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**PUBLIC HEARING TESTIMONY**

**REGARDING INSURANCE ISSUES and COVID-19**

**ON**

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**VIA**

**ONLINE PUBLIC VIDEO**

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**WRITTEN TESTIMONY OFFERED BY:**

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It was recommended by Insurance Committee Chair Kevin Cahill that we submit written testimony in lieu of in-person testimony in the interest of the limited time and format of this hearing. I want to thank all the committee members for the opportunity to weigh in on behalf of the New York Insurance Association (NYIA) about insurance issues and the COVID-19 pandemic. NYIA is the state trade association that has represented the property and casualty insurance industry in New York for more than 135 years. NYIA's membership is broad and diverse, consisting of stock, mutual and cooperative insurance companies writing in every county of New York State. At the outset, I would like to emphasize that many of NYIA's members are small businesses that have served their local communities for many years. In addition, the agents that represent our insurance companies and sell our products are Main Street businesses in your districts and collectively we provide vital services to your constituents and offer them financial security.

You should know that insurance companies have been providing assistance to their policyholders voluntarily during this unprecedented time. Insurers have been working with their customers for months to provide them with flexibility as far as payments, even before these types of measures were formalized by regulators. Companies have announced plans to provide relief to policyholders in the form of refunds, credits, or other types of givebacks. Insurance companies must file with the New York State Department of Financial Services for these reductions and have been working diligently with regulators to have these requests approved quickly so they can provide New Yorkers with monetary support.

We understand that today's hearing will cover a variety of topics but want to weigh in on some of the proposals that are being discussed. There are a few bills that have been

introduced that may sound like a solution, but in reality would only exacerbate the business climate, compounding an already difficult situation—specifically, S8211A (Gounardes)/A10226B (Carroll) and A10327 (Rosenthal, L). These bills purport to assist small businesses by rewriting insurance policies to mandate retroactive coverage of business interruption insurance for existing policies, despite no physical damage or loss is present or a virologic pandemic being excluded, up to the limits of the policy.

Looking to insurance companies to resolve a statewide, and indeed, not only national, but international pandemic crisis that was unforeseen by most, if not all, policymakers within the last year would have tremendously negative consequences for the property and casualty industry, their policyholders and the New York insurance marketplace. The National Association of Insurance Commissioners (NAIC), the collective body of insurance regulators across the country have stated that attempts to mandate retroactive business interruption coverage, as these bills would do, are misguided. The NAIC has recently stated:

Business interruption policies were generally not designed or priced to provide coverage against communicable diseases, such as COVID-19 and therefore include exclusions for that risk. Insurance works well and remains affordable when a relatively small number of claims are spread across a broader group, and therefore it is not typically well suited for a global pandemic where virtually every policyholder suffers significant losses at the same time for an extended period. While the U.S. insurance sector remains strong, if insurance companies are required to cover such claims, such an action would *create substantial solvency risks* for the sector, significantly undermine the ability of insurers to pay other types of claims, and potentially exacerbate the negative financial and economic impacts the country is currently experiencing.<sup>1</sup> (emphasis added)

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<sup>1</sup> [https://content.naic.org/article/statement\\_naic\\_statement\\_congressional\\_action\\_relating\\_covid\\_19.htm](https://content.naic.org/article/statement_naic_statement_congressional_action_relating_covid_19.htm)

In addition, the National Conference of Insurance Legislators, an organization of legislators serving on state insurance and financial institutions committees across the United States, has also weighed in with their grave concerns related to the issue of forcing business interruption insurance to provide coverage for COVID-19:

We understand that professionals and businesses will be facing unprecedented, dire economic challenges; however, we cannot compound the damage to the broader economy by forcing insurers to pay claims for which they did not contract. To do so could destabilize these insurers and render them unable to pay claims for which they did accept the risk, and did rate & reserve.<sup>2</sup> *This could jeopardize the solvency of any number of insurers.* (emphasis added)

As the NAIC and NCOIL state, this legislation is so onerous that it would put the solvency of the entire property and casualty insurance industry in New York at risk and they would not be able to pay for other covered perils for businessowners, homeowners and auto claims.

S8211A (Gounardes)/A10226B (Carroll) and A10327 (Rosenthal, L) propose to protect the solvency of property and casualty insurers, but it actually forces to provide coverage for a now known and expanding loss that insurers did not contract for, account for, price for, or otherwise underwrite, by “authorizing” (not requiring) the Superintendent of the Department of Financial Services (DFS) to assess a charge against all entities engaged in the business of insurance in New York State to reimburse property and casualty insurers who are mandated under these bills to provide retroactive business interruption coverage in policies that do not meet the terms of coverage. Even if the DFS Superintendent were inclined to assess such a charge against all property and casualty insurance companies, life

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<sup>2</sup> <http://ncoil.org/wp-content/uploads/2020/03/TC-ML-letter-to-Congress-re-COVID-3-25-2020.pdf>

insurers and health insurers (who themselves have had their own challenges with the COVID-19 pandemic crisis), it is doubtful that such a charge would avoid widespread insurer insolvency. It is estimated that the costs that bills such as those under consideration here would cost on a national basis approximately \$255-431 billion *per month* with estimated collected premiums on business interruption policies estimated at \$6 billion per month.<sup>3</sup> The foregoing figures are staggering, and even if not entirely limited to New York, the fact that New York has been the epicenter of the COVID-19 pandemic crisis suggests that the figures in New York will nevertheless be enormous. Furthermore, S8211A (Gounardes)/A10226B (Carroll) and A10327 (Rosenthal, L) do not contemplate whether business interruption was even purchased. The legislation goes as far as to state that any policy for loss or damage of property shall be construed to include coverage for business interruption due to the COVID-19 pandemic, even if the policy did not include any form of business interruption coverage.

Insurance companies are in the business of pricing risk. If the risk of pandemic could be priced, there would undoubtedly be a market for the coverage. However, the issue would then be the affordability of such coverage. It is impossible for insurance companies to provide coverage for a crisis that has the scope and magnitude of COVID-19. The situation is not geographically isolated, even to the United States, and it is not for a defined period of time. There have been suggestions that the industry has billions of dollars in reserves and these reserves should be utilized to pay for retroactive business interruption coverage. While the industry does possess significant reserves, the purpose of these reserves is to set aside money to pay for claims for which they have received premium. If a company

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<sup>3</sup> <https://us.milliman.com/en/insight/COVID-19-business-interruption-coverage-and-the-physical-loss-or-damage-requirement#1>. Furthermore, one of the entities listed in S8211A (Gounardes)/A10226B (Carroll) that could be required to pay a charge to offset business interruption losses are excess line insurers which are not subject to the authority of DFS in any event, and could not be required to pay such a charge.

underestimates their reserves, they will need access to capital or surplus. Insurers invest their capital to offset their combined loss ratio (cost of claims and operating expenses). If a company does not receive enough premium for their products or experience more claims than they have reserved for, they would operate at a loss unless they can make that up with investment returns. Various investment tools can help lower premiums and serve as a safety net should liabilities exceed reserves. Insurance companies have invested \$24 billion in New York municipal bonds alone. Suggesting that this money be diverted to pay for uncovered perils would ripple across the foundation of New York's economy.

The inevitable result of attempting to mandate retroactive business interruption coverage is that insurers would simply stop offering this product as the risk is uninsurable with the best-case scenario of the coverage being unaffordable for the average organization. This will only make it more difficult on small business owners to recover when other catastrophes strike such as hurricanes, winter storms, tornados, or wildfires.<sup>4</sup>

We understand that public officials are looking for solutions for their small business owner constituents. These efforts are well intentioned, but the impact of any proposal needs to be carefully weighed. In the instance of forcing business interruption insurance to cover losses from COVID-19, the impact would be devastating to the insurance industry. As New York City Council Member, Costa Constantinides, wrote in a letter to officials urgently requesting federal financial aid for small businesses:

These businesses are not asking for a handout, moreover. They simply want business interruption insurance to get them through until our society is able to return to normal. Unfortunately, their insurance providers are likely unable to cover all business losses incurred as the losses are so great that they may face insolvency

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<sup>4</sup> <https://www.wsj.com/articles/politicians-target-insurance-contracts-11585350279>

themselves. The last thing we need right now is to potentially bankrupt one industry to save another.<sup>5</sup>

In the terrible event that an insurance company becomes insolvent, it would compound this already challenging situation. This is because of how New York's Property/Casualty Security Fund operates. The fund is governed by Article 76 of the New York Insurance Law and is a backstop mechanism that protects policyholders by covering their claims if their insurer becomes insolvent. However, this backstop coverage comes at a significant cost to all New Yorkers. Whenever the guaranty fund's assets are depleted due to insurer insolvency, all property and casualty insurance companies are assessed to rebuild the fund's assets. This, of course, will impact premiums for all policyholders in New York as increased assessments represent an increase in the cost of business for insurance companies operating in New York. Consequently, these bills, were they to become law would represent a significant increase in the cost of living and doing business in New York as the cost of all property and casualty insurance policies, including those for home and auto, would increase to offset these losses. It is possible in this situation that the number of insolvencies created by forcing business interruption coverage could overwhelm the guaranty fund and result in the failure of the fund. The overarching implications of the proposals are profound and would wreak havoc on the entire property and casualty marketplace in New York.

Legislation such as S8211A (Gounardes)/A10226B (Carroll) and A10327 (Rosenthal, L) would, in effect, rewrite every existing business policy to include coverage which does not exist under the policy for small businesses with 250 or fewer employees. Business interruption insurance requires physical damage or physical loss to the property. If

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<sup>5</sup> <https://www.crainsnewyork.com/coronavirus/councilman-asks-feds-save-small-businesses-insurance-overrun>

the physical damage element is satisfied, then, and only then, can the ancillary coverage for the actions of civil authorities that limit access to, or use of, the property be triggered. It is unknown as a factual matter how a pathogen physically alters and damages property. In fact, courts have stated that in order to be damaged there “must be a distinct and demonstrable physical change to the property necessitating some remedial action to demonstrate physical loss or damage.”<sup>6</sup> Current judicial consensus is if the property can be easily cleaned or there is no physical alteration, then there is no physical damage. In the case of COVID-19 a virus, the threat of the pandemic or governmental action to ban or limit individuals from congregating, does not constitute physical damage or physical loss. Even were a court to find that a pathogen causes physical damage,<sup>7</sup> the pathogen or substance must be confirmed to be or have been on the premises in order to constitute physical damage.<sup>8</sup> It is unclear and entirely speculative to assume that in the case of COVID-19 that it is or has been physically present in all businesses that have been impacted by the pandemic crisis.

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<sup>6</sup> <https://us.milliman.com/en/insight/COVID-19-business-interruption-coverage-and-the-physical-loss-or-damage-requirement#4>. See also, <https://www.whiteandwilliams.com/resources-alerts-ISO-Excluded-Coronavirus-Coverage-15-Years-Ago.html>, citing, *Mama Jo’s, Inc. v. Sparta Ins. Co.*, 2018 U.S. Dist. LEXIS 201852 (S.D. Fla. Jun 11, 2018) (holding that restaurant did not sustain direct physical loss when dust and debris from nearby roadwork could be remediated by cleaning); *Mastellone v. Lightning Rod Mut. Ins. Co.*, 884 N.E.2d 1130 (Ohio Ct. App. 2008) (finding that mold which could be removed by cleaning was not physical damage, as it did not alter or otherwise affect the structural integrity of the building’s siding); *Universal Image Prods. v. Chubb Corp.*, 703 F. Supp. 2d 705 (E.D. Mich. 2010) (holding that intangible harms such as odors or the presence of mold and bacteria in an HVAC system did not constitute physical damage to property); *Great N. Ins. Co. v. Benjamin Franklin Fed. Sav. & Loan Ass’n*, 793 F. Supp. 259 (D. Or. 1990) (opining that asbestos contamination was not a physical loss, as the building remained unchanged), *aff’d*, 953 F.2d 1387 (9th Cir. 1992).

<sup>7</sup> <https://www.whiteandwilliams.com/resources-alerts-ISO-Excluded-Coronavirus-Coverage-15-Years-Ago.html>, citing *Gregory Packaging, Inc. v. Travelers Property and Casualty Company of America*, No. 12-cv-04418, 2014 U.S. Dist. LEXIS 165232 (D.N.J. Nov. 25, 2014) (holding that ammonia contamination constituted physical damage).

<sup>8</sup> <https://us.milliman.com/en/insight/COVID-19-business-interruption-coverage-and-the-physical-loss-or-damage-requirement#4>

DFS has approved forms excluding business interruption coverage for damages or loss resulting from viruses or bacteria “capable of inducing physical distress, illness, or disease.”<sup>9</sup> Because DFS must consider the overall health of the insurance marketplace for both insurers and consumers, DFS’s approval of such an exclusion is presumptive evidence that such exclusion was not unreasonable or violative of the public policy of the State of New York. On the contrary, an attempt to retroactively remove such DFS approved exclusions from existing contracts violates principles of New York insurance law and policy requiring that insurance cover a *fortuitous* future event (not known past or occurring perils)<sup>10</sup> and is destructive of the bargained for expectations of parties to a business interruption insurance contract, and likely violative of constitutional principles as well. By declaring a pandemic exclusion null and void S8211A (Gounardes)/A10226B (Carroll) and A10327 (Rosenthal, L.) would substitute the judgment of the Department of Financial Services, the very agency which the legislature has delegated authority to regulate solvency of the financial services (including insurance) precisely for the expertise that DFS has in such matters. DFS also issued an informative FAQ on business interruption coverage. One particularly relevant question and response is below for reference.

How does my business interruption insurance policy treat the novel coronavirus (COVID-19)?

It is unlikely that a current business interruption policy has contemplated the coronavirus specifically. However, you should check to see if your policy has an exclusion that would disable coverage for an incident triggered by an epidemic or pandemic, which might apply as the COVID-19 situation evolves. Also, any claim would still need to be related to your property damage for coverage to be triggered.<sup>11</sup>

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<sup>9</sup> See, e.g. CP 01 40 07 06, available at,

<https://northstarmutual.com/UserFiles/File/forms/policyforms/Current/CP%2001%2040%2007%2006.pdf>

<sup>10</sup> See, NYIL §1101(1), which requires that insurance contracts in cover “fortuitous” events.

<sup>11</sup> [https://www.dfs.ny.gov/consumers/coronavirus/business\\_interruption\\_insurance\\_faqs](https://www.dfs.ny.gov/consumers/coronavirus/business_interruption_insurance_faqs)

If these bills to become law, they would be subject to intense constitutional scrutiny. U.S. Constitution Article I, section 10, clause 1, states, *inter alia*, that “[n]o state shall...pass any...law impairing the obligation of contract.” The New York Court of Appeals has stated that “the initial inquiry” of an impairment of contracts analysis “contains three components: whether there is a contractual relationship, whether a change in law impairs that contractual relationship, and whether the impairment is substantial”<sup>12</sup> This bill represents a substantial impairment of existing contractual relationships between insurers and their insureds as it would impose an unaccounted for, unpriced, and non-underwritten claim trigger on existing policies that never contemplated such coverage, and even requires policies that have lapsed by the contract terms to be automatically renewed regardless of the rights of one of the parties to the contract to potentially refuse to continue the contractual relationship. The constitutionality of this legislation is clearly suspect and would be tied up in the courts for many years. If the state were to pass such a measure, it would not provide any immediate relief to the needs of businesses. While we understand putting forth these types of proposals may be enticing for some elected officials, it only creates false hope for constituents that these types of claims would be covered by insurance. Insurance provides financial security to policyholders and is a good solution for a wide array of different risks—fire, windstorm, hail or lightning to name just a few examples. The risk has to be insurable though. Insurance is not a solution for every situation that arises. We face many woes as a nation and global community and insurance cannot be expected to

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<sup>12</sup> *Am. Econ. Ins. Co. v. State*, 30 NY3d 136, 150 (2017) (citing, *General Motors Corp. v. Romein*, 503 U.S. 181, 186 (1992)).

provide coverage that is not part of an insurance policy to address any and every issue that develops.

In fact the COVID-19 pandemic crisis has been so widespread that federal, not state solutions, are required. For example, the Small Business Administration has long administered the existing Economic Injury Disaster Loan (EIDL) Program which allows small businesses to borrow up to \$2 million dollars at interest rates as low as 4 percent over 30 years.<sup>13</sup> Furthermore, the CARES Act (HR 748) which was recently signed into law further expands SBA aid to small businesses by allowing small businesses to apply for Section 7(a) loans from SBA member banks with those portions of the loan which are used for payroll, utilities, rent, and other fixed business costs incurred from February 15, to June 30 to be *forgiven* (i.e. free money from a \$349 billion fund set aside from the federal government to cover small business operation costs under the terms of the program with an additional \$310 billion from a second round of funding). Furthermore the CARES Act includes numerous other tax and accounting provisions to assist small businesses survive the COVID-19 pandemic, including but not limited to, delay of employer payroll taxes, extending net operating loss (NOL) carryback to five years, and expanding the business interest expense deduction from 30 percent to 50 percent.<sup>14</sup> Additionally, Congress is considering other measures to help with the COVID-19 crisis.

Furthermore, Congress could enact a program to provide greater protections for small businesses from the risk of pandemic. Several proposals are being considered by Congress with a desired outcome of helping ensure that such coverage is available for

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<sup>13</sup> <https://www.sba.gov/funding-programs/disaster-assistance>

<sup>14</sup> <https://www.gcpartnership.com/en/News/GCP-News/March-2020/CARES-Act-Summary>

business during a future pandemic. While we are a firm believer in state regulation of insurance, the sheer magnitude of the pandemic necessitates a federal response. I encourage the state Senators and Assemblymembers to contact New York's congressional delegation to explore federal solutions to this massive and widespread crisis.

In addition, property and casualty insurance companies play a vital role in communities across New York State and the country. Insurance companies continue to employ millions of people across the country, hundreds of thousands here in New York, and have put measures in place to protect their health and safety. As I mentioned at the outset many being small businesses with an acute understanding of the struggles their neighbors face. Companies are also engaging in philanthropic and other community efforts as well as continuing to provide their customers with the services and financial protection they need.

Thank you for your time and, as always, I am available to answer any questions from any of the committee members. Please feel free to follow up with me via email at [emelch@nyia.org](mailto:emelch@nyia.org).