

United States House of Representatives  
Committee on Financial Services  
2128 Rayburn House Office Building  
Washington, D.C. 20515

November 16, 2020

## Memorandum

**To:** Members, Committee on Financial Services

**From:** FSC Majority Staff

**Subject:** November 19, 2020, HCDC Subcommittee hearing entitled, “Insuring against a Pandemic: Challenges and Solutions for Policyholders and Insurers”

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The Subcommittee on Housing, Community Development and Insurance will hold a hearing entitled “Insuring against a Pandemic: Challenges and Solutions for Policyholders and Insurers” on Thursday, November 19, 2020 at 10:00 a.m. EST, on the virtual meeting platform Cisco Webex. This hearing will have one panel with five witnesses:

- **Ann Cantrell**, Owner, Annie’s Blue Ribbon General Store, on behalf of the National Retail Federation
- **John Doyle**, President & Chief Executive Officer, Marsh
- **Brian Kuhlmann**, Chief Corporate Counsel, Shelter Insurance, on behalf of APCIA and NAMIC
- **Michelle Menendez McLaughlin**, Chief Underwriting Officer, Chubb North America
- **R.J. Lehmann**, Executive Editor and Senior Fellow, International Center for Law and Economics

### Insurance Coverage for Pandemic Related Losses

In response to the COVID-19 pandemic, state and local officials across the country issued stay at home orders, shutting down businesses for weeks and months at a time. These shutdowns have resulted in enormous losses for businesses across the country; the American Property and Casualty Insurance Association (APCIA) estimated that losses just for businesses with under 100 employees during the pandemic in the spring were as much as \$431 billion per month.<sup>1</sup> However, when businesses looked to insurers to cover these losses under business interruption policies, many were told that such losses were specifically excluded or otherwise not covered by those policies. A string of lawsuits have been filed by businesses challenging claim denials.<sup>2</sup>

There have been far fewer questions as to whether event cancellation policies would be paying out due to pandemic related cancellations, which include major sporting events, concerts, festivals, and conferences. For example, the estimated cost to insurers of cancelling the 2020 Summer Olympic Games in Tokyo is \$2 billion, though postponement rather than cancellation will likely prevent the worst-case

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<sup>1</sup> “Legal and Regulatory Developments—Business Interruption Insurance for COVID-19 Related Losses,” *JD Supra*, (May 7, 2020), <https://www.jdsupra.com/legalnews/legal-and-regulatory-developments-75994/>

<sup>2</sup> “The ongoing case for coverage,” *JD Supra*, (April 1, 2020), <https://www.jdsupra.com/legalnews/business-interruption-insurance-the-53920/>

scenario for insurers with hundreds of millions of dollars in exposure.<sup>3</sup> Another area of insurance that has encountered significant uncertainty in the context of a pandemic is workers compensation claims, with states taking a wide variety of actions to extend workers compensation protections to first responders, health workers, and in some cases, essential employees like grocery store workers.<sup>4</sup> Other aspects of the insurance industry have seen very different outcomes during the pandemic, however. After stay-at-home orders caused a steep decline in driving in March and April, a significant decline in auto accidents and insurance claims led many auto insurers to issue refunds and credits to policyholders.<sup>5</sup>

### **The Role of the Federal Government**

Consumers and businesses purchase insurance to protect against the risk of loss. In 1945, Congress passed the McCarran-Ferguson Act, which exempted the industry from federal regulation. As a result, insurance is largely regulated at the state level. The Dodd-Frank Wall Street Reform and Consumer Protection Act established the Federal Insurance Office (FIO) within the Department of the Treasury, which has the authority to “monitor the extent to which traditionally underserved communities and consumers have access to affordable non-health insurance products,” but does not have authority to issue regulations or preempt state laws beyond those that are not in compliance with international standards.<sup>6</sup> The National Association of Insurance Commissioners (NAIC) helps to coordinate regulation across states.<sup>7</sup> In May, the NAIC sought to inform state insurance regulators’ response to the COVID-19 pandemic by requesting information from insurers about their exposure to business interruption coverage.<sup>8</sup>

### **Business Interruption Coverage**

Most businesses carry commercial property insurance, which protects assets against physical risk such as fires or other damaging events.<sup>9</sup> Some businesses choose to supplement that coverage with business interruption or business income (BI) coverage, which is aimed at covering sustained profit losses from a forced closure.<sup>10</sup> Although comprehensive data is unavailable, the NAIC estimates that 30-40% of businesses carry some form of business interruption coverage,<sup>11</sup> and news reports indicate that many of those policies contain clauses specifically exempting “viral pandemics.”<sup>12</sup> These clauses began appearing in policies following the SARS outbreak in 2002,<sup>13</sup> and in 2006, the Insurance Services Office (ISO) issued a circular stipulating that commercial property policies should offer “no coverage

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<sup>3</sup> “Olympics delay, not cancellation, provides reprieve for insurers,” *Reuters*, (March 24, 2020), <https://www.reuters.com/article/health-coronavirus-olympics-insurance/olympics-delay-not-cancellation-provides-reprieve-for-insurers-idUSL8N2BH255>

<sup>4</sup> “COVID-19: Workers’ Compensation,” *National Conference of State Legislatures*, (May 13, 2020), <https://www.ncsl.org/research/labor-and-employment/covid-19-workers-compensation.aspx>

<sup>5</sup> “Auto accidents, insurance claims both down sharply as we stay off the road,” *Car and Driver*, (April 20, 2020), [caranddriver.com/news/a32201608/auto-accidents-insurance-claims-down-coronavirus/](http://caranddriver.com/news/a32201608/auto-accidents-insurance-claims-down-coronavirus/)

<sup>6</sup> U.S. Department of the Treasury, [Federal Insurance Office](#)

<sup>7</sup> The National Association of Insurance Commissioners, [About](#)

<sup>8</sup> “COVID-19 Property/Casualty Data Call,” *National Association of Insurance Commissioners*, [https://content.naic.org/index\\_about.htm](https://content.naic.org/index_about.htm)

<sup>9</sup> “Business Interruption Insurance and COVID-19,” *Congressional Research Service*, (March 31, 2020), <https://www.everycrsreport.com/reports/IN11295.html>

<sup>10</sup> *Ibid.*

<sup>11</sup> “Re: May 21 Small Business Committee hearing,” *National Association of Insurance Commissioners*, (May 20, 2020), [https://naic.org/documents/government\\_relations\\_200521.pdf](https://naic.org/documents/government_relations_200521.pdf)

<sup>12</sup> “Insurers Knew the Damages Pandemics Could Wreak on Businesses. So they Excluded Them,” *Washington Post*, (April 2, 2020), <https://www.washingtonpost.com/business/2020/04/02/insurers-knew-damage-viral-pandemic-could-wreak-businesses-so-they-excluded-coverage/>

<sup>13</sup> *Ibid.*

for loss or damage caused by or resulting from any virus, bacterium or other microorganism that induces or is capable of inducing physical distress, illness or disease.”<sup>14</sup>

Insurance companies have argued that even without these specific exemptions, BI policies are simply not designed to cover pandemic risks because policyholders must demonstrate direct physical property damage. Case law is split on this question, however. For instance, one 2010 case found that even though a business’ premises suffered from mold and bacteria, the claimant did not meet its burden of proof for coverage because the entire building did not need to be evacuated.<sup>15</sup> Another 2018 court ruling affirmed the insurance industry’s interpretation by finding that a business that was disrupted and inconvenienced by nearby roadwork did not qualify for business income coverage because the disruption did not cause “direct physical loss” to the property.<sup>16</sup> Conversely, the New Hampshire Supreme Court has ruled that “direct physical loss” need not refer to direct physical damage.<sup>17</sup> Although the physical damage from the virus has not generally risen to the level of property damage required by some court rulings, some local officials, such as New York City Mayor Bill De Blasio, have directly referenced “physical losses” caused by the virus in stay at home orders.<sup>18</sup> Business interruption cases have been the subject of extensive litigation internationally as well, and recent rulings in the United Kingdom have required insurers to offer coverage despite references to exemptions for certain diseases.<sup>19</sup>

Through the Coronavirus Aid, Relief, and Economic Security (CARES) Act, Congress approved a Paycheck Protection Program (PPP) to provide forgivable loans to businesses affected by the COVID-19 pandemic. Within two weeks of the PPP’s initiation, the \$349 billion approved by CARES Act had been exhausted, and Congress approved additional funding to ensure the PPP’s continuation.<sup>20</sup> Although the PPP has helped many businesses meet their payroll, utility, mortgage, and rent costs amid the economic recession caused by COVID-19, businesses have not used the program to recoup losses caused by sustained, involuntarily closure. Data released by the NAIC in July found that over 184,000 businesses had made a claim related to COVID-19, but over 99% of those claims remained unpaid.<sup>21</sup>

### **State and Federal Policy Proposals Regarding Business Interruption Coverage**

The Insurance Information Industry along with other insurance industry trade groups have contended that global pandemics are “uninsurable,” and that “retroactive payouts would bankrupt

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<sup>14</sup> “New endorsements filed to address exclusion of loss due to virus or bacteria,” *Insurance Services Office*, (July 6, 2006), <https://www.propertyinsurancecoveragelaw.com/files/2020/03/ISO-Circular-LI-CF-2006-175-Virus.pdf>

<sup>15</sup> *Universal Image Productions, Inc. v. Chubb Corp.*, 703 F.Supp.2d 705, 710 (E.D. Mich. 2010)

<sup>16</sup> “Business Interruption Coverage In Light of COVID-19,” *Kelley Kronenberg*, (May 4, 2020), <https://www.kelleykronenberg.com/business-interruption-coverage-in-light-of-covid-19/>

<sup>17</sup> *Ibid.*

<sup>18</sup> “Emergency Executive Order No. 101,” *Office of the Mayor of New York*, (March 17, 2020), <https://www1.nyc.gov/assets/home/downloads/pdf/executive-orders/2020/eo-101.pdf>

<sup>19</sup> “UK Ruling a ‘Significant Step’ Toward Certainty for COVID-19 Business Interruption Claims,” *McGuire Woods*, September 21, 2020, <https://www.mcguirewoods.com/client-resources/Alerts/2020/9/uk-ruling-covid-19-business-interruption-claims>

<sup>20</sup> “Where Have the Paycheck Protection Loans Gone So Far,” *Federal Reserve Bank of New York*, (May 6, 2020), <https://libertystreeteconomics.newyorkfed.org/2020/05/where-have-the-paycheck-protection-loans-gone-so-far.html>

<sup>21</sup> “COVID-19 Property and Casualty Insurance Business Interruption Data Call,” *National Association of Insurance Commissioners*, July 2020, <https://content.naic.org/sites/default/files/inline-files/Claims2.pdf>

insurers.”<sup>22</sup> One analysis found that just two months of retroactive coverage on COVID-19 business interruption claims would cause total capital across US-based insurers and reinsurers to decline by as much as 50%.<sup>23</sup> Despite the massive scope of such payouts, legislation has been introduced in ten states.<sup>24</sup> On April 14, Rep. Mike Thompson (D-CA) introduced the Business Interruption Coverage Act, which prohibits insurance claim denials in the case of major events such as the COVID-19 pandemic.<sup>25</sup> The National Council of Insurance Legislators (NCOIL) has taken the position that any state legislation that retroactively adjusts contracts would violate the Contracts Clause found in Article I of the Constitution.<sup>26</sup>

One solution being considered for more immediate relief is modeled after the Victims Compensation Fund (VCF) created by Congress following the 9/11 terrorist attacks.<sup>27</sup> The VCF required setting up a process for adjudication, administered by a special master, and has paid out more than \$5.5 billion since its establishment.<sup>28</sup> Although the NCOIL has written in support of an approach modeled after the VCF, they do not favor the VCF’s claims adjustment process, and instead have suggested an approach that builds on existing insurance industry infrastructure for processing claims.<sup>29</sup>

On May 21, the insurance industry released a plan for addressing global events like pandemics. The Business Continuity Protection Plan (BCPP) would give businesses the option of purchasing revenue replacement insurance that would automatically pay out up to 80% of their revenue following an emergency declaration by the president. Under the BCPP, participating insurers would collect fees, although the payment of claims would be administered by the Federal Emergency Management Agency.<sup>30</sup> Although the major insurance industry trade groups support the BCPP, some insurers have offered alternatives. For instance, Chubb has released a proposal that would split pandemic risk between the government and industry, with insurers guaranteeing fast reimbursements for payroll expenses to small businesses up to \$60 billion, and the government assuming more traditional business interruption insurance for larger businesses, at up to \$1.1 trillion in exposure.<sup>31</sup>

Rep. Carolyn Maloney has also introduced H.R. 7011, the Pandemic Risk Insurance Act (PRIA), modeled after the Terrorism Risk Insurance Act (TRIA) passed after the September 11<sup>th</sup> attacks. Like TRIA, H.R. 7011 would create a federal backstop for businesses that experience losses and events that are

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<sup>22</sup> “Understanding Business Industry Insurance and Pandemics,” *Insurance Information Institute*, (April 13, 2020), [https://www.iii.org/sites/default/files/docs/pdf/business\\_interruption\\_101\\_041320\\_2.pdf](https://www.iii.org/sites/default/files/docs/pdf/business_interruption_101_041320_2.pdf)

<sup>23</sup> “Two Months of Retroactive Business Interruption Coverage Could Wipe Out Half of Insurers’ Coverage,” *AM Best*, (May 5, 2020), <http://news.ambest.com/presscontent.aspx?refnum=29325&altsrc=9>

<sup>24</sup> “Business Interruption/Business Owner’s Policies,” *National Association of Insurance Commissioners*, (November 11, 2020), [https://content.naic.org/cipr\\_topics/topic\\_business\\_interruptionbusinessowners\\_policies\\_bop.htm](https://content.naic.org/cipr_topics/topic_business_interruptionbusinessowners_policies_bop.htm)

<sup>25</sup> “Thompson Introduces the Business Interruption Coverage Act,” *Rep. Mike Thompson*, (April 14, 2020), [https://mikethompson.house.gov/newsroom/press-releases/thompson-introduces-the-business-interruption-insurance-coverage-act#:~:text=Mike%20Thompson%20\(CA%2D05\),safety%20power%20shutoffs%20or%20evacuations.](https://mikethompson.house.gov/newsroom/press-releases/thompson-introduces-the-business-interruption-insurance-coverage-act#:~:text=Mike%20Thompson%20(CA%2D05),safety%20power%20shutoffs%20or%20evacuations.)

<sup>26</sup> “Business Interruption Insurance and Coronavirus,” *National Council of Insurance Legislators*, (March 25, 2020), <https://us.eversheds-sutherland.com/portalsresource/TC-ML-letter-to-Congress-re-COVID-3-25-2020.pdf>

<sup>27</sup> “The September 11th Victim Compensation Fund,” *Congressional Research Service*, (October 17, 2019), <https://www.crs.gov/Reports/R45969?source=search&guid=2ef232df64af4cf1ad904ac984ab3ceb&index=1>

<sup>28</sup> *Ibid.*

<sup>29</sup> “Business Interruption Insurance and Coronavirus,” *National Council of Insurance Legislators*, (March 25, 2020), <https://us.eversheds-sutherland.com/portalsresource/TC-ML-letter-to-Congress-re-COVID-3-25-2020.pdf>

<sup>30</sup> “Insurance Trades Unveil Federal Pandemic Solution,” *NAMIC, APCA, and the BIG I*, (May 21, 2020), [https://www.iamagazine.com/docs/default-source/pdfs/joint-industry-press-release-5-21-2020afd9d0d5cc254e3592bf8b52f0a32def.pdf?sfvrsn=1fe182da\\_0](https://www.iamagazine.com/docs/default-source/pdfs/joint-industry-press-release-5-21-2020afd9d0d5cc254e3592bf8b52f0a32def.pdf?sfvrsn=1fe182da_0)

<sup>31</sup> “U.S. Industry Rifts Deepen Over Pandemic Cover,” *Financial Times*, 7.9.2020, <https://www.ft.com/content/4d7249eb-efa5-4b51-86ec-fe36a1467185>

canceled following a pandemic. Participation by insurers would be optional, and the total for federal aggregate compensation would be capped at \$750 billion annually.

### **Legislation**

- **H.R. 7011, the Pandemic Risk Insurance Act (Maloney)** establishes the Pandemic Risk Insurance Program to create a federal backstop for businesses that experience losses and events that are canceled following a pandemic.
- **H.R. \_\_\_\_\_. (Discussion Draft)** directs the Treasury Department's Federal Insurance Office to study the extent and availability of business interruption coverage, including claims and losses that occurred to businesses during the COVID-19 pandemic.