2020 La Cava reopened with limited hours for take-out and delivery only, "prohibiting customers from dining in."

The complaint described and attached several government orders relating to the pandemic. On March 4, 2020 the Governor of California declared a state of emergency due to the rapid spread of COVID-19 in California, and on March 15 the Mayor of Los Angeles issued a public health order prohibiting restaurants in the city from serving food on their premises. On March 19 the Governor issued Executive Order No. N-33-20 requiring residents of California to stay in their homes, with limited exceptions. Also on March 19, the Mayor issued a "Safer at Home" public order, finding "the COVID-19 virus can spread easily from person to person and it is physically causing property loss or damage due to its tendency to attach to surfaces for prolonged periods of time." (Capitalization omitted.) The Mayor's order provided restaurants could offer food to customers "but only via delivery service, to be picked up, or drive-thru." In May, restaurants were again permitted to serve customers on-site by moving all dining outdoors, limiting group size, and spacing tables, among other restrictions. However, on November 22, 2020 the Los Angeles County Department of Health suspended outdoor dining at restaurants, and the Governor did not lift statewide stay-at-home orders to allow restaurants to reopen for outdoor dining until January 25, 2021.

The complaint included numerous allegations concerning the transmissibility of the COVID-19 virus and unfolding pandemic in California. Citing reports by the World Health Organization (WHO) and the Center for Disease Control and

Prevention (CDC), the complaint alleged the COVID-19 virus can spread through "[f]loating respiratory droplets, called aerosols" that "behave like smoke," and it can both "linger in the air for minutes to hours" and also "travel[] on air currents until they attach to an object or other surface." The WHO and CDC "have recognized the tendency of the [COVID-19 virus] to attach to objects and surfaces, 'such as tables, doorknobs, and handrails,' " and the virus " 'may remain viable for hours to days on surfaces made from a variety of materials.' " The complaint alleged further, "Numerous other scientific studies have discovered that the [COVID-19] virus can survive and persist on surfaces and buildings for nearly a month." Moreover, "The scientific community has confirmed that coronavirus and COVID-19 alter the conditions of properties and buildings such that the premises are no longer safe and habitable for normal use. Without substantial physical alterations, systems changes to facilities, and new protocols for air circulation, disinfection, and disease prevention, an infected property cannot remain open to the public. Cleaning of surfaces alone is insufficient."

*3 Specifically, according to one WHO publication, the COVID-19 virus "adheres to, attaches to, and alters the surfaces of the property and surfaces upon which ... physical droplets land, and physically changes these once safe surfaces to 'fomites.' Fomites are objects, previously safe to touch, that now serve as agents and [a] mechanism for transmission of deadly, infectious viruses and diseases." "Thus, the coronavirus and COVID-19 physically change properties and surfaces such that contact with these properties and surfaces, which previously would have been safe, is now deadly and dangerous. This constitutes real and severe damage to and loss of the properties."

The complaint alleged La Cava suffered physical loss of or damage to its dining rooms and other property "caused by the actual presence of virus droplets in the air and on the surfaces in the vicinity of and in [its] restaurant" and "in the form of virus matter present on walls, floors, tables, chairs, silverware, dishes, and other surfaces." The complaint identified 10 commercial businesses, including three restaurants, in Sherman Oaks and its environs, where employees contracted COVID-19. Three of La Cava's employees suffered from COVID-19 in December 2020 and January 2021. The complaint alleged on information and belief that "La Cava is aware that it entertained customers since March 2020 who subsequently tested positive for COVID-19 and who had the ability to use the restroom facilities during the time they were outside dining." "[T]he

virus ... is therefore certain to have been present at La Cava at various times,” and “droplets containing SARS-CoV-2 have been physically present at the La Cava restaurant premises insured by the Policy at all relevant times.” The complaint alleged further in paragraph 81, “The presence of droplets containing coronavirus at La Cava led to its closure and constitutes covered physical damage to [La Cava's] premises. Once the La Cava management was made aware by the Orders of the clear and present danger of the virus and its existence everywhere in LA County, including on the surfaces and in the air in and around La Cava's premises, it promptly shut down operations.”

In addition to lost business revenue due to the suspension of operations, La Cava “incurred substantial costs in an attempt to mitigate the suspension of its operations, including but not limited to expenses incurred for reconfiguration to outside dining and increased sanitation procedures. [La Cava] would not have incurred those costs but for the direct physical loss or damage caused by the coronavirus, COVID-19, and the [government] Orders.”

On March 18, 2020, two days after its initial suspension of operations, La Cava submitted a claim to Century-National by telephone for the income lost as a result of the virus and the related government orders. As alleged, Century-National “undertook no steps to determine whether the virus had caused physical damage to the La Cava premises.” Instead, “without engaging in any legitimate, true, meaningful, or thorough investigation, [Century-National] denied [La Cava's] claim.” Specifically, on April 9, 2020 Century-National (through its claims adjuster) responded in a letter stating the business income coverage did not apply to the claim because “[t]he suspension of your business was not caused by a ‘direct physical loss of or damage to property’ at your designated premises” and “[t]he government directives at issue did not ‘prohibit access’ to your designated premises and did not result from a loss or damage at ... premises ‘other than’ your designated premises.” (Capitalization omitted.)

La Cava's first cause of action for declaratory judgment sought a declaration that Century-National was obligated to provide coverage for losses incurred in connection with La Cava's COVID-19-related claims. The second cause of action for breach of contract alleged La Cava “suffered the direct physical loss of property and lost business income following California's Stay at Home Order and due to the presence of the coronavirus in and around its premises —losses which were covered under the Policy purchased

from [Century-National].” These losses included “loss of and damage to some or all of [La Cava's] covered property and its functionality, which became useless, dangerous, or uninhabitable, resulting in substantial loss of business income, lost revenue from having to suspend or limit its operations, and extra expenses incurred to mitigate the suspension of its operations.” The complaint also alleged there were no relevant policy exclusions, and La Cava complied with the terms and conditions of the policy.

*4 The third cause of action for breach of the implied covenant of good faith and fair dealing alleged Century-National engaged in bad faith by, among other things, denying La Cava's claim without undertaking steps to determine whether the virus had caused physical damage to the premises, “[u]nreasonably refusing to conduct a thorough investigation of [La Cava's] claims, and ignoring evidence that supports coverage instead of inquiring into possible bases that might support [La Cava's] claim.” The fourth cause of action for violation of the UCL, pleaded as a class claim,² alleged Century-National engaged in unlawful conduct in violation of Insurance Code section 790 et seq. by categorically denying La Cava's and other class members' claims without a fair investigation.

2 The class allegations are not at issue in this appeal.

C. Century-National's Demurrer

On April 14, 2021 Century-National filed a demurrer to the first amended complaint.³ Century-National argued that under California law, the phrase “direct physical loss or damage to property” in an insurance contract requires a physical alteration of the insured property, but La Cava did not and could not allege its loss of business income was attributable to any physical alteration of La Cava's property by the COVID-19 virus. In support of its position, Century-National cited nearly two dozen decisions from federal district courts in California holding business closures due to the COVID-19 virus or related government orders did not result from direct physical loss of or damage to property and dismissing the insured's claims based on the denial of coverage. In addition, the civil authority coverage under the policy did not cover the losses because the government shutdown orders did not prohibit access to La Cava's premises and were not issued “due to direct physical loss or damage to property” at La Cava, as provided in the policy. Further, Century-National did not act in bad faith because it properly denied coverage based on an “undeniably” genuine dispute

as to the existence of coverage as shown by the fact “nearly every judge in California to consider the coverage issues herein has found no coverage for these COVID-19 business-interruption claims.”

3 On February 19, 2021 the trial court sustained Century-National's demurrer to the original complaint with leave to amend. The original complaint did not include the allegations that since March 2020 three of La Cava's employees and many of its customers and the employees of nearby businesses tested positive for the COVID-19 virus.

After a hearing, on June 2, 2021 the trial court sustained Century-National's demurrer without leave to amend. Citing five federal district court decisions in California denying coverage and observing that “substantially all of the federal district courts” were in agreement, the court found, “[C]ourts have routinely held, and this Court agrees, that the existence of COVID-19 in the air or on surfaces does not constitute ‘direct physical loss of or damage to property’ within the meaning of the insurance policy.” Accordingly, La Cava's allegations were insufficient as a matter of law to establish a covered loss. Civil authority coverage did not apply for the additional reason that La Cava failed to allege facts demonstrating it was “prohibited from accessing its building.” Because La Cava could not allege it was entitled to coverage under any provision of the policy, all four causes of action failed, and La Cava had not demonstrated a basis for leave to amend. The court entered a judgment of dismissal on June 16, 2021.

La Cava timely appealed.

DISCUSSION

A. Standard of Review

[1] [2] [3] “‘In reviewing an order sustaining a demurrer, we examine the operative complaint de novo to determine whether it alleges facts sufficient to state a cause of action under any legal theory.’ ” (*Mathews v. Becerra* (2019) 8 Cal.5th 756, 768, 257 Cal.Rptr.3d 2, 455 P.3d 277; accord, *T.H. v. Novartis Pharmaceuticals Corp.* (2017) 4 Cal.5th 145, 162, 226 Cal.Rptr.3d 336, 407 P.3d 18.) When evaluating the complaint, “we assume the truth of the allegations.” (*Brown v. USA Taekwondo* (2021) 11 Cal.5th 204, 209, 276 Cal.Rptr.3d 434, 483 P.3d 159; accord, *Lee v. Hanley* (2015) 61 Cal.4th 1225, 1230, 191 Cal.Rptr.3d 536, 354 P.3d 334.) “However,

we are not required to accept the truth of the factual or legal conclusions pleaded in the complaint.” (*Marina Pacific Hotel and Suites, LLC v. Fireman's Fund Insurance Company* (2022) 81 Cal.App.5th 96, 105, 296 Cal.Rptr.3d 777 (*Marina Pacific*); accord, *Mathews*, at p. 768,, 257 Cal.Rptr.3d 2, 455 P.3d 277 [“ ‘We treat the demurrer as admitting all material facts properly pleaded, but not contentions, deductions or conclusions of fact or law.’ ”].)

B. Interpretation of Insurance Contracts

*5 [4] [5] [6] “In general, interpretation of an insurance policy is a question of law that is decided under settled rules of contract interpretation.” (*State of California v. Continental Ins. Co.* (2012) 55 Cal.4th 186, 194, 145 Cal.Rptr.3d 1, 281 P.3d 1000; accord, *Marina Pacific, supra*, 81 Cal.App.5th at p. 105, 296 Cal.Rptr.3d 777.) “The principles governing the interpretation of insurance policies in California are well settled. ‘Our goal in construing insurance contracts, as with contracts generally, is to give effect to the parties’ mutual intentions. [Citations.] ‘If contractual language is clear and explicit, it governs.’ [Citations.] If the terms are ambiguous [i.e., susceptible of more than one reasonable interpretation], we interpret them to protect “ ‘the objectively reasonable expectations of the insured.’ ” [Citations.] Only if these rules do not resolve a claimed ambiguity do we resort to the rule that ambiguities are to be resolved against the insurer.’ ” (*Minkler v. Safeco Ins. Co. of America* (2010) 49 Cal.4th 315, 321, 110 Cal.Rptr.3d 612, 232 P.3d 612; accord, *Montrose Chemical Corp. of California v. Superior Court* (2020) 9 Cal.5th 215, 230, 260 Cal.Rptr.3d 822, 460 P.3d 1201; *Marina Pacific*, at p. 105, 296 Cal.Rptr.3d 777.)

[7] [8] “The ‘tie-breaker’ rule of construction against the insurer stems from the recognition that the insurer generally drafted the policy and received premiums to provide the agreed protection.” (*Minkler v. Safeco Ins. Co. of America, supra*, 49 Cal.4th at p. 321, 110 Cal.Rptr.3d 612, 232 P.3d 612; accord, *Marina Pacific, supra*, 81 Cal.App.5th at p. 106, 296 Cal.Rptr.3d 777.) “To further ensure that coverage conforms fully to the objectively reasonable expectations of the insured, ... in cases of ambiguity, basic coverage provisions are construed broadly in favor of affording protection, but clauses setting forth specific exclusions from coverage are interpreted narrowly against the insurer. The insured has the burden of establishing that a claim, unless specifically excluded, is within basic coverage, while the insurer has the burden of establishing that a specific exclusion applies.” (*Minkler*, at p. 322, 110 Cal.Rptr.3d 612, 232 P.3d 612; accord, *Montrose Chemical Corp. of California v.*

Superior Court, supra, 9 Cal.5th at p. 230, 260 Cal.Rptr.3d 822, 460 P.3d 1201; *Marina Pacific*, at p. 106, 296 Cal.Rptr.3d 777.)

C. Coverage for COVID-19 Pandemic-related Losses

At the time the trial court sustained the second demurrer, no California appellate court had addressed whether business losses caused by the COVID-19 pandemic were covered by commercial property insurance. Multiple California appellate courts have now addressed this question, but with differing results. In *Marina Pacific, supra*, 81 Cal.App.5th 96, 296 Cal.Rptr.3d 777, we addressed whether the owners of an insured restaurant and hotel had sufficiently pleaded they had suffered “direct physical loss of or damage to” the property supporting coverage under a commercial property insurance policy based on allegations of contamination of the insured premises with the COVID-19 virus.⁴ We concluded they had.

⁴ Our decision in *Marina Pacific* was filed on July 13, 2022, after La Cava's reply brief was filed. Century-National addressed our decision in its July 26 answer to the amicus brief filed by United Policyholders in support of La Cava, and the American Property and Casualty Insurance Association and the National Association of Mutual Insurance Companies addressed the decision in their amicus brief in support of Century-National, also filed on July 26, 2022. On July 27 we invited the parties to address *Marina Pacific* in any answer to an amicus brief or a supplemental brief. La Cava addressed our decision in its August 15 answer.

In *Marina Pacific*, the owners sued their insurer for breach of contract and related claims after the insurer denied coverage for losses claimed as a result of the COVID-19 pandemic. (*Marina Pacific, supra*, 81 Cal.App.5th at p. 102, 296 Cal.Rptr.3d 777.) The policy provided business interruption coverage for “ ‘the actual loss of business income and necessary extra expense you sustain due to the necessary suspension of your operation during the period of restoration arising from direct physical loss or damage to [covered] property.’ ”⁵ (*Id.* at p. 99, 296 Cal.Rptr.3d 777.) As we explained, the owners’ complaint alleged the COVID-19 virus “not only lives on surfaces but also bonds to surfaces through physicochemical reactions involving cells and surface proteins, which transform the physical condition of the property. The virus was present on

surfaces throughout the insured properties, including the hotel lobby, kitchens at both the hotel and restaurant, employee breakroom, service elevator and parking garage, as well as on the properties’ food, bedding, fixtures, tables, chairs and countertops. Because of the nature of the pandemic, the virus was continually reintroduced to surfaces at those locations. As a direct result, the [owners] were required to close or suspend operations in whole or in part at various times and incurred extra expense as they adopted measures to restore and remediate the air and surfaces at the insured properties. The [owners] specifically alleged they were required to ‘dispose of property damaged by COVID-19 and limit operations at the Insured Properties.’ ” (*Id.* at pp. 108-109, 296 Cal.Rptr.3d 777.)

⁵ The policy at issue in *Marina Pacific* also included “ ‘communicable disease coverage’ ” for “ ‘direct physical loss or damage’ to insured property ‘caused by or resulting from a covered communicable disease event,’ including costs necessary to repair or rebuild insured property damaged or destroyed by the communicable disease and to ‘[m]itigate, contain, remediate, treat, clean, detoxify, disinfect, neutralize, cleanup, remove, dispose of, test for, monitor and assess the effects [of] the communicable disease.’ ” (*Marina Pacific, supra*, 81 Cal.App.5th at p. 100, 296 Cal.Rptr.3d 777.) The communicable disease coverage also covered losses from the suspension of operations “ ‘due to direct physical loss or damage to property at a location caused by or resulting from a covered communicable disease event.’ ” (*Ibid.*) The policy at issue here does not contain a similar provision.

*6 Based on these allegations, we reversed the trial court's order sustaining the insurer's demurrer without leave to amend. (*Marina Pacific, supra*, 81 Cal.App.5th at p. 114, 296 Cal.Rptr.3d 777.) We assumed for purposes of our opinion that the undefined policy term “direct physical loss or damage” meant the owners needed to allege an external force acted on the insured property causing a “distinct, demonstrable, physical alteration of the property,” as stated in *MRI Healthcare Center of Glendale, Inc. v. State Farm General Ins. Co.* (2010) 187 Cal.App.4th 766, 115 Cal.Rptr.3d 27 (*MRI Healthcare*). (See *Marina Pacific*, at p. 108, 296 Cal.Rptr.3d 777; *MRI Healthcare*, at pp. 770, 779, 115 Cal.Rptr.3d 27 [failure of MRI machine to function after it was demagnetized to enable roof repair following

storms was not a covered loss because “there was no ‘distinct, demonstrable [or] physical alteration’ of the MRI machine”].)

We concluded the complaint adequately alleged physical alteration of the premises, explaining, “Assuming, as we must, the truth of those allegations, even if improbable, absent judicially noticed facts irrefutably contradicting them, the insureds have unquestionably pleaded direct physical loss or damage to covered property within the definition articulated in *MRI Healthcare*—a distinct, demonstrable, physical alteration of the property.” (*Marina Pacific, supra*, 81 Cal.App.5th at p. 109, 296 Cal.Rptr.3d 777.) We recognized our holding was at odds with many federal district court decisions dismissing claims for pandemic-related business losses. (*Ibid.*) But those cases did not involve similar factual allegations, and to the extent they were analogous, federal pleading standards, unlike California’s, permitted the district courts to dismiss the claims. (*Id.* at pp. 109-110, 296 Cal.Rptr.3d 777.) We observed, “Unlike in federal court, the plausibility of the insureds’ allegations has no role in deciding a demurrer under governing state law standards, which ... require us to deem as true, ‘however improbable,’ facts alleged in a pleading—specifically here, that the COVID-19 virus alters ordinary physical surfaces transforming them into fomites through physicochemical processes, making them dangerous and unusable for their intended purposes unless decontaminated.’” (*Marina Pacific*, at pp. 109-110, 296 Cal.Rptr.3d 777; see *Hacker v. Homeward Residential, Inc.* (2018) 26 Cal.App.5th 270, 280, 236 Cal.Rptr.3d 790 [in considering the merits of a demurrer, “‘the facts alleged in the pleading are deemed to be true, however improbable they may be’ ”].)

We also addressed three published Court of Appeal decisions that had addressed pandemic coverage, each affirming an order sustaining the insurer’s demurrer. We concluded *Musso & Frank Grill Co., Inc. v. Mitsui Sumitomo Ins. USA Inc.* (2022) 77 Cal.App.5th 753, 293 Cal.Rptr.3d 1 and *Inns-by-the-Sea v. California Mutual Ins. Co.* (2021) 71 Cal.App.5th 688, 286 Cal.Rptr.3d 576 (*Inns-by-the-Sea*) were distinguishable because both involved only allegations of loss of use of the insured property as a result of government-ordered closures to limit the spread of COVID-19, “rather than, as expressly alleged here, a claim the presence of the virus on the insured premises caused physical damage to covered property, which in turn led to business losses.” (*Marina Pacific, supra*, 81 Cal.App.5th at p. 110, 296 Cal.Rptr.3d 777; see *Musso & Frank*, at pp. 758-759, 293 Cal.Rptr.3d 1 [policy requiring physical loss or damage

to property did not cover losses incurred as a result of pandemic-related order mandating that restaurants close by midnight]; *Inns-by-the-Sea*, at p. 703. [“*Inns* alleges that it ceased operations ‘as a direct and proximate result of the Closure Orders.’ It does not make the proximate cause allegation based on the particular presence of the virus on its premises.”].)⁶

6 As argued by amicus curiae United Policyholders, the Fourth District in *Inns-by-the-Sea, supra*, 71 Cal.App.5th at page 710, 286 Cal.Rptr.3d 576 observed that “a virus could cause a suspension of operations through direct physical loss of or damage to property,” and noted that “case law supports the view that ... an invisible substance or biological agent might give rise to coverage because it causes a policyholder to suspend operations due to direct physical loss of or damage to property.” (*Id.* at p. 710, fn. 21, 286 Cal.Rptr.3d 576.)

Although such allegations were absent in *Inns-by-the-Sea*, the court noted, “‘It could be a different story if a business—which could have otherwise been operating—had to shut down because of the presence of the virus within the facility. For example, a restaurant might need to close for a week if someone in its kitchen tested positive for COVID-19, requiring the entire facility to be thoroughly sanitized and remain empty for a period. Perhaps the restaurant could successfully allege that the virus created physical loss or damage in the same way some chemical contaminant might have.’” (*Id.* at pp. 704-705, 286 Cal.Rptr.3d 576.)

*7 We recognized the decision by our colleagues in Division Four of this district in *United Talent Agency v. Vigilant Ins. Co.* (2022) 77 Cal.App.5th 821, 293 Cal.Rptr.3d 65 was not distinguishable in that it presented similar allegations to those at issue in *Marina Pacific*. (*Marina Pacific, supra*, 81 Cal.App.5th at p. 111, 296 Cal.Rptr.3d 777.) In *United Talent*, the Court of Appeal affirmed an order sustaining the insurer’s demurrer, concluding allegations that the presence of the COVID-19 virus on property constituted direct physical loss or damage were insufficient as a matter of law to trigger coverage because “the virus exists worldwide wherever infected people are present, it can be cleaned from surfaces through general disinfection measures, and transmission may be reduced or rendered less harmful through practices unrelated to the property, such as social

distancing, vaccination, and the use of masks. Thus, the presence of the virus does not render a property useless or uninhabitable, even though it may affect how people interact with and within a particular space.” (*United Talent*, at p. 838., 293 Cal.Rptr.3d 65.) We rejected this approach, reasoning, “We are not authorized to disregard those allegations when evaluating a demurrer ... based on a general belief that surface cleaning may be the only remediation necessary to restore contaminated property to its original, safe-for-use condition.” (*Marina Pacific*, at p. 111, 296 Cal.Rptr.3d 777.) Moreover, “[e]ven if there had been evidence subject to proper judicial notice to establish that disinfecting repaired any alleged property damage, it would not resolve whether contaminated property had been damaged in the interim, nor would it alleviate any loss of business income or extra expenses.... [T]he duration of exposure may be relevant to the measure of policy benefits; it does not negate coverage.” (*Id.* at p. 112, 296 Cal.Rptr.3d 777.)

Since our *Marina Pacific* decision, Division Two of the First District has published two opinions addressing COVID-19 pandemic-related losses under policies providing coverage for direct physical loss of or damage to property. In *Apple Annie, LLC v. Oregon Mutual Ins. Co.* (2022) 82 Cal.App.5th 919, 925, 298 Cal.Rptr.3d 886, the Court of Appeal affirmed an order sustaining the insurer's demurrer, holding a restaurant owner failed to allege direct physical loss of or damage to its restaurant where the owner alleged only that its business losses were due to suspension of operations under state and county orders. In supplemental briefing after *Marina Pacific* was decided, the owner acknowledged *Marina Pacific* “ ‘does not directly implicate [the owner's] theory of coverage,’ ” but it argued there was a reasonable possibility it could amend its complaint to include allegations similar to those in *Marina Pacific*. (*Id.* at pp. 936-937, 298 Cal.Rptr.3d 886.) However, because at oral argument the owner's attorney stated as an officer of the court he could not state what facts he could allege in an amended complaint, the Court of Appeal concluded the owner did not meet its burden to obtain leave to amend. (*Id.* at p. 936, 298 Cal.Rptr.3d 886.) In *Tarrar Enterprises, Inc. v. Associated Indemnity Corp.* (2022) 83 Cal.App.5th 685, 688-689, 299 Cal.Rptr.3d 698, the Court of Appeal held that although the trial court properly sustained the insurer's demurrer because the insured had not alleged direct physical loss of or damage to property, the court abused its discretion in denying leave to amend because the insured's appellate briefs set forth “in some detail” the proposed amendments.⁷

7

In *Amy's Kitchen, Inc. v. Fireman's Fund Ins. Co.* (2022) 83 Cal.App.5th 1062, 1070-1071, 299 Cal.Rptr.3d 885, Division Four of the First District interpreted a policy providing coverage for a communicable disease event not to require physical alteration of the premises because the policy language specifically referred to coverage for the costs to disinfect, cleanup, and remove the communicable disease. The Court of Appeal reversed the trial court order, holding the court should have granted leave to amend to plead a communicable disease event. (*Id.* at pp. 1072-1073, 299 Cal.Rptr.3d 885.)

D. The Trial Court Erred in Sustaining the Demurrer

1. La Cava adequately stated causes of action for breach of contract and declaratory judgment based on alleged direct physical loss or damage to its property caused by the COVID-19 virus

On appeal, La Cava contends the alleged contamination of its restaurant by the COVID-19 virus constituted a “physical change” sufficient to trigger coverage under the Century-National policy. Century-National and amici curiae argue the policy language providing coverage for a direct physical loss of or damage to property required a distinct, demonstrable, physical alteration of the property. Even assuming La Cava was required to allege a distinct, demonstrable physical alteration of the property to show coverage under the policy (as stated in *MRI Healthcare, supra*, 187 Cal.App.4th at page 779, 115 Cal.Rptr.3d 27),⁸ the allegations of the complaint were sufficient.

8

In its opening brief, La Cava argued the policy term “direct physical loss of or damage to” should not be interpreted to require a physical alteration, and the interpretive rule adopted in *MRI Healthcare, supra*, 187 Cal.App.4th 766, 115 Cal.Rptr.3d 27 should be limited to cases involving intangible changes to personal property, not real property. However, La Cava acknowledged in its supplemental briefing that “in light of *Marina Pacific Hotel's* holding that identical circumstances to La Cava's satisfy this standard, the dispute is no longer relevant.”

*8 [9] The first amended complaint alleged the virus was “certain to have been present at La Cava at various times,” including “in the form of virus matter present on walls, floors, tables, chairs, silverware, dishes, and other surfaces.”

As alleged, this was because thousands of people visited La Cava in the weeks preceding the shutdown, and based on the spread of the pandemic, it was “beyond doubt that some—likely many—of them were infected with the virus and breathed virus matter onto surfaces at La Cava.” Further, since March 2020 La Cava had patrons who subsequently tested positive for COVID-19 and who had the ability to use the restrooms although they were dining outside, and three employees contracted COVID-19 in late December 2020 and January 2021. (See *Marina Pacific*, *supra*, 81 Cal.App.5th at p. 108, 296 Cal.Rptr.3d 777 [owners alleged virus “was present on surfaces throughout the insured properties”].)

The complaint also alleged health authorities and medical scientists advised that the virus “can remain on smooth surfaces for at least 28 days,” and it “adheres to, attaches to and alters the surfaces of the property and surfaces” it comes into contact with, creating “fomites,” which are “objects, previously safe to touch, that now serve as agents and mechanism for transmission of deadly, infectious viruses and diseases.” (See *Marina Pacific*, *supra*, 81 Cal.App.5th at p. 101, 296 Cal.Rptr.3d 777 [owners alleged COVID-19 virus “‘actually bonds and/or adheres to such objects through physico-chemical reactions’ ” and “ ‘caus[es], among other things, a distinct, demonstrable or physical alteration to property’ ”].) “Cleaning of surfaces alone is insufficient,” and safe operations would require “substantial physical alterations, systems changes to facilities, and new protocols for air circulation, disinfection, and disease prevention.” Because routine cleaning was insufficient, “[t]he presence of droplets containing coronavirus at La Cava led to its closure and constitute[d] covered physical damage to [La Cava’s] premises.” As a result, La Cava lost business revenues and incurred substantial costs to mitigate the damage by reconfiguring its property and increasing its sanitization procedures. (See *Marina Pacific*, at pp. 108-109, 296 Cal.Rptr.3d 777 [owners “were required to close or suspend operations in whole or in part at various times and incurred extra expense as they adopted measures to restore and remediate the air and surfaces at the insured properties”].)

As discussed, the trial court found these allegations were not sufficient as a matter of law, relying on federal decisions ruling out the possibility of covered losses and the absence of authority supporting La Cava’s position. We disagree with the court’s reasoning, as stated in its order sustaining the demurrer to the original complaint, that La Cava could not show the COVID-19 virus permanently damages surfaces because “it is well-known that SARS-CoV-2 surface contamination is

ephemeral, and [La Cava] has not presented the Court with any authority holding that an ephemeral, pathogenic surface contamination qualifies as ‘damage to’ property under this or similar policies.” As we discussed in *Marina Pacific*, *supra*, 81 Cal.App.5th at page 109, 296 Cal.Rptr.3d 777, the insured is not required to provide authority at the pleading stage to support its position that contamination with the COVID-19 virus caused damage to the surfaces in its premises.

In its answer to the amicus brief filed by United Policyholders, Century-National argues *Marina Pacific* embodies a “narrow exception” to the general rule that pandemic-related damages are not recoverable under business loss coverage, and it urges us instead to follow the skeptical approach taken by Division Four of this district in *United Talent Agency v. Vigilant Ins. Co.*, *supra*, 77 Cal.App.5th 821, 293 Cal.Rptr.3d 65. We see no reason to deviate from our decision in *Marina Pacific*, which did not carve out simply a “narrow exception,” as suggested by Century-National. Further, as discussed, the policy provisions at issue in *Marina Pacific* are not materially different from those in the Century-National policy.⁹ Although Century-National is correct that we considered the communicable diseases coverage in construing the policy language in *Marina Pacific*, we concluded there was a sufficient, independent basis for lost business income coverage under the policy provision for losses due “to the necessary suspension of your operation during the period of restoration arising from direct physical loss or damage to [covered] property.” (*Id.* at pp. 109, 112, 296 Cal.Rptr.3d 777.)

9

Amici curiae American Property and Casualty Insurance Association and the National Association of Mutual Insurance Companies seek to distinguish *Marina Pacific* on similar grounds. They also contend that allowing La Cava’s complaint to proceed would destabilize insurance markets by upholding claims for losses due to any regulation that limits a business’s operations, such as a noise ordinance mandating early closure or a fire regulation reducing occupancy and requiring reconfiguration. We are unpersuaded. These types of regulations would not involve allegations that “an external force acted on the insured property causing a physical change in the condition of the property,” as alleged by La Cava with respect to the COVID-19 virus contamination of its restaurant. (*Marina Pacific*, *supra*, 81 Cal.App.5th at p. 107, 296 Cal.Rptr.3d 777; accord, *ARI*

Healthcare, *supra*, 187 Cal.App.4th at p. 779, 115 Cal.Rptr.3d 27.) Moreover, to the extent amici contend we should interpret the Century-National and similar policies not to apply to COVID-19 virus contamination for policy reasons, that is an argument best made to the Legislature, not directed to our review of the adequacy of the allegations in the first amended complaint.

*9 Century-National's argument that La Cava shut down because of the government closure orders, and not the COVID-19 pandemic fares no better. Century-National points to La Cava's allegation in paragraph 81 that "[o]nce the La Cava management was made aware by the Orders of the clear and present danger of the virus and its existence everywhere in LA County, including on the surfaces and in the air in and around La Cava's premises, it promptly shut down operations." Although this allegation references the government orders, a fair reading of the allegation is that it was the orders that apprised La Cava of the existence and danger of the COVID-19 virus, not that the shut down happened as a result. Moreover, as alleged, the City of Los Angeles Mayor's May 15 public health order prohibited restaurants from serving food on site, limiting restaurants to delivery, pickup, or drive-through service of customers, but it did not require restaurants to shut down entirely. To the extent the complaint alleges La Cava initially shut down for two weeks, then modified its operations, due to the COVID-19 virus and the government orders, it is a question of fact for a summary judgment motion or trial whether the restaurant closure and modifications resulted from damage caused by the COVID-19 virus or the government orders.

[10] Because La Cava sufficiently pleaded direct physical loss or damage to its property caused by the COVID-19 virus to trigger coverage, the trial court erred in sustaining the demurrer to the causes of action for breach of contract and declaratory judgment. "[T]he elements of a cause of action for breach of contract are (1) the existence of the contract, (2) plaintiff's performance or excuse for nonperformance, (3) defendant's breach, and (4) the resulting damages to the plaintiff." (*Marina Pacific*, *supra*, 81 Cal.App.5th at p. 108, 296 Cal.Rptr.3d 777; accord, *Oasis West Realty, LLC v. Goldman* (2011) 51 Cal.4th 811, 821, 124 Cal.Rptr.3d 256, 250 P.3d 1115.) Century-National's demurrer challenged only the third element, contending it did not breach its obligation to pay benefits under the policy because La Cava failed to allege damage to or loss of La Cava's premises within the meaning of the policy.¹⁰ And the parties' coverage dispute is clearly a proper basis for a declaratory judgment cause of

action. (Code Civ. Proc., § 1060 ["Any person interested ... under a contract ... may, in cases of actual controversy relating to the legal rights and duties of the respective parties, bring an original action ... for a declaration of his or her rights and duties ..., including a determination of any question of construction or validity arising under the ... contract."]; see *Lee v. Silveira* (2016) 6 Cal.App.5th 527, 546, 211 Cal.Rptr.3d 705 [declaratory relief claimant must show "two essential elements: '(1) a proper subject of declaratory relief, and (2) an actual controversy involving justiciable questions relating to the rights or obligations of a party'"].)

10 Because we conclude La Cava alleged loss of business income caused by direct physical loss of or damage to its property, we do not reach whether La Cava adequately alleged entitlement to civil authority coverage, which under the policy required government action that "prohibits access to the premises due to direct physical loss of or damage to the property, other than at the described premises"

2. La Cava adequately alleged causes of action for bad faith and violation of the UCL based on Century-National's summary denial of its insurance claim

As discussed, Century-National argued in its demurrer that even if the trial court were to find La Cava adequately alleged breach of the policy, La Cava could not state a claim for breach of the covenant of good faith and fair dealing because there was a genuine dispute over policy coverage in light of the fact "nearly every judge in California" that had considered the question of coverage for COVID-19-related business losses found no coverage. Although the trial court did not reach this argument, Century-National contends on appeal the complaint independently failed to state a claim for bad faith because the denial of La Cava's insurance claim turned on a disputed interpretation of the policy. La Cava has adequately alleged causes of action for bad faith and violation of the UCL.¹¹

11 Century-National does not dispute that allegations sufficient to support a cause of action for breach of the covenant of good faith and fair dealing are also sufficient to support a claim for violation of the UCL. (See *Zhang v. Superior Court* (2013) 57 Cal.4th 364, 380, 159 Cal.Rptr.3d 672, 304 P.3d 163 ["[B]ad faith insurance practices may qualify as any of the three statutory forms of

unfair competition. They are unlawful; the insurer's obligation to act fairly and in good faith to meet its contractual responsibilities is imposed by the common law, as well as by statute. They are unfair to the insured; unfairness lies at the heart of a bad faith cause of action. They may also qualify as fraudulent business practices.”], citations and footnote omitted.)

*10 [11] [12] “[I]n a claim against an insurance carrier, ‘there are at least two separate requirements to establish breach of the implied covenant [of good faith and fair dealing]: (1) benefits due under the policy must have been withheld; and (2) the reason for withholding benefits must have been unreasonable or without proper cause.’” (*Grebow v. Mercury Ins. Co.* (2015) 241 Cal.App.4th 564, 581, 194 Cal.Rptr.3d 259; accord, *Tilbury Constructors, Inc. v. State Comp. Ins. Fund* (2006) 137 Cal.App.4th 466, 475, 40 Cal.Rptr.3d 392.) It is “settled law in California that an insurer denying or delaying the payment of policy benefits due to the existence of a genuine dispute with its insured as to the existence of coverage liability or the amount of the insured's coverage claim is not liable in bad faith even though it might be liable for breach of contract.” (*Chateau Chamberay Homeowners Assn. v. Associated Internat. Ins. Co.* (2001) 90 Cal.App.4th 335, 347, 108 Cal.Rptr.2d 776; accord, *Case v. State Farm Mutual Automobile Ins. Co., Inc.* (2018) 30 Cal.App.5th 397, 402, 241 Cal.Rptr.3d 458.) “[W]here there is a *genuine* issue as to the insurer's liability under the policy ..., there can be no bad faith liability imposed on the insurer for advancing its side of that dispute.” (*Chateau Chamberay*, at p. 347, 108 Cal.Rptr.2d 776; accord, *Case*, at p. 402, 241 Cal.Rptr.3d 458.)

[13] [14] [15] However, “‘[t]he genuine dispute rule does not relieve an insurer from its obligation to thoroughly and fairly investigate, process and evaluate the insured's claim. A genuine dispute exists only where the insurer's position is maintained in good faith and on reasonable grounds.’” (*Ghazarian v. Magellan Health, Inc.* (2020) 53 Cal.App.5th 171, 186, 266 Cal.Rptr.3d 841.) “‘[T]he reasonableness of an insurer's claims-handling conduct is ordinarily a question of fact, [but] becomes a question of law where the evidence is undisputed and only one reasonable inference can be drawn from the evidence.’” (*Hedayati v. Interinsurance Exchange of the Automobile Club* (2021) 67 Cal.App.5th 833, 843, 283 Cal.Rptr.3d 199; accord, *Chateau Chamberay Homeowners Assn. v. Associated Internat. Ins. Co.*, *supra*, 90 Cal.App.4th at p. 350, 108 Cal.Rptr.2d 776 [affirming summary adjudication of bad faith claim in favor of insurer

where insured offered only a two-page expert declaration expressing conclusory opinion the insurer had not conducted an adequate and thorough investigation of loss].)

The first amended complaint alleged Century-National “undertook no steps to determine whether the virus had caused physical damage to the La Cava premises,” and “without engaging in any legitimate, true, meaningful, or thorough investigation,” it summarily denied the claim. Further, Century-National responded to La Cava's policy claim with what “appears to be a form letter sent in response to business income claims arising from [government shutdown orders]” stating, in relevant part, “The suspension of your business was not caused by a ‘direct physical loss of or damage to property’ at your designated premises.”

[16] Century-National does not challenge the sufficiency of the allegations it failed to conduct any investigation of La Cava's claim; rather, it contends its denial was based on a disputed interpretation of the policy. But a genuine dispute foreclosing a bad faith claim exists only where the insurer's position is maintained “in good faith and on reasonable grounds.” (*Ghazarian v. Magellan Health, Inc.*, *supra*, 53 Cal.App.5th at p. 186, 266 Cal.Rptr.3d 841.) At the pleadings stage, Century-National's denial of coverage just three weeks after La Cava tendered its claim and in the earliest days of our understanding of the novel COVID-19 virus, cannot be deemed as a matter of law to have been made in good faith with reasonable grounds. Century-National treats *Marina Pacific* as a sea change in the law and characterizes its own position in April 2020 as clearly justified by the later endorsement of that position by numerous district courts. But at the time, it was settled law that environmental contamination that resulted in physical damage could trigger business income coverage. (See *Inns-by-the-Sea*, *supra*, 71 Cal.App.5th 688, 703, 286 Cal.Rptr.3d 576 [surveying pre-pandemic cases recognizing an insured could allege “the COVID-19 virus—like smoke, ammonia, odor, asbestos—is a physical force” and was present on insured premises and directly caused damage].) La Cava alleged COVID-19 was present and physically damaged its restaurant, and it alleged its insurance claim was not limited to civil authority coverage. And, as alleged, Century-National did not take any steps to determine whether COVID-19 caused physical damage to the La Cava premises before denying coverage.

DISPOSITION

*11 The judgment is reversed. The matter is remanded for the trial court to vacate its order sustaining the demurrer without leave to amend and to enter a new order overruling the demurrer. La Cava is to recover its costs on appeal.

PERLUSS, P. J.

SEGAL, J.

All Citations

--- Cal.Rptr.3d ----, 2022 WL 18110247

We concur:

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EXHIBIT B

Another Planet Entertainment, LLC v. Vigilant Ins. Co.,
2022 WL 17972557

EXHIBIT B

Another Planet Entertainment, LLC v. Vigilant Ins. Co.,
2022 WL 17972557

2022 WL 17972557

United States Court of Appeals, Ninth Circuit.

ANOTHER PLANET ENTERTAINMENT,

LLC, Plaintiff-Appellant,

v.

VIGILANT INSURANCE

COMPANY, Defendant-Appellee.

No. 21-16093

I

Filed December 28, 2022

Synopsis

Background: Insured event promoter and venue operator filed suit against insurer, claiming breach of contract, bad faith, and fraud based on insurer's denial of coverage, under commercial property policy, for business income losses incurred following government closure orders issued during COVID-19 pandemic. The United States District Court for the Northern District of California, Vince Chhabria, J., 2021 WL 2670743, granted insurer's motion to dismiss for failure to state claim. Insured appealed.

[**Holding:**] The Court of Appeals held that question would be certified as to whether actual or potential presence of COVID-19 virus on insured's premises constituted direct physical loss or damage to property under policy.

Question certified.

Procedural Posture(s): On Appeal; Motion to Dismiss for Failure to State a Claim; Certified Question.

West Headnotes (2)

[1] **Federal Courts** ⇌ Inferior courts
Court of Appeals will ordinarily accept the decision of an intermediate appellate court as the controlling interpretation of state law.

[2] **Federal Courts** ⇌ Particular questions

In insured's action against insurer, claiming breach of contract, bad faith, and fraud based on insurer's denial of coverage for business income losses incurred following government closure orders issued during COVID-19 pandemic, question would be certified to California Supreme Court as to whether actual or potential presence of COVID-19 virus on insured's premises constituted "direct physical loss or damage to property" for purposes of coverage under commercial property insurance policy.

D.C. No. 3:20-cv-07476-VC

Attorneys and Law Firms

Kirk Pasich (argued), Nathan M. Davis, and Arianna M. Young, Pasich LLP, Los Angeles, California, for Plaintiff-Appellant.

Jonathan D. Hacker (argued), Jenya Godina, and Jeremy R. Gorton, O'Melveny & Myers LLP, Washington, D.C.; Susan Koehler Sullivan, Douglas J. Collodel, Gretchen S. Carner, and Brett C. Safford, Clyde & Co US LLP, Los Angeles, California; for Defendant-Appellee.

Before: Carlos T. Bea, Sandra S. Ikuta, and Morgan Christen, Circuit Judges.

ORDER CERTIFYING QUESTION TO THE CALIFORNIA SUPREME COURT

We respectfully ask the California Supreme Court to answer the certified question presented below, pursuant to California Rule of Court 8.548, because we have concluded that resolution of this question of California law "could determine the outcome of a matter pending in [this] court," and "[t]here is no controlling precedent" in the decisions of the California Supreme Court. Cal. R. Ct. 8.548(a).

This case involves an insured who sued for breach of contract, bad faith, and fraud when its insurer denied coverage for business income losses that the insured incurred following government closure orders issued during the COVID-19 pandemic. The insured alleged that the COVID-19 virus was present on its premises before the orders were issued, or would have been present had the insured not closed

its venues in compliance with the orders, and it sought coverage under several provisions of its commercial property insurance policy that require “direct physical loss or damage to property” to trigger coverage. The district court dismissed the insured's suit for failure to state a claim.

The issue here is whether the insured's allegations, if taken as true, were sufficient to show “direct physical loss or damage to property” as defined by California law.

I

We summarize the material facts. *See* Cal. R. Ct. 8.548(b) (3). Another Planet is an event promoter and venue operator that owns event venues in California and Nevada. In 2019, Vigilant Insurance Company issued a commercial property insurance policy to Another Planet for the period from May 1, 2019 to May 1, 2020. After the COVID-19 pandemic began in early 2020, government closure orders forced Another Planet to suspend its operations, close its venues, and cancel events, resulting in “substantial financial losses.” Another Planet sought and was denied coverage from Vigilant. In response, Another Planet filed an action in the Northern District of California, alleging breach of contract, bad faith, and fraud.

Another Planet seeks coverage under several provisions of its policy that require actual or imminent “direct physical loss or damage to property”: (1) a set of four “Business Income” provisions stating that Vigilant will cover certain business income losses if they are caused by “direct physical loss or damage” to property; (2) a “Civil Authority” provision stating that Vigilant will cover losses caused by a civil authority's prohibition of access to covered or dependent business premises as “the direct result of direct physical loss or damage to property” within one mile of the premises; and (3) a “Loss Prevention Expenses” provision stating that Vigilant will cover costs incurred to protect a building or personal property from “imminent direct physical loss or damage” caused by a covered peril if the insured provides notice of “any loss prevention action” within 48 hours.

*2 In its First Amended Complaint, Another Planet alleged that the COVID-19 virus “was present at various times on and in its insured properties, or would have been present had it not been for the closures of its properties directed to curb the spread of SARS-CoV-2.” It further alleged that aerosolized droplets of the COVID-19 virus can “stay suspended in air and infective for at least 16 hours” and

can remain active on inert surfaces for at least 28 days, meaning the droplets “physically alter the air and airspace in which they are present and the surfaces of both the real and personal property to which they attach, constituting physical loss or damage.” Another Planet claimed that the presence of COVID-19 droplets “can render both real and personal property unusable for its intended purpose and function, constituting physical loss or damage.” The complaint also noted that minimizing the spread of COVID-19 “requires steps to be taken,” including “physical distancing, regular disinfection, air filtration, and further physical alterations, such as installation of physical barriers restricting the movement of the aerosolized droplets.”

Vigilant filed a motion to dismiss under Federal Rule of Civil Procedure 12(b)(6), arguing that Another Planet had not sufficiently alleged direct physical loss or damage to property. The district court agreed and dismissed the case with prejudice after giving Another Planet one opportunity to amend its complaint. As relevant to this request for certification, the district court concluded that it “seem[ed] unknowable” whether the COVID-19 virus was actually present on Another Planet's premises.

II

[1] Because California law governs interpretation of the policy and the California Supreme Court has not yet considered the issue, we “must determine what result [that] court would reach based on state appellate court opinions, statutes and treatises.” *Mudpie, Inc. v. Travelers Cas. Ins. Co. of Am.*, 15 F.4th 885, 889 (9th Cir. 2021) (quoting *Diaz v. Kubler Corp.*, 785 F.3d 1326, 1329 (9th Cir. 2015)). “We will ordinarily accept the decision of an intermediate appellate court as the controlling interpretation of state law.” *Id.* (quoting *Tomlin v. Boeing Co.*, 650 F.2d 1065, 1069 n.7 (9th Cir. 1981)). Here, however, two different divisions of the Second District of the California Courts of Appeal have issued conflicting decisions regarding whether allegations like Another Planet's suffice to state a viable claim for “direct physical loss or damage to property.”

Two months after the district court dismissed Another Planet's suit, Division 4 of the Second District of the California Courts of Appeal decided *United Talent Agency v. Vigilant Insurance Co.*, which involved claims for coverage under insurance provisions identical to those in Another Planet's policy. 77 Cal.App.5th 821, 293 Cal. Rptr. 3d 65, 68 (2022). In *United*

Talent Agency, the insured alleged that the COVID-19 virus had been present on its insured premises or would have been present but for the government closure orders and the insured's efforts to reduce and prevent the virus's presence; that several of the insured's employees, their spouses, and their dependents had tested positive for COVID-19; and that COVID-19 droplets "land on and adhere to surfaces and objects" and thus "physically change the property by becoming part of its surface." *Id.* at 69. The insured in *United Talent Agency* compared COVID-19 to "mold, asbestos, mudslides, smoke, oil spills, and other similar elements that cause property damage, although they later might be removed, cleaned, or remediated." *Id.*

The Court of Appeal in *United Talent Agency* held that the superior court properly sustained the insurer's demurrer, concluding that the insured did "not establish[] that the presence of the virus constitutes physical damage to insured property." *Id.* at 76–80. The court acknowledged the existence of cases concluding that the presence of a "physical force" like "smoke, ammonia, odor, or asbestos" can constitute direct physical damage by "render[ing] real property uninhabitable or unsuitable for its intended use." *Id.* at 77 (quoting *Inns-by-the-Sea v. Cal. Mut. Ins. Co.*, 71 Cal.App.5th 688, 286 Cal. Rptr. 3d 576, 589 (2021)). But the court reasoned that the presence of COVID-19 is only " 'short lived' contamination that can be addressed by simple cleaning" and thus does not constitute direct physical loss or damage. *Id.* at 76–77 (quoting *Inns-by-the-Sea*, 286 Cal. Rptr. 3d at 588 n.17).

*3 Three months after *United Talent Agency*, Division 7 of the Second District of the California Courts of Appeal came to a different conclusion in *Marina Pacific Hotel & Suites, LLC v. Fireman's Fund Insurance Co.*, a case involving the denial of coverage under a policy that also contained the same "direct physical loss or damage" language at issue here. 81 Cal.App.5th 96, 296 Cal. Rptr. 3d 777, 780 (2022). In *Marina Pacific*, the insureds alleged that the COVID-19 virus causes a "distinct, demonstrable or physical alteration to property" because it "actually bonds and/or adheres to ... objects through physico-chemical reactions involving, *inter alia*, cells and surface proteins." *Id.* at 781. The insureds claimed that the COVID-19 virus had been present "on a variety of physical objects in [their] insured properties, including furniture, countertops, walls, bedding, appliances and food and other packaged items, as well as in the air," and that they had disposed of property damaged by the virus. *Id.* at 781–82. Further, they alleged that "public health authorities ha[d] ordered that Hotel Erwin be evacuated, decontaminated,

or disinfected" after several employees of the hotel tested positive for COVID-19. *Id.* at 782.

The Court of Appeal held in *Marina Pacific* that "[a]ssuming ... the truth of those allegations, even if improbable, absent judicially noticed facts irrefutably contradicting them, the insureds ha[d] unquestionably pleaded direct physical loss or damage to covered property within the definition articulated in *MRI Healthcare*—a distinct, demonstrable, physical alteration of the property." *Id.* at 787–90 (citing *MRI Healthcare Cir. of Glendale v. State Farm Gen. Ins. Co.*, 187 Cal.App.4th 766, 115 Cal. Rptr. 3d 27, 37–38 (2010)). The court acknowledged that *United Talent Agency* was "[n]ot distinguishable" but maintained that the court there improperly disregarded the insured's factual allegations as improbable when evaluating the insurer's demurrer. *Id.* at 790.

On appeal, Another Planet highlights this split in authority and urges us to adopt *Marina Pacific's* holding because *United Talent Agency* "misapplied California law by making factual conclusions contrary to those alleged in the operative complaint." Vigilant disagrees, arguing that we should follow *United Talent Agency* because *Marina Pacific* "is an outlier decision at odds with an overwhelming body of precedent." Vigilant contends that *Marina Pacific* "gave short shrift" to the court's ability to "consider common-sense realities at the demurrer stage."

The answer to this question "could determine the outcome of [this] matter," Cal. R. Ct. 8.548(b)(4), because if the allegation of the presence or potential presence of the COVID-19 virus is sufficient to show "direct physical loss or damage to property," the district court erred in dismissing Another Planet's complaint for failure to state a claim, and we would remand to the district court for further proceedings. Alternatively, if the allegation is not sufficient, we would affirm the district court.

III

[2] In light of the foregoing discussion, and because the answer to this question "could determine the outcome of a matter pending in [this] court," Cal. R. Ct. 8.548(a), we respectfully certify to the California Supreme Court the following 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?

We do not intend our framing of this question to restrict the California Supreme Court's consideration of any issues that it determines are relevant. If the California Supreme Court decides to consider the certified question, it may in its discretion reformulate the question. *Broad v. Mannesmann Anlagenbau AG*, 196 F.3d 1075, 1076 (9th Cir. 1999). We will accept the California Supreme Court's decision on this question. See Cal. R. Ct. 8.548(b)(2).

If the California Supreme Court accepts review of the certified question, we designate Appellant Another Planet Entertainment, LLC as the petitioner pursuant to California Rule of Court 8.548(b)(1).

*4 The clerk of our court is hereby ordered to transmit forthwith to the California Supreme Court, under official seal of the United States Court of Appeals for the Ninth Circuit, a copy of this order and all relevant briefs and excerpts of record, along with a certificate of service on the parties. Cal. R. Ct. 8.548(c), (d).

Further proceedings in our court are stayed pending the California Supreme Court's decision on whether it will accept review, and if so, receipt of the answer to the certified question. This case is withdrawn from submission until further order from this court. The Clerk is directed to administratively close this docket, pending further order.

The panel will resume control and jurisdiction on the certified question upon receiving an answer to the certified question or upon the California Supreme Court's decision to decline to answer the certified question. Within 10 days after the California Supreme Court decides whether or not to accept the certified question, the parties shall file a joint report informing this court of the decision. If the California Supreme Court accepts the certified question, the parties shall file a joint status report every six months after the date of the acceptance, or more frequently if circumstances warrant.

It is so **ORDERED**.

All Citations

--- F.4th ----, 2022 WL 17972557, 2022 Daily Journal D.A.R. 13,015