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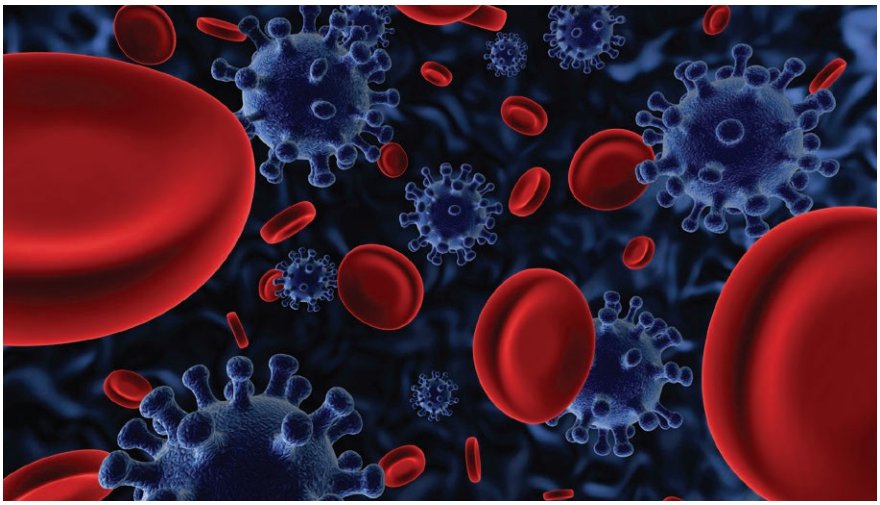
BKCG
BURKHALTER KESSLER CLEMENT & GEORGE LLP

Is There Coverage For The Financial Losses To Your Business Due To COVID-19?

The events of today bring much uncertainty and unanticipated change to all of our lives and businesses. While there is no doubt that we will persevere, the financial cost associated with this interruption is likely to be staggering. It is in times like these when many businesses will turn to their insurers to help mitigate the financial losses caused by the virus and associated shutdowns.

This bulletin is written to assist you in understanding your first party property insurance policy and whether your business may have coverage due to the COVID-19 pandemic. A few of the issues you want to consider is whether your claim falls within the insuring provision, whether a governmental order that shuts down your business triggers coverage, your business interruption loss due to the mandated closures, and whether your policy excludes coverage for damage caused by or resulting from a virus.

BKCG is ready and available to assist your business as you navigate through these difficult and uncertain times.



Is There Coverage For The Financial Losses To Your Business Due To COVID-19?

On March 11, 2020, the World Health Organization ("WHO") declared that the worldwide outbreak of the COVID-19 virus is now officially a pandemic. The WHO and U.S. health experts anticipate a significant increase in the number of reported COVID-19 cases over the next several weeks. Consequently, businesses have cancelled events. Other businesses have sent workers home. The impact on the service sector and the halting of the production of some goods is severe. In certain areas, there have been forced closures of restaurants, bars, and businesses.

Many factories throughout Asia and Europe have been shut down meaning products that U.S. businesses depend on cannot be supplied. These cancellations and shutdowns have serious economic consequences for many businesses as business income is lost and expenses will have to be incurred to clean and sanitize property. This raises an issue of whether a business has any avenue under its business property insurance policy to help recover these financial losses.

Below we discuss certain coverage issues that you should be aware of when contemplating whether to make a claim under your first party property policy. Please keep in mind that we are simply identifying issues for you to consider. A review of the specifics of your policy would be required to provide you with any coverage advice for your particular claim.

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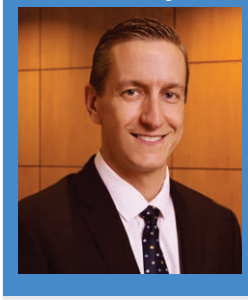
Refinement Of Joint Employer Rule May Spell Relief To California Franchisors

On January 12, 2020, the United States Department of Labor finalized its makeover of the joint employer rule, which should substantially narrow the joint employer definition and add clarity about the circumstances under which a franchisor and a franchisee could be considered joint employers of the same person. The new rule, which goes into effect on March 16, 2020, is important to franchisor-franchisee relationships, portfolio member companies and employers that often rely on staffing agency services.

Under the new rule, a person or entity will be considered a joint employer if the person or entity is "acting directly or indirectly in the interest of an employer in relation to the employee." The new rule provides relief for employers for many reasons. First, the mere reservation of rights to supervise or control an employee's condition of employment no longer means that the party is a joint employer.

Second, the party must actually exercise control over some facets of the employee's work. Third, simply maintaining employment records for an employee will not be enough, by itself, to render a party a joint employer.

The recent change in the rule follows a long-awaited decision from the NLRB, in which it ultimately found that McDonald's is not a joint employer with its franchisees. Industry experts believe that the revised and clarified definition will lead to lower costs and greater growth for the franchise industry.



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The Insuring Provision

The insuring provision of the property policy contains a requirement that there be "direct physical loss or damage" to the covered property. "Direct physical loss or damage" essentially means some type of damage having a material existence and perceptible through the senses. Even if the damage occurs on a microscopic level, it is sufficient to constitute "physical loss or damage." This issue has been litigated in a variety of contexts. See *Western Fire Ins. Co. v. First Presbyterian Church* (1968) 165 Colo. 34 (where court held there was direct physical loss when gasoline vapors penetrated the foundation of an insured church and accumulated, rendering the building uninhabitable); *Matzner v. Seaco Ins. Co.* 1998 WL 566658 (Mass.Super.1998) (where court held that carbon monoxide levels in an apartment building sufficient to render the building uninhabitable constituted a "direct physical loss"); and *Farmers Ins. Co. of Oregon v. Truitanich* (1993) 123 Or.App. 6 (where court held that an odor from methamphetamine "cooking" constituted direct physical loss to a house). While there are courts that take a narrower view of the "direct physical loss or damage requirement" and look for more tangible and visual evidence of damage, courts tend to read the insuring provision more broadly when the claimed damage concerns food, medicine, and health/life safety issues.

In the context of COVID-19, an insured may be required to incur expenses to clean and sanitize its property due to the presence of the virus. In that situation, the insured would have the initial burden to show the existence of the virus on the surfaces of the property. This can be done through an expert or even possibly by demonstrating that a person such as an employee who tested positive for COVID-19 was at the property thereby necessitating the cleaning of the premises.

Civil Authority

Many policies contain what is known as "Civil Authority" coverage. In a nutshell, civil authority is an order by the government to shut down or to stay away from a certain area. To trigger coverage, there are typically four requirements: (1) an insured peril (2) that causes or results in (3) an order or action of civil or military authority (4) during which access to or ingress/egress from real or personal property was impaired, inhibited or prevented to some extent. Regional – and in this case, worldwide – catastrophes implicate this coverage. For instance, although a business may not have sustained any physical loss or damage to its own property, a business may nevertheless claim to have sustained business interruption as a result of some restriction or access to its property. The catastrophe generates government directives impacting access to business that may not be damaged or otherwise directly affected by the peril. As seen with catastrophes such as 9/11 and the Southern California wildfires, governmental bodies will issue declarations and orders restricting vehicular traffic, impose curfews, cordon off areas, and issue warnings to keep away from certain areas.

With COVID-19, most claims will likely center on whether there is an insured peril and whether there has been an "order" or "action" of civil authority. The insured peril question can only be resolved through an analysis of your policy language. If your policy provides coverage for damage caused by a "virus," then civil authority is more likely.

The issue of whether there has been an "order" or "action" of civil authority will be decided on an area by area basis unless the Federal Government issues a mandatory nationwide quarantine. For instance, the six Bay Area counties announced a "shelter in place" order for all residents directing everyone to stay inside their homes and away from others as much as possible for the next three weeks. The result is that bars, restaurants, fitness centers, and other businesses will be closed. Most likely, this will be considered to be an order or action of civil authority that will trigger coverage. Orange County took a less drastic measure and issued an order effective March 17, 2020, officially closing all non-essential public and private gatherings outside a household. There were exceptions for "essential activities" that are specifically set forth in the order. If your business is closed as a result of the Orange County order, there is a likelihood that it could trigger civil authority coverage. Still, other counties have not issued an official order. If an order is not issued in those counties, civil authority coverage is less likely.

Business Interruption And Contingent Business Interruption

To the extent that you have sustained property damage or have been impacted by an order of civil authority, business interruption coverage very well may be triggered. The purpose and nature of Business Interruption ("BI") insurance is to indemnify the insured for any loss sustained by the insured because of its inability to continue to use the business property. To trigger business interruption, there must be: (1) physical loss or damage (2) to covered property (3) by a covered peril (4) that causes a necessary suspension of operations to the business (5) which, in turn, results in lost income or extra expense. Indemnity is for the period of time to repair the covered damage plus any additional extended period provided in your policy.

Contingent Business Interruption ("CBI") is for instances where your business depends on obtaining products from a supplier or you have customers whose business is temporarily halted so they cannot purchase from you. CBI coverage is generally triggered by a covered loss to a customers' or supplier's property or to property on which the insured company depends on to attract customers. Indemnity is provided for the interruption in your customer's business caused by a covered event ***at your supplier's or customer's property***. Suppose your supplier of microchips is located in Milan, Italy and had its operations interrupted due to a covered event. In turn, you may be compelled to also suspend your production because you no longer can obtain the microchips needed for your product or you can only receive a reduced allocation of the microchips. In that instance, you will suffer a CBI loss and your business interruption loss should be covered in order to make you whole.

Both BI and CBI are triggered when there is a covered peril that causes damage. Whether COVID-19 is a covered peril depends on your policy language.

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Force Majeure – The Law's Answer To Some Of The Business Challenges Posed By The Coronavirus

On January 30, 2020 the World Health Organization (WHO) declared the Coronavirus (or Covid-19) a public health emergency of international concern. More recently on March 11, 2020, the WHO declared the virus a pandemic, which the Centers for Disease Control and Prevention generally defines as an epidemic that has spread over several countries or continents, usually affecting a large number of people.

The virus has already caused worldwide economic disruption and businesses will likely experience more disruption, especially if the virus continues to spread. Businesses may, and some already undoubtedly have, find themselves in the unenviable position of being unable to perform their contractual obligations because the Coronavirus makes performance impossible. Consider for example a scenario in which a company that contracted to sell certain goods is literally unable to deliver them because a government shut down shipping lanes due to the virus. As another example, one can also envision a circumstance in which a company contractually obligated to manufacture certain goods cannot do so because the virus sickened too many of its employees. There are countless scenarios in which this pandemic could prevent a business from performing under a contract due to no real fault of that business. Can businesses protect themselves from this type of legal problem?

Fortunately, the answer generally is yes. A force majeure clause in a contract may provide protection if a party cannot meet its contractual obligations due to effects from the Coronavirus. Force majeure clauses typically include language like: "Neither party shall be liable for any delays or failures in performance resulting from extraordinary occurrences beyond the control of the party seeking to be excused, including, without limitation, acts of God, acts of war or terrorism, civil unrest, riots, or disasters." Of course, the specific language in any given force majeure clause may differ, but the usual intent of such a clause is to excuse a party's performance if an unforeseeable and extraordinary event renders performance impossible. For contracts involving the sale of commercial goods, the California Commercial Code generally allows a party to assert a defense based on force majeure, even if the contract omits an express force majeure clause.

If your company is unable to perform its contractual obligations due to the Coronavirus, a force majeure provision may assist you. Moreover, this unfortunate pandemic serves as a good reminder that it is important to include these types of clauses in commercial contracts in the future. If you have any questions regarding force majeure provisions, you should consult with a BKCG attorney.

Please contact Josh Waldman at jwaldman@bkcglaw.com or call (949) 975-7500 if you have any questions about any issue discussed in this article, or any other related matter.

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Contamination and Pollution Exclusion

Most first party property policies are called "all-risk" policies but the name is a bit of a misnomer. Not all events are covered. Instead, coverage is provided for damage due to all causes UNLESS there is an applicable exclusion. If an exclusion applies, there will be no coverage for your property damage, BI, or CBI losses. Consequently, the policy language and the interpretation of any exclusion is extremely important.

COVID-19 presents an issue of whether a "virus" is an excluded peril. While each policy must be reviewed in its entirety, if a "virus" were to be excluded it would most likely be wrapped up in the "contamination and pollution" exclusion or, possibly, in a separate endorsement that expressly excludes viruses. Very often, a policy that excludes contamination and pollution specifically defines the term "pollutant" as an irritant or contaminant, whether in solid, liquid, or gaseous form, including smoke, vapor, soot, fumes, acids, alkalis, chemicals, and waste. The term "contaminant" is oftentimes not defined.

While there is plenty of case law interpreting the pollution and contamination exclusion, there is no consensus as to whether a virus is a "pollutant" or "contaminant." In fact, there are cases where courts have held that a virus is not a pollutant because it found the policy language ambiguous. *Johnson v. Clarendon National Insurance Co.*, 2009 WL2524619; *Westport Insurance Corp. v VN Hotel Group*, LLC 761 F. Supp. 2d 1337. You should review the specific terms of your policy with your broker to determine whether your policy specifically excludes damage caused by or resulting from a "virus" or whether the language is not clear.

Have Your Policy Reviewed

These are difficult and uncertain times for all of us. Undoubtedly, many businesses are going to be financially hurt because of forced closures due to COVID-19 and governmental shut down orders. In the event your business sustains a loss due to a closure, it is important to review your policy to see whether your property policy can provide indemnity.

BKCG is ready and available to assist you in analyzing your insurance coverage and determining whether you have a claim for your business losses. Please call or email us for more information or for a review of your policy.

Please contact Keith Butler at kbutler@bkcglaw.com or call (949) 975-7500 if you have any questions about any issue discussed in this article, or any other related matter.

New Important Changes To California's Fair Employment And Housing Act (FEHA) Became Effective On January 1, 2020.

The California legislature passed new employment laws effective January 1, 2020 that expanded protections for California employees from workplace harassment, discrimination and retaliation. Although many believe that the "me too" movement motivated these new laws, the legislation actually goes far beyond providing additional protection to women asserting sexual harassment/ gender discrimination claims.

One of the most significant new laws is a substantial lengthening of the statute of limitations for claims for unlawful discrimination, harassment and retaliation. Prior to January 1, 2020, California law generally afforded an employee only one-year from the occurrence of the unlawful discrimination, harassment and/or retaliation to file a complaint with the California Department of Fair Employment and Housing (DFEH). If an employee failed to file her complaint within this time period, employers could usually defeat the case fairly early in the litigation process. Because this one-year period was a relatively short statute of limitations as compared to the applicable limitations period for most other types of civil claims (i.e., breach of contract - 2 or 4 years, fraud – generally 3 years), the statute of limitations defense constituted a common defense that employers frequently relied upon. However, the new law extends the one-year deadline to three years from the date of the unlawful occurrence. Defense lawyers anticipate that their successful use of the statute of limitations defense will be far less common in these FEHA claims due to the legislature's three-fold lengthening of the limitations period.

Another major change that employers should be aware of is that California law expanded protections under the FEHA to prohibit discrimination and harassment based on a person's natural hairstyle. The California legislature recognized that employer grooming policies that prohibited natural hair, such as afros, braids and locks, disproportionately impacted black employees and applicants. As such, the legislature concluded that these policies, as well as discrimination/harassment based on an employee's natural hairstyle, tended to have a disparate impact on African Americans. To remediate this concern, the new law bars employers from implementing or enforcing policies or dress codes that prohibit or limit a person's natural hairstyle, and prohibits all other form of discrimination or harassment due to an employee's natural hairstyle.

If you have any questions regarding the foregoing changes in the law, or related to any other employment matters, you should contact your attorney.

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What You Should Know About The "Business-To-Business" Exception To California's New Independent Contractor Law

As most businesses in California are now aware, as a result of Assembly Bill 5 (better known as "AB5"), a new law came into effect on January 1, 2020, which has drastically altered the legal landscape in terms of who can now qualify as an independent contractor of a business, rather than an employee. The new law, codified as Section 2750.3 of the California Labor Code, has established a default "ABC" test, mandating that a person providing labor or services for remuneration shall be considered an employee rather than an independent contractor unless the hiring entity demonstrates that all of the following conditions are satisfied:[1]

(A) The person is free from the control and direction of the hiring entity in connection with the performance of the work, both under the contract for the performance of the work and in fact;

(B) The person performs work that is outside the usual course of the hiring entity's business; and

(C) The person is customarily engaged in an independently established trade, occupation or business of the same nature as that involved in the work performed.

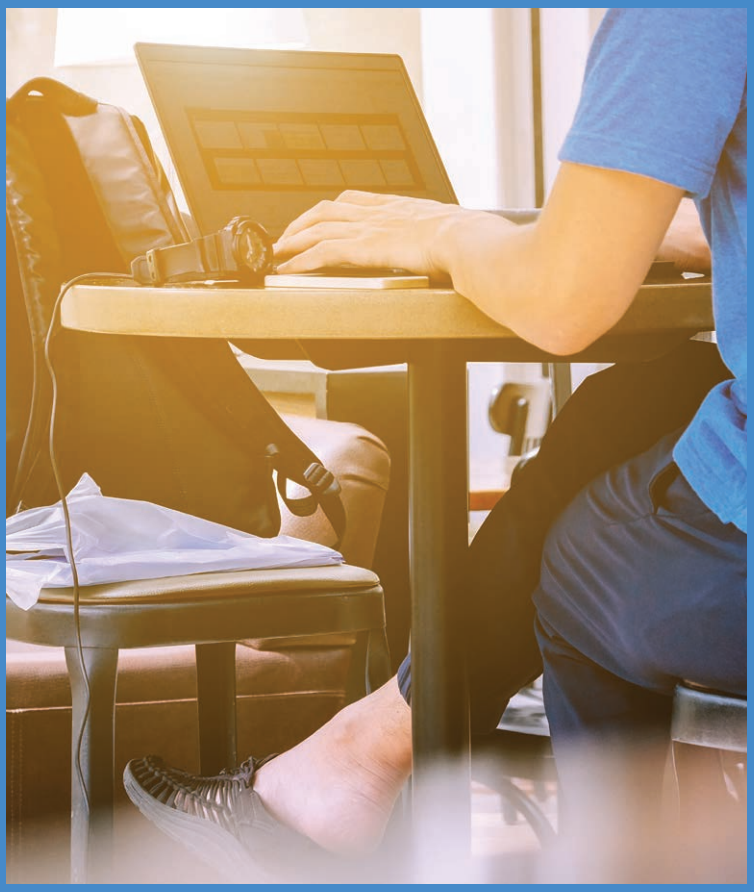
The most troublesome of these tests for most businesses is the (B) test, since many businesses contract with other businesses, often on an ongoing, long-term basis, to provide them with services, as independent contractors, that are essential elements of their business (including outside sales agents), and would thus run afoul of the (B) test.

Thankfully, the new law provides a business-to-business exemption from the ABC test which still requires satisfaction of the Borello test mentioned in the footnote below, but which allows a business (the "contracting business") to use, as an independent contractor, another bona fide business (the "business service provider"), which must be set up as either a properly documented sole proprietorship, or a legal entity such as a limited liability company, corporation or partnership, to provide services that are within the usual course of the hiring entity's business. In order to qualify for this exception, however, all of the following 12 conditions must be met:[2] (continued on page 5)

[1]Tests (A) and (C) are broadly comparable to criteria which applied prior to the passage of AB5 under the Borello test which California used to determine whether someone was an independent contractor or not (see https://www.dir.ca.gov/dlse/faq_independentcontractor.htm, which also lists occupations excepted from the ABC test, as to which the Borello test still applies).

[2]See Labor Code §2750.3(e), paraphrased in part in this article.

What You Should Know About The "Business-To-Business" Exception To California's New Independent Contractor Law (continued from page 4)



1. The business service provider is free from the control and direction of the contracting business entity in connection with the performance of the work, both under the contract for the performance of the work and in fact.

2. The business service provider is providing services directly to the contracting business rather than to customers of the contracting business.

3. The contract with the business service provider is in writing.

4. If the work is performed in a jurisdiction that requires the business service provider to have a business license or business tax registration, the business service provider has the required business license or business tax registration.

5. The business service provider maintains a business location that is separate from the business or work location of the contracting business.

6. The business service provider is customarily engaged in an independently established business of the same nature as that involved in the work performed.

7. The business service provider actually contracts with other businesses to provide the same or similar services and maintains a clientele without restrictions from the hiring entity.

8. The business service provider advertises and holds itself out to the public as available to provide the same or similar services.

9. The business service provider provides its own tools, vehicles, and equipment to perform the services.

10. The business service provider can negotiate its own rates.

11. Consistent with the nature of the work, the business service provider can set its own hours and location of work.

12. The business service provider cannot be an individual providing services for which a license from the Contractor's State License Board is required.

As with any new law, only in time will we get a clear understanding of how the courts, the Employment Development Department and the Labor Commissioner, to mention just a few relevant parties, will interpret these twelve criteria. For example:

- How closely will the business service provider's ability to negotiate its own rates be examined? What if the parties negotiate but the contracting business never budges from its initially proposed rates?

- What if a particular project must, for logistical reasons, be performed by the business service provider at a specific time and place set by the contracting business?

- What if the business service provider has three clients, suddenly loses two of them and tries hard but fails to procure replacement clients for a period of several months, leaving it with only one client? At what point must the contracting business terminate the relationship?

- What if the nature of the services contracted for requires the use of highly-specialized, expensive equipment, that is owned by the contracting business? Must the service provider lease the equipment for the duration of the relationship?

- What if the business service provider lies to the contracting party about its compliance with any of the above criteria?

However, a few key points are clear. Many of these points are not so different from the situation that applied under the Borello test, but now there is little or no margin for error on the part of the contracting business if legal liability for employee misclassification is to be avoided.

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What You Should Know About The "Business-To-Business" Exception To California's New Independent Contractor Law (continued from page 5)

1. The days of the "dedicated" independent contractor, providing services to only one client - you - are over. The business service provider must have two or more clients and be actively marketing its services to the wider public. What that actually means in practice is still unclear, of course (is having a website alone sufficient, for example?).

2. It is essential that the contracting business initially verify, and periodically monitor or audit, the business service provider's ongoing compliance with each of the foregoing criteria. All of the legal risk falls on the contracting business if the legal requirements are not met. What's more, there is little, if any, legal downside to non-compliance from the service provider's perspective, so it is critical that the contracting business remain vigilant in order to avoid potentially bankruptcy-inducing liability for violating this law.

3. The written Independent Contractor Agreement should include corresponding representations and warranties from the service provider regarding compliance and require it to provide immediate notice to the contracting business if any of the 12 required legal criteria are no longer being met.

4. As a practical manner, the contracting business should insist – and confirm – that the business service provider is furnishing the contracted services only through its own bona fide employees, and not through the use of independent contractors. Ask to see their W-2s, redacted as appropriate, if need be.

5. The business service provider must be providing services to you, the contracting business, not to your customers. Some interaction with your customers is probably fine. But having the service provider directly furnish the same service (or a subset of such services) to your customers that you yourself would be typically providing to your customers through your own employees probably is not. As an example, if you are a general services accounting firm, you can't use an independent contractor to prepare your client's tax returns, but if your firm only normally performed audits, perhaps you could.

6. Do not fall into the "all of my competitors are still using independent contractors for this purpose, so I can, too" trap. Not every business owner understands the law (or even tries to), and many business owners are willing to take the legal risk of employee misclassification (often not understanding the sheer magnitude of the potential financial consequences) because they want to cut corners and try to save money on employee overhead costs. One claim alone could put you out of business.

This article is not intended to be a comprehensive study of the business-to-business exception to the new law, but merely to alert you to some of the most important things you will need to consider if you still wish to use independent contractors to provide services that are an inherent part of your business.

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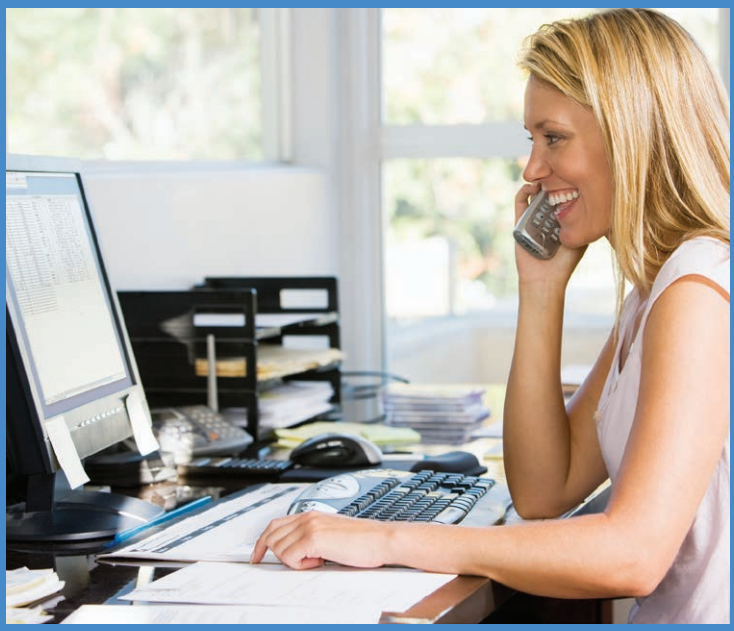

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