

ALERT

Does New Jersey's Efficient Proximate Cause Doctrine Overcome the Virus Exclusion?

By Robert D. Chesler, Nicholas M. Insua, and John P. Lacey, Jr.

Immediately following the initial outbreak of COVID-19, several insurance companies publicly declared that policyholders are not entitled to business interruption coverage if their property policies contain a virus exclusion. As a result, many policyholders have been discouraged by a virus exclusion in their property policies. The virus exclusion, however, may not be dispositive. In fact, for purposes of exclusions in property policies, New Jersey has adopted the efficient proximate cause doctrine. This doctrine states that the cause of a loss is either the first precipitating event or the final damage-inducing act. Applying this doctrine, policyholders have argued that while the precipitating cause of their loss may have been the coronavirus, the final act causing loss was the governmental order that closed down their businesses. Since the government order is the efficient proximate cause of the loss, the virus exclusion should not apply.

The New Jersey Supreme Court established the efficient proximate cause doctrine in *Auto Lenders Acceptance Corp. v. Gentilini Ford, Inc.*¹ There, an employee of the defendant had falsified credit information in connection with several automobile sales transactions. The court was tasked with determining whether a direct physical loss had occurred as result of the employee's dishonest acts. The court noted:

Where a peril specifically insured against sets other causes in motion which, in an unbroken sequence and connection between the act and final loss, produces the result for which recovery is sought, the insured peril is regarded as the proximate cause of the entire loss.... In other words, it has been held that recovery may be allowed where the insured risk was the last step in the chain of causation set in motion by an uninsured peril, or where the insured risk itself set into operation a chain of causation in which the last step may have been an excepted risk.²

Further, in *Simonetti v. Selective Ins. Co.*³ homeowners discovered mold growth in their home two months after a severe rainstorm. The insurance policy at issue contained a fungi exclusion, which, in relevant part, stated: "[w]e do not insure, however, for loss: [c]aused by . . . mold."⁴ The homeowner's argued that the mold was a direct physical loss to the home

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caused by water intrusion from the rain storm — a covered loss. The Appellate Division ultimately found there were genuine issues of material fact, and stated:

[T]he fact that two or more identifiable causes – one a covered event and one excluded – may contribute to a single property loss does not necessarily bar coverage . . . [a]nd with regard to sequential causes of loss, our courts have determined that an insured deserves coverage where the included cause of loss is either the first or last step in the chain of causation which leads to the loss.⁵

In a very recent case, *New Jersey Transit Corp. v. Certain Underwriters at Lloyd's London*⁶, the New Jersey Appellate Division applied the efficient proximate cause doctrine to find coverage for flooding caused by Superstorm Sandy. The flooding was the result of the windstorm. The insurance policy at issue contained a flood sublimit, which the insurance company contended reduced coverage. Regardless, the court found the claim was fully covered. Specifically, the court held that the efficient proximate cause of the loss was the windstorm and not the flooding, and determined the flood sublimit did not apply.

Many exclusions in property policies contain what is known as anti-concurrent language. An example of this language states:

We will not pay for loss or damage caused directly or indirectly by any of the following. Such loss or damage is excluded regardless of any other cause or event that contributes concurrently or in any sequence to the loss.

Some New Jersey courts have enforced this language to foreclose coverage when two causes — one covered and one excluded — contribute to a loss.⁷ Notably, the standard virus exclusion does not contain this language (although it can still appear in non-standard exclusions).

New Jersey law construes exclusions narrowly in favor of coverage. If the insurance company could have written an exclusion more clearly, the exclusion will be construed against the insurance company. The existence of the anti-concurrent language shows that the insurance companies could have written the virus exclusion so that it applied regardless of the efficient proximate clause language, but chose not to. This is a potent argument that the efficient proximate cause doctrine applies even if the virus and the lockdown order both contributed sequentially or concurrently to the loss.

Policyholders should not credit insurance industry propaganda that coverage does not exist for coronavirus business interruption claims. At the very least, every policyholder incurring a loss should promptly give notice of its claim to its insurance company in order



to avoid late notice issues. Once the insurance company denies coverage, the policyholder need not commit to coverage litigation immediately. The policyholder can await further litigation and statutory developments, being careful, though, to comply with statutory and contractual limitation periods for bringing claims against the insurance company.

As noted in our earlier alert, New Jersey has favorable law on the issue of whether loss of functionality constitutes property loss or damage. When combined with New Jersey's favorable law on efficient proximate cause, New Jersey may be a favored state for litigation regarding insurance coverage for COVID-19 business interruption claims. ▲

ENDNOTES

1 181 N.J. 245 (2004).

2 *Id.*, at 257 (quoting 5 John Alan Appleman, *Insurance Law & Practice*, § 3083, at 309–11 (1970)).

3 372 N.J. Super. 421 (App. Div. 2004).

4 *Id.*, at 426.

5 *Id.*, at 431.

6 461 N.J. Super. 440 (App. Div. 2019).

7 See e.g., *Zero Barnegat Bay, LLC v. Lexington Ins. Co.*, No. 14CV1716PGSDEA, 2019 WL 1242436 (D.N.J. Mar. 18, 2019).

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