

By Paul S. White,
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“The only mistake a company can make is to develop a wait and see attitude.”

Scott M. Gawlicki,

Flu Season: Companies Must Prepare for the Possibility of an Avian Flu Pandemic, InsideCounsel, Feb. 1, 2006, available at http://www.insidecounsel.com/issues/insidecounsel/15_175/labor/304-1.html.

The Impact of a Global Avian Flu Pandemic

Floods, hurricanes, earthquakes, fires and terrorist activities have given the insurance industry more “greatest loss year ever” statistics than ever before.

Calamities of biblical proportions seem to confront

insurers annually. Some experts project, however, that a bird flu pandemic could carry the greatest toll of all on expense and on human life.

Every year, influenza viruses infect 600 to 1,200 million people worldwide and are attributed to 500,000 to 1,000,000 deaths worldwide, with 25,000 to 45,000 deaths in the United States. By comparison, a 1918 flu pandemic killed at least 40 million people worldwide when the global population was just 1.75 billion. The threat of an

avian flu virus today raises the specter of a worldwide economic and health crisis of catastrophic proportions—carrying the potential to be even more devastating than the 1918 pandemic. The reason is simple: there is no cure or vaccine for avian flu. See *California’s Level of Preparedness for an Outbreak of Avian Influenza*, (November 4, 2005) (testimony of Scott P. Layne, MD, Associate Professor of Epidemiology, UCLA School of Public Health, Los Angeles, CA, to the Chair of the Assembly Budget Committee on Health and Human Services, California Assembly).

This article will discuss, in general, what avian flu is and then explore the possible insurance coverage implications that could arise from an avian flu pandemic. Initially, we will speculate on possible claims that could be tendered under general liability, property, life insurance, errors & omissions, and directors and officers policies. Such possible claims will then be compared with possible insurance issues that could arise under standard policy language. Given the myriad unknowns that could accompany an avian flu outbreak, we emphasize that this article is not intended to provide conclusions on whether such an outbreak would or would not be covered by any insurance product, but rather has

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as its focus possible claims and coverage issues that could arise. Any claim or coverage would obviously require independent evaluation and investigation.

Bird Flu in Context

To place the impact of a bird flu pandemic in context, some perspective on other disasters is worth noting. According to a 2006

Some project that

employers and, in turn, their general liability insurers are likely to see the greatest number of claims should an avian bird flu pandemic hit.

National Business Institute report entitled *Insurance Coverage Trends*:

- In September 2003, 24,000 people along the east coast filed federal flood claims after Hurricane Isabel.
- Hurricane Katrina generated over 1.7 million claims and caused more than \$38 billion in property and business interruption losses.
- The January 1994, Northridge, California, earthquake caused \$12.5 billion in private insured losses.
- The September 11th terrorist attacks generated roughly \$18.8 billion to \$20.7 billion in insured property losses. It is expected that insurers will pay an estimated \$32.5 to \$34.7 billion by the time all claims are resolved.

Jacquelyn A. Beatty, *Catastrophic Losses**2 (National Business Institute 2006).

Given the above statistics that demonstrate the cost to the insurance industry relative to the claim potential associated with catastrophic loss/damage, should the industry be concerned about the potential for claims relative to a viral pandemic such as avian flu?

The U.S. Congressional Budget Office predicts that a severe pandemic would infect more than 90 million in the United States and has the potential to cause the

death of more than 2 million people in the U.S. alone. Michael Bradford, *Potential Avian Flu Pandemic Raises Insurance Questions*, Business Insurance, Jan. 2, 2006.

The World Bank estimates that each year of a severe pandemic could cost the U.S. economy anywhere from \$100 to \$200 billion, and economies worldwide could suffer a per year total loss of approximately \$800 billion. *Id.*

But despite widely known statistics relative to the catastrophic potential of avian flu losses, Standard & Poor's reports that insurers remain "minimally ruffled" about the possibility of an avian flu pandemic and the potential claims impact it might have. Standard & Poor's, *U.S. Insurers Not Yet Feverish over Avian Flu* (June 2, 2006), available at <http://www2.standardandpoors.com>. "...Until human to human transmission actually happens (which to date it has not), [insurers] see the potential for damage to their financial health marginal." *Id.*; see also Michael Bradford, *Risk Managers Wary of Avian Flu Threat, But Responses Vary*, Business Insurance, Dec. 26, 2005.

Of course, it remains to be seen whether insurers are correct in steadfastly being minimally concerned. As noted above, the world has yet to see a single human-to-human transmission of avian flu. There is not yet a pandemic. There only have been isolated bird-to-human cases reported to date worldwide. No business has yet shut down in response to avian flu concerns. Only a relatively few poultry flocks worldwide have had to be destroyed to prevent possible contagion. But at this point, when it comes to avian flu, anything is possible. It could very well prove to be that avian flu is the next Hurricane Katrina and the insurance industry will be forced to mobilize and respond to claims, spending dollars equal to or exceeding those noted above.

Bird Flu Background

So What Exactly Is Avian Flu?

Avian flu is an infection caused by influenza A viruses. Although the viruses are carried by wild birds, these types of birds are often just carriers; however, when domesticated birds such as ducks, turkeys and chickens contract the virus, they can become very sick and can even die from it. Avian flu is very contagious among birds. The virus is spread through an infected bird's saliva,

nasal secretions and feces. Center for Disease Control and Prevention, *Key Facts about Avian Influenza (Bird Flu) and Avian Influenza a (H5N1) Virus*, available at http://www.cdc.gov/flu/avian/gen-info/pdf/avian_facts.pdf (last visited Sept. 25, 2006).

There exist many different subtypes of type A influenza viruses and all known subtypes can be found in birds. Although the term "avian influenza virus" generally refers to the influenza A viruses found mainly in birds, it is possible for humans to contract the virus—particularly the H5N1 strain. Although the risk of human infection remains, at this point, relatively low, there have been confirmed cases of the various subtypes infecting humans since 1997. As may be expected, most cases of human infection from subtypes of influenza A viruses resulted from contact with either infected poultry or contaminated surfaces. Center for Disease Control and Prevention, *supra*.

Although only a few of the influenza A viruses have actually infected humans, the influenza A (H5N1) virus, also known as H5N1 virus, has impacted humans the most, causing "the largest number of detected cases or severe disease and death in humans." As of January 2006, 147 people in six countries are known to have been infected with the virus; 78 have died as a result of the infection, which is a 53 percent mortality rate to date. Despite these reported human infections, the H5N1 virus remains a very rare disease in people. Additionally, if a person is infected with H5N1, the virus is not easily transferred from one person to another. Center for Disease Control and Prevention, *supra*. Common symptoms of avian flu in humans include general influenza-like symptoms such as fever, cough, sore throat and muscle aches. Additional symptoms include eye infections, pneumonia, severe respiratory diseases and other severe and life threatening complications. Center for Disease Control and Prevention, *supra*.

There are not yet any confirmed, reported cases of human-to-human transmission. "Predicting the likelihood that the Avian Flu will develop the ability to travel from human to human is difficult. However one striking characteristic of the virus is its ability for rapid mutation in infected animals and humans. While these mutations

have affected patterns of virus transmission and spread among domestic animals and wild birds, they have not had any discernable impact on modes of transmission among humans.” Joseph Nicosia III, *Avian Flu: The Consumer Costs of Preparing for Global Pandemic*, 18 Loy. Consumer L. Rev. 479, 483 (2006). Thus, it remains to be seen what could be the overall scope and effect of human-to-human transmission of avian flu. As a result of an influenza virus’ ability to change, scientists are concerned that the virus will begin to spread more easily. Furthermore, because of the limited number of cases of human infection, little or no immunity exists to protect the human population. Center for Disease Control and Prevention, *supra*.

What Is a Pandemic?

A pandemic is a global disease outbreak. A flu pandemic occurs when a new influenza virus emerges for which people have little or no immunity and for which there is no vaccine. A pandemic occurs when the disease spreads easily from person to person, causes serious illness and is spread across the world in a very short period of time. Widespread commercial air travel and extensive international shipping of food creates transmission opportunities and provides the means for the rapid spread of contamination and infection of avian flu. *General Information*, available at <http://www.PandemicFlu.gov/general> (last visited Sept. 20, 2006).

Possible Claims under General Liability Insurance Policies

Coverage under a General Liability Policy

Commercial General Liability (CGL) policies generally are written pursuant to forms provided by the Insurance Services Office (ISO). CGL policies obligate the insurer to defend and/or indemnify the policyholder for claims alleging “bodily injury” or “property damage” against it that are the result of an “occurrence.” The insuring coverage grant usually obligates the insurer to pay “all sums” that the insured becomes legally obligated to pay as damages because of incidents covered by the policy. This grant of insurance coverage, however, is subject to several coverage exclusions.

An “occurrence” is generally defined as “an accidental event... including continu-

ous or repeated exposure to substantially the same general harmful conditions.” (Some policies under a separately negotiated endorsement may define an occurrence as an accident or event. This language has been construed as a broader coverage grant, including coverage for non-accidental, e.g., intentional, acts. See, e.g., *United Pac. Ins. Co. v. McGuire Co.*, 229 Cal. App. 3d 1560, 1563, 281 Cal. Rptr. 375, 377 (1991)). “Property damage” is defined to include “physical injury to or destruction of tangible property... or loss of use of tangible property which has both been physically injured or destroyed” while “bodily injury” usually requires actual injury to a person’s body (as opposed to mere emotional distress).

Interpreting similar language defining property damage, the California Court of Appeal has held:

[S]trictly economic losses like lost profits, loss of good will, loss of the anticipated benefit of a bargain and loss of an investment, do not constitute damage or injury to tangible property covered by a comprehensive general liability policy.

Allstate Ins. Co. v. Interbank Fin. Servs., 215 Cal. App. 3d 825, 830, 264 Cal. Rptr. 25 (1989) (emphasis omitted). See also *Giddings v. Indus. Indem. Co.*, 112 Cal. App. 3d 213, 169 Cal. Rptr. 278 (1980) (suits alleging banking and securities law violations as well as waste and misappropriation did not involve property damage within the meaning of the policy); *Devin v. USAA*, 6 Cal. App. 4th 1149, 8 Cal. Rptr. 2d 263 (1992), *review denied* (negligent misrepresentation with respect to the sale of a house caused only a non-tangible pecuniary loss); *Aim Ins. v. Culcasi*, 229 Cal. App. 3d 209 (1991) (an employer’s failure to forward an employee’s insurance application papers—which caused economic injury when the requested coverage was not in place—did not constitute property damage); *Liberty Bank v. Travelers Indem.*, 870 F.2d 1504, 1508–09 (9th Cir. 1989) (economic loss to lenders stemming from loss of subordination in security promised by bank is not property damage); see also *Snug Harbor, Ltd v. Zurich Ins.*, 968 F.2d 538, 542 (5th Cir. 1992) (“Courts have also held that purely economic losses—for example, loss of the use of money a claimant would have received but for the insured’s negligence—

do not constitute ‘the loss of use of tangible property’”).

Possible Claims

Some project that employers and, in turn, their general liability insurers are likely to see the greatest number of claims should an avian bird flu pandemic hit. The following list of possible claims against employers is excerpted and quoted in relevant part from an article appearing in the July 12, 2006, *Connecticut Law Tribune Labor & Employment Supplement*:

Americans with Disabilities Act and state-law discrimination claims:

Discrimination claims or suits could arise under the ADA or various state laws if employers pursue medical testing in too aggressive a manner. Similarly, employer policies requiring medical clearances from employees returning from travel may also create potential liability. Under the ADA, disability-related inquiries or medical examinations are permissible only when job-related and consistent with a business necessity. Other areas in which ADA claims could arise is relative to employer policies requiring return-to-work certifications or other medical examinations of potentially affected employees—that is, people who may have contracted the flu virus while traveling. In particular, mandatory testing of asymptomatic individuals may create a risk of liability.

Occupational Safety and Health Act

claims: The general-duty clause of the 1970 act that established the Occupational Safety and Health Administration requires that employers provide employees with a workplace free from “recognized hazards” that cause or are likely to cause death or serious physical harm. OSHA has recognized that avian flu is a potential health hazard and has published guidance for various industries on its Web site. To reduce the risk of potential OSHA claims, employers should review OSHA and CDC advisories and take reasonable precautions based on this information to prevent the spread of illness among their employees and other personnel. At the same time, when responding to employee concerns relative to exposure, employers must be also cognizant of their legal obligation

to appropriately protect employee privacy and abide by the ADA limitations on medical examinations.

On a related note, there is also the possibility of negligence or other civil liability suits brought by company employees against their employers because of exposure to or the contracting of avian flu while working in the course and scope of their

If a pandemic breaks out before a vaccine is available, would the U.S. government or pharmaceutical manufacturers somehow be legally responsible for the delay?

employment. One would anticipate, however, that workers' compensation laws would play a significant role in the resolution of such claims, including, but not limited to, laws that workers' compensation is the exclusive remedy for injuries sustained at work.

Wage-and-hour claims: Employers should remain consistent with federal and state wage-and-hour requirements if they require employees to remain at home because of flu-related concerns or take action in response to employees who refuse to work because of flu-related concerns. Requirements vary depending on whether an employee is nonexempt or exempt under the federal Fair Labor Standards Act. Employers providing paid leave should do so in a nondiscriminatory manner.

Family and Medical Leave Act claims: Under the Family Medical Leave Act, employers with 50 or more employees are required to provide employees with up to 12 weeks of leave per year for serious health conditions or to care for close relatives (spouse, child, or parent) with a serious health condition. Employees who have not been employed for 12 months,

or who have not worked at least 1,250 hours in the last 12 months, are not eligible for leave. Thus, arguably, employees exhibiting flu symptoms or those who have a child, spouse, or parent with flu symptoms may be eligible for leave under the Family and Medical Leave Act of 1993 or state law equivalents. Employers should consider how to handle a situation where an affected employee has exceeded permitted leave or is not eligible for FMLA leave. Also, whether to designate leave as under the FMLA—especially if it may be unclear whether an employee is affected by a flu virus or merely avoiding the workplace—may require case-by-case analysis, which must be performed in a nondiscriminatory manner.

In *Brenneman v. MedCentral Health System*, 366 F.3d 412 (6th Cir. 2004), the court found that the evidence in that case did not bring the flu under the protection of the FMLA, but the court left the door open for future claims. The decision indicates that had the patient been prescribed a different treatment regimen or had the patient sought treatment for the interaction of the flu and his diabetes, the court might have held otherwise.

The Fourth Circuit held in *Miller v. AT & T Corporation*, 250 F.3d 820 (4th Cir. 2001), that where the patient's flu required a second doctor's visit, and the physician conducted a physical examination and drew blood, constitutes treatment within the meaning of the FMLA. In other words, severe cases of influenza can be a serious health condition when the prescribed course of treatment meets the regulatory definition of that term. Under this decision, a case of influenza that resulted in a three-day work absence and hospitalization would also arguably meet the regulatory definition of a serious health condition.

Therefore, at this point under the case law, it appears that if an employee and employer are subject to the FMLA, and the employee sees a doctor for the flu, goes home, rests and drinks fluids, no matter how long the absence, it is not considered serious enough to invoke FMLA protection. However, if an employee requires inpatient treat-

ment for the flu, or even multiple doctors' visits, then perhaps the FMLA is implicated.

See also Linda G. Burwell & Terry W. Bonnette, Commentary: *As Fear of Avian Flu Outbreak Grows, Employers Must Review Workplace Sick Policies*, Mich. Law. Wkly., Nov. 28, 2005.

Race and national origin discrimination: Depending on an outbreak's country of origin, employers should be especially careful to ensure that employees are not targeted by flu-related policies or practices because of their ethnicity or country of origin.

Medical-privacy claims: Employers seeking medical certifications from employees must adhere to the applicable confidentiality requirements of the ADA and, possibly, privacy regulations under the Health Insurance Portability and Accountability Act of 1996. Employers may need to provide physicians with authorizations from their employees in order to obtain return-to-work medical certifications or to confirm eligibility for medical leave. All communications relating to these tests must be kept in confidential files separate from other personnel records. But employers should also note that medical disclosures required by law, such as reports to governmental agencies that may be monitoring the flu, are generally permissible under HIPAA.

Union contracts: Unionized workplaces may already have policies, such as sick-leave provisions, that will address flu concerns in some fashion under their collective-bargaining agreements. Bargaining rights may be triggered if employers with unionized work forces attempt to modify those policies.

Brian Arbetter and Peter Gillespie, *Be Prepared: Avian Flu Goes to Work, Employers Should Begin Planning to Avoid Problems in the Event of a Flu Outbreak*, The Conn. Law Trib., July 12, 2006.

Other Claims

- Products or other liability suits against an airline company that failed to install a high-efficiency particulate air-recirculation filter in an aircraft that transported someone infected with avian flu so that other passengers on the plane

contracted the virus. (These filters are standard in all new aircraft, and are currently in approximately 75 percent of all existing aircraft). See J. Nils Wright, *Airlines Get Ready to Defend Against Avian Flu Outbreak*, Business Insurance, May 22, 2006.

- A myriad of negligence or other liability suits, e.g., against childcare or day-care providers when one infected child in their care gets other children sick, against a company that fails to implement a pandemic contingency plan, and against the poultry industry. (In fact, should there be an avian flu pandemic, liability suits against poultry growers, meat packers, processors, retailers and restaurants would be likely be inevitable. These parties will be the first to be sued.)

History teaches us that vaccinations are not always created before a disease or illness has a devastating effect on the population (polio, etc.). History also teaches that sometimes the cure is more dangerous than the disease, e.g. the swine flu vaccine discussed later in this article. Moreover, “[t]he standard techniques for creating a vaccine for this virus might not work, or might not work quickly enough (it takes roughly six months using current technology), to produce a large enough supply early enough to inoculate even the highest risk groups, particularly if two doses are required for the vaccine to be effective (recognizing that for a vaccine to work at all, it must be administered before a patient becomes ill from a virus).” Steven Weisbart, *Pandemic: Can the Life Insurance Industry Survive the Avian Flu?*, Ins. Info. Inst. (Jan. 17, 2006) available at <http://www.iii.org/media/hottopics/additional/birdflu/>.

According to the *Baltimore Daily Record*, a medical journal:

MedImmune Inc. and the National Institutes of Health have begun initial human trials of a potential treatment for avian influenza. Clarenia Stephen, a spokeswoman for the Gaithersburg-based biotech, said the vaccine would harness a live version of the flu strain as well as the spray-up-the-nose delivery technology MedImmune uses in its FluMist seasonal flu treatment. Enrollment in the Phase I trials began last Wednesday with a goal of 20 participants. Ste-

phen said it was too early in the process to say when the company might begin to see results. The company developed the potential avian flu treatment in conjunction with the National Institute of Allergy and Infectious Diseases, a division of the Bethesda-based NIH. Stephen said the treatment, if proven successful, would have a number of advantages over other avian flu vaccines known to be in development. Using the live strain creates a stronger immune response and is therefore a more effective vaccination, she said. The treatment has also been shown to be effective in combating other, less severe strains of influenza. She noted the intranasal delivery technology already has Food and Drug Administration approval, which could speed the eventual approval process.

Joe Bacchus, *Gaithersburg-based MedImmune, Inc., National Institutes of Health in Avian Flu Trials*, Daily Rec., June 19, 2006.

Thus, one potential source of claim would be relative to any delay in developing, manufacturing and/or distributing the vaccine. If a pandemic breaks out before a vaccine is available, would the U.S. government or pharmaceutical manufacturers somehow be legally responsible for the delay? And, what if, ultimately, the vaccine does more harm than good? *Cook v. United States*, 545 F. Supp. 306, 306–07 (N.D. Cal. 1982), was a suit filed against the federal government for bodily injuries sustained after persons were inoculated with federally sponsored swine flu vaccinations.

Cook v. United States involved three actions brought under the Swine Flu Act and the Federal Tort Claims Act. The plaintiffs sought damages from the federal government for injuries they sustained due to Guillain-Barre Syndrome (“GBS”), which they argued was caused by their federally sponsored swine flu vaccinations. *Id.* at 307. Based on a strong statistical correlation between swine flu vaccination and an increase in GBS cases, the government stipulated to liability in GBS cases that arose ten weeks or less after vaccination. *Id.* The plaintiffs in this case presented evidence in order to show a connection between the vaccination and the onset of GBS fourteen or eighteen weeks after vaccination. *Id.* After listening to the testimony of several experts in the field, the court concluded

that the evidence the plaintiffs presented in order to extend the period of causality was “characterized by relatively minute samples and consequently minute differences in the relevant data.” As a result, the court held that the plaintiffs failed to meet their burden of proving the existence of a causal relationship after the tenth week following vaccination. *Id.* at 315.

In addition to claims or suits for bodily injury, an avian flu pandemic also presents the opportunity for “property damage” claims or suits. Below are possible third-party claims/suits against a policyholder for property damage caused by an avian-flu related occurrence:

- **Direct property loss.** A turkey farmer who loses his or her turkey crop and sues the policyholder for loss of the flock/crop would be an example of a direct property loss. The policyholder could be the company that distributed or shipped the turkeys and somehow exposed them to avian flu. (Possible claims against government entities relative to the “taking” of infected or potentially infected poultry flock are covered in the Possible Claims: Avian Flu-Related First Party Property Losses—Turkey “Depopulation” section.)
- **Indirect or licensing property loss.** Others may claim a loss of property when a requisite license to raise poultry flocks is denied due to increased concern over the potential for avian flu contamination. For example, the issue in *Board of Supervisors of Rockingham County v. Stickle*, 556 S.E.2d 748, 749 (Va. 2002), was whether a fairly debatable issue of disease was presented by the decision of the Board of Supervisors of Rockingham County (“Board”) to deny Stickle’s request for a special use permit to raise and release game birds on his farm. After Stickle filed his special use permit application, the Board made a site visit to Stickle’s farm and discovered that Stickle raised turkeys on his farm for a commercial poultry company. *Id.* at 750. As a result, the Board denied the request for a special use permit based on its concern over wild birds carrying diseases into poultry flocks. *Id.* at 751. The lower court found that the Board’s action was not fairly debatable and accordingly overturned the Board’s denial of the spe-

cial use permit. *Id.* The Board subsequently appealed. *Id.* The Third Circuit held that one of the testifying expert's "common-sense appraisal of the 'significant risk' to poultry from the release of pen-raised game birds [was] amply sufficient to make the issue fairly debatable." *Id.* at 754. Thus, the court found that the Board did not act arbitrarily when it denied Stickley's application for a special use permit. *Id.*

- **Constitutional claims raised by avian flu:** quarantine of infected or exposed persons, or the "taking" of personal property (*i.e.*, the right of government to destroy a potentially infected flock—case examples are discussed in Possible Claims: Avian Flu-Related First Party Property Losses—Turkey "Depopulation" section below).

Possible Claims under First-Party Property Policies Coverage under a First-Party Property Policy

A property insurance contract, as distinguished from general liability insurance, is a contractual relationship in which the insurer agrees to indemnify a policyholder in the event a designated property experiences a covered loss. Several persons or entities may have an insurable interest in the designated property at the same time, *e.g.*, property owner, mortgagee or tenants.

The nature of a property insurance policy is to provide an insured with benefits for accepted risks of loss, in exchange for the receipt of premiums. Property insurance policies generally insure either (1) "all risks" of physical loss unless perils are specifically excluded; or (2) "named perils" such as losses from specifically identified causes, *e.g.*, fire or earthquake. "All risk" policies typically provide coverage for "direct physical loss of or damage to Covered Property... caused by or resulting from any Covered Cause of Loss," which includes all risks except those excluded or limited under the policy. ISO Form BP 00 02 12 99. Courts in many states apply a "manifestation" trigger to progressive losses, effectively meaning that the policy on the risk at the time the loss was discovered is the only policy potentially applicable to the loss. *See, e.g., Prudential-LMI Comm. Ins. v. Superior Court*, 51 Cal. 3d 674, 699 (1990);

but see Vermont Electric Power Co. v. Hartford Steam Boiler Inspection & Ins. Co., 72 F. Supp. 2d 441, 446–47 (D. Vt. 1999) (holding that in states that do not require standardized policy language, courts must look to policy language to determine trigger, rather than adopt uniform trigger theory), *aff'd*, 831 F.2d 287 (3d Cir. 1987).

The typical all-risk policy begins with a broad insuring provision, which states that the policy covers "direct physical loss or damages to Covered Property." The insurer then specifies which risks it will not assume by listing those causes of loss as policy exclusions. *See Mutual Fire Ins. Co. of Calvert County v. Ackerman*, 872 A.2d 110 (Md. App.2005); *Morgan v. Auto Club Family Ins. Co.*, 899 So.2d 135 (Md.App.2005); *Garvey v. State Farm Fire & Cas. Co.*, 48 Cal. 3d 395, 406, 770 P.2d 704 (1989); *Jordan v. Allstate Ins. Co.*, 116 Cal. App. 4th 1206 (2004). In other words, "the insurer promises to pay money to the insured upon the happening of an event, the risk of which has been insured against." *Montrose Chem. Corp. v. Admiral Ins. Co.*, 10 Cal. 4th 645 (1995); H. Walter Croskey & Ron Heeseman, California Practice Guide: Insurance Litigation §6:200 (The Rutter Group 2004). The property insurer covering the insured risk when property damage first manifests itself is generally the insurer solely responsible for the loss, even if property damage continues after the insurer's policy expires. *See, e.g., Prudential-LMI Commercial Ins. Co. v. Superior Court (Lundberg)*, 51 Cal. 3d 674, 679, 274 Cal. Rptr. 387, 404 (1990); *Allstate Ins. Co. v. Quinn Constr. Co.*, 713 F. Supp. 35 (D. Mass. 1989), *opinion vacated*, 784 F. Supp. 927 (D. Mass. 1990); *Cohen v. North Am. Life & Cas. Co.*, 150 Minn. 507 (Minn. 1921); *Jackson v. State Farm Fire & Cas. Co.*, 108 Nev. 504 (Nev. 1992).

In addition, first-party property claims require direct physical loss to the property and proof of causation. Property policies require that the loss at issue result from "direct physical loss or damage." For example, California courts have concluded that this phrase requires "direct" loss, and as such encompasses only physical harm to the covered property. Direct loss does not include consequential or resulting economic loss bearing a more attenuated connection to the covered cause of loss. *Id.* Similarly, California courts have concluded

that the phrase "direct physical loss" also requires a "physical" loss. *Id.*; *Ward General Ins. Servs., Inc. v. Employers Fire Ins. Co.*, 114 Cal. App. 4th 548, 554, 556 (2003). Physical loss requires the loss of tangible property. *Ward*, 114 Cal. App. 4th at 554, 556. *See also Bergren v. Premier Ins. Co.*, 56 Cal. App. 3d 273 (1976) (interest on a construction loan incurred by insured after a covered fire is "consequential" and not direct physical loss). As referenced, economic losses are intangible, and generally are not covered physical losses. *State Farm Fire & Cas. Co. v. Superior Court*, 215 Cal. App. 3d 1435, 1445 (1989).

Moreover, first-party cases may involve losses that result in more than one concurrent cause. Relative to causation, there are two schools of analysis currently employed by courts across the country. A minority follows the doctrine of concurrent causation, where coverage is afforded so long as a covered cause of loss contributes in a meaningful way to the insured's damages. In these jurisdictions, coverage is allowed whenever two or more causes contribute to a risk and at least one of the causes is covered under the policy. It is completely unnecessary to determine exactly which event occurred first or even the degree to which the various causes of loss contributed. So long as a covered cause of loss appreciably or meaningfully contributes, and is not remote or tenuous in nature, then the insurer must find coverage under the policy. Concurrent causation analysis utilizes a "but for" analysis that is akin to the "direct causation" theory employed in tort law. *See, e.g., Ang v. Martin*, 114 P.2d 637 (Wash. 2005); *Hurd v. Williamsburg County*, 611 S.E.2d 488 (S.C. 2005). If the damages would not have occurred "but for" the contribution of a covered cause of loss, then there is coverage on the claim. This is the case even if there are multiple contributing causes that are clearly excluded under the policy.

By contrast, the majority of jurisdictions employ the doctrine of efficient proximate cause. In these states, coverage is afforded if the predominant cause of the loss is a covered cause of loss. Just as concurrent causation is akin to the "but for" theory in tort law, the doctrine of efficient proximate cause is more analogous to the proximate or legal causation analysis in tort law.

See *Palsgraf v. Long Island R. Co.*, 162 N.E. 99 (N.Y. 1928). “Efficient proximate cause” means the “predominating cause of the loss,” or the most important cause of the loss. *Garvey*, 48 Cal. 3d at 403. The efficient proximate cause need not be the first or immediate cause of loss. *Id.*; see also *Murray v. State Farm Fire & Cas. Co.*, 509 S.E.2d 1 (W. Va. 1998). Under this doctrine, once the predominant cause of the loss is identified, coverage turns on whether it is a covered or excluded cause of loss under the policy. If that predominant cause is excluded, then the entire claim may be excluded, even if there are covered events that contributed along the chain of events.

An insured may be required to mitigate losses. Under the “sue and labor” clause, the insured must

Take all reasonable steps to protect the Covered Property from further damage and keep a record of your expenses necessary to protect the Covered Property, for consideration in the settlement of the claim.

ISO Form CP 00 10 06 95. An insurer’s duty under a sue and labor clause to compensate the insured for expenses incurred in the preservation and protection of insured property is qualified, however: the expenses in question must be incurred to preserve the insured property from a peril insured against under the policy, or in other words, the loss must be covered in the first instance. *Shell Oil Co. v. Winterthur Swiss Ins. Co.*, 12 Cal. App. 4th 715, 766 (1993) (citing *Young’s Market Co. v. American Home Assur. Co.*, 4 Cal. 3d 309, 313 (1971)).

Avian Flu-Related First-Party Property Losses

The predominant and most anticipated issue is whether the presence of avian flu virus constitutes direct physical loss or damage. For example, when the virus is detected on doorknobs in a workplace or other public areas accessible to employees, does this constitute direct physical loss under a first-party property policy?

In a decision that could provide some guidance, the Eighth Circuit Court of Appeals recently addressed whether a plaintiff could recover the loss of business income resulting from an embargo on beef products due to “mad cow disease.” In *Source Food Tech., Inc. v. U.S. Fidelity*

& Guar. Co., No. 06-1166 (8th Cir. Oct. 13, 2006), the insured argued that the closing of the border to imported beef product caused direct physical loss to its beef product because its beef product was treated as though it were physically contaminated by mad cow disease and lost its function. The insured relied on *Gen Mills, Inc. v. Gold Medal Ins. Co.*, 622 N.W. 2d 147 (Minn. Ct. App. 2001), and *Marshall Produce Co. v. St. Paul Fire & Marine Ins. Co.*, 98 N.W. 2d 280 (Minn. 1959), to support its position that the impairment of function and value of a food product caused by government regulation is a direct physical loss to insured property. The Eighth Circuit found that those cases were distinguishable and that coverage in those cases was triggered by actual physical contamination of insured property. However, the Eighth Circuit found that Source Food’s inability to transport its truckload of beef product across the U.S./Canadian border did not constitute product that was physically contaminated or damaged in any manner and to characterize an inability to transport such beef product across the border would render the word “physical” meaningless. Consequently, the court granted summary judgment in favor of an insurer on the plaintiff’s breach of contract claim on the basis that Source Food did not experience direct physical loss to property.

Further issues relate to the exclusions applicable in a first-party context. For example, in both first party and the CGL context, insurers will likely assert that pollution exclusions bar coverage relative to pandemic claims/suits. Nationwide, there is a split of authority as to whether pollution exclusions apply solely to industrial pollution or also apply to indoor events. See *Avian Flu: Planning for a Pandemic*, Metropolitan Corp. Couns., July 2006, at 39. Moreover, many policies provide coverage for lost business income for the period of cessation or interruption of operations. *Id.* However, this coverage may only be available where the cessation of operations arises from actual damage to property. *Id.*

Below are a variety of possible first-party claims:

Business Interruption Losses

“One of the distinguishing elements of a pandemic versus other types of business

interruption is that pandemics will result in the temporary—and in some case permanent—loss of human capital...” Mark A. Hofmann, *Government Releases Pandemic Plan, Employers to Play a Key Role in Fight against Avian Flu Threat*, Business Insurance, May 8, 2006.

Possible claims arising from businesses being disrupted carry the specter of touch-

An avian flu pandemic
also presents the
opportunity for “property
damage” claims or suits.

ing nearly every type of business where people interact:

The economic effects of a pandemic could be devastating, says Laurie Garrett, a senior fellow for global health at the Council on Foreign Relations in New York City, whose article on the subject is in the July/August issue of *Foreign Affairs*.

The airlines and travel industry would feel the hit first, predicts Garrett, who is the author of the book *The Coming Plague: Newly Emerging Diseases in a World out of Balance*.

She says that international trade might then dry up as frantic governments try to shut down their borders to prevent the spread of the disease. Essential imported goods, such as raw materials, medicines and certain foods, would become suddenly unavailable. As the pandemic progresses, schools and day care centers would be almost certain to shut down.

“Parents will stop coming in to work to stay home and take care of their children,” Garrett says. “Business will grind to a halt all over the place. What if the supermarkets stop being stocked? What if you can’t get milk?”

Kristin Choo, *The Avian Flu Time Bomb*, 91 A.B.A. J. 36, 40 (2005).

Turkey “Depopulation”

The cases below address coverage under

first-party property policies issued to those in the poultry business.

The appellants in *Reichley v. Pennsylvania Department of Agriculture*, 427 F.3d 236, 240 (3d Cir. 2005), produced poultry for human consumption. In order to guard against the spread of diseases, the Pennsylvania Department of Agriculture (PDA) had the authority to quarantine ani-

When the virus is detected on doorknobs in a workplace or other public areas accessible to employees, does this constitute direct physical loss?

mals it suspected were exposed to dangerous and transmittable disease. *Id.* at 238. This case arose when appellants received notice that some of their flocks allegedly tested positive for avian influenza. *Id.* at 241–43. Accordingly, PDA quarantined the flocks and subsequently depopulated them. *Id.* The appellants received compensation from PDA for their loss. *Id.* at 242–43. After the destruction of the flocks, appellants learned that none of the flocks had in fact been infected with avian influenza. *Id.* at 242–43. As a result, the appellants brought suit against the PDA alleging, among other things, violations of procedural due process. *Id.* at 243. The appellants claimed they were “denied notice and an opportunity for a hearing before depopulation.” *Id.* at 247. The court held in favor of the PDA, stating that “[d]ue process does not require a pre-deprivation notice and hearing where there is an adequate scheme to compensate the property owner for the deprivation.” *Id.* Specifically, because the PDA compensated farmers for a percentage of the value of the depopulated flocks, notice and a hearing were not required. *Id.*

In *Rose Acre Farms, Inc. v. United States*, 373 F.3d 1177, 1183 (Fed. Cir. 2004), the plaintiff, Rose Acre Farms, brought suit against the United States Department of

Agriculture (USDA), alleging it was entitled to compensation under the Fifth Amendment for the taking of its eggs and hens. On January 30, 1991, the USDA passed regulations “that restricted the interstate sale and transportation of eggs and poultry from flocks determined” to be contaminated with salmonella. *Id.* at 1180, 1181. After the passage of the regulations, salmonella outbreaks were traced to three of Rose Acre’s farms. *Id.* at 1182. Pursuant to the regulations, the USDA removed sixty hens from each house for organ testing. *Id.* Additionally, Rose Acre Farms had to “depopulate, clean and disinfect the infected houses, and then have those houses pass USDA inspection.” *Id.* The court in *Rose Acre Farms* vacated the Court of Federal Claims’ judgment granting Rose Acre Farms compensation. *Id.* at 1198. The court also remanded the case instructing the lower court to reevaluate the *Penn Central* factors, which include “‘economic impact of the regulation on the claimant,’ ‘the extent to which the regulation has interfered with the distinct investment-backed expectations’ and ‘the character of the governmental action’” in order to determine whether a taking compensable under the Fifth Amendment has occurred. *Id.* at 1198, 1184.

The suit in *Yancey v. United States*, 915 F.2d 1534, 1536 (Fed. Cir. 1991), was brought by Andrew and Elizabeth Yancey seeking compensation for their turkey breeder stock that was sold for slaughter as a result of a quarantine imposed by the United States Department of Agriculture (USDA) to control an outbreak of avian influenza. The Yanceys based their claim on a violation of the Fifth Amendment for a taking of their property without compensation “because the quarantine prevented the interstate sale of their stock and thereby destroyed its economic value.” *Id.* at 1537–38. The court ultimately held that the quarantine constituted a Fifth Amendment taking and, as a result, the Yanceys were entitled to compensation for lost profits. *Id.* at 1543. The court reasoned that the “Yanceys suffered severe economic impact and had no way of anticipating the interference with their investment backed interest” and despite following USDA regulations, their turkey business was destroyed through no fault of their own. *Id.*

Following the discovery of avian influ-

enza in Pennsylvania, the Pennsylvania Department of Agriculture (PDA) and the United States Department of Agriculture (USDA) established a quarantine zone that included several counties in Pennsylvania. *Empire Kosher Poultry, Inc. v. Hallowell*, 816 F.2d 907, 909 (3d Cir. 1987). Empire, currently without a processing plant within the quarantine zone, requested permission from the PDA to move live poultry out of the quarantine zone to one of its plants for slaughtering, but the PDA refused. *Id.* at 910. Following this denial, a flock of birds owned by Empire became infected with avian influenza and were accordingly destroyed. *Id.* at 911. Empire filed suit in the district court, alleging that the restriction on movement outside the quarantine area “caused a ‘taking’ of its property without just compensation, and deprived it of its property without due process of law, by arbitrarily and capriciously imposing an unnecessary quarantine.” *Id.* at 911. The Court of Appeal denied Empire’s substantive due process claim and held, among other things, that the quarantine zone was not overly broad and was instead selected to cover known areas of infection and to include a buffer zone so as to avoid the accidental shipment of poultry out of the quarantine areas. *Id.* at 913. The court also denied Empire’s Fifth Amendment claim and held that “[d]iminution in value of property such as Empire claims is not sufficient by itself to establish a right of compensation as a result of a public health regulation in the public interest.” *Id.* at 916.

Possible Claims under Life Insurance Policies

Some have asserted that the single greatest shock wave to the insurance industry relative to avian flu would be felt by the life insurance sector. *See Weisbart, supra.*

If the worst-case scenario happens and 2 million Americans lose their lives to avian influenza, life and health insurance claims could skyrocket. According to the Insurance Information Institute, “a moderate avian flu outbreak similar to the 1957 and 1968 flu pandemics has the potential to have a significant impact on life insurance companies and health insurance companies directly and property and casualty companies indirectly.” D. Kent Michie, Utah Insurance Commissioner, *Avian Flu*

Pandemic, Utah Insurance Bulletins (Mar. 1, 2006). In fact, the Insurance Information Institute estimates that even a moderate outbreak of the avian flu will generate \$3.1 billion in death claims. And, if the outbreak is severe, it will cause about \$133 billion in death claims. *Id.*

The effect of such outbreaks will be particularly great on life insurance companies that concentrate their marketing and sales efforts on group and individual term products because the claims volume will require them to look to the capital markets to shore up capital and surplus that will be needed to respond to such high volumes of claims payments. This may also be true of health insurance companies that will see a surge of health insurance claims. *Id.*

Possible Claims under E&O and D&O Policies

Errors & Omission coverage comes in a variety of packages. Litigation targets that often arise in any health or pharmaceutical crisis context often include:

- E&O coverage for medical professionals
- E&O coverage for pharmacies
- E&O coverage for businesses that fail to implement a pandemic contingency plan

An avian flu pandemic will inevitably lead to litigation premised on theories that the outbreak could have been prevented or substantially mitigated. Similarly, litigation will not only target the purported errors and omissions of businesses, but could also target the directors and officers of such businesses for failing to act and the subsequent financial impact on companies and shareholders. For example, the potential financial devastation that could impact a company could conceivably lead to claims against directors and officers by stockholders and employees who participate in stock purchases or retirement plans and who allege director and officer misconduct has led to a decrease in stock value.

E&O claims

E&O Coverage for Medical Professionals

E&O policies for medical professionals often extend coverage for “medical incidents,” typically defined as “any act or omission [¶] [a]rising out of the providing of or failure to provide professional medical... services...” See, e.g., ISO Form PR 00 01 12 97.

E&O policies for hospitals define “medical incidents” to mean “any act or omission [¶] [i]n the providing of or failure to provide professional health care services to your patients, including: [¶] [t]he providing or dispensing of... medications... in connections with such services.” *Id.* (emphasis added).

E&O Coverage for Pharmacies

E&O policies for pharmacists similarly provide coverage for liability arising out of acts and omissions in providing professional services. The role of pharmacists has evolved beyond the mere filling of prescriptions to include patient consultation and counseling, prescription evaluation and drug product selection, and courts have long recognized an expanding list of professional duties that pharmacists owe their patients.

It should be noted that specific policy forms were developed in the mid-1980s by the Bermuda excess market (e.g., XL Insurance Ltd and ACE Insurance Company Ltd.). Richard Jacobs *et al.*, *Liability Insurance in International Arbitration: The Bermuda Form* §§1.01–1.02, at 1-2 (2004). Since the introduction of the specialized Bermuda forms, other insurers have begun to write policies with similar features at lower excess layers.

While the Bermuda forms have several similarities to standard CGL policies, they also have several unique provisions.

Aggregated Claims/ integrated Occurrence

The policies have provisions regarding an aggregation of claims and an integrated occurrence provision, which allows a pharmaceutical company to combine or aggregate related claims into a single occurrence. This then allows a policyholder confronting multiple claims, which might not themselves provide access to excess coverage, to elect to give notice of an “integrated occurrence” and once it does “all Personal Injury or Property Damage that falls within the Integrated Occurrence... shall be treated as such for all purposes...” Form XL 004 Article V(D), quoted in Jacobs, *supra*, §8.07, at 129; XL Notice Guidelines, quoted in Jacobs, *supra*, §8.23, at 136; XL 004 Form Article V(C), quoted in Jacobs, *supra*, §8.01, at 127.

In other situations, claims against the pharmaceutical company may be deemed an “integrated occurrence.” The XL 004 form’s “occurrence” provisions state:

...where an occurrence exists and a **series** of and/or several or alleged Personal Injuries,... occur which are attributable directly, indirectly or allegedly to the *same actual or alleged event, condition, cause, defect, hazard and/or failure to warn of such*, all such actual or alleged Personal Injuries... shall be added together and treated as encompassed by one Occurrence irrespective of the period... or area over which the alleged Personal Injuries... occur or the number of such actual or alleged Personal Injuries....

Form XL 004 Form, Article III(V)(2), quoted in Jacobs, *supra*, §6.22, at 95 (emphasis added). To be deemed an integrated occurrence under the XL 004 form, the alleged injuries must (1) either commence within 30 days of each other or be the subject of the insured’s permissive notice of integrated occurrence, and (2) the injuries must be related to each other, such as claims involving the same drug. In contrast, the SELIC-02 form allows the insured to include claims of which it first became aware during the five years preceding the notice of integrated occurrence. David E. Schroeder, *The Bermudan Excess-Liability-Forms*, in Forum: Casualty & Environment (Issue No. 2 March 1999), available at http://www.geinsurancesolutions.com/erccorporate/theinstitute/pc/inst_ind_cas_market_bermudan.htm (last visited Jan. 12, 2005). Under either form, aggregation and integrated occurrence may allow insureds to reach the retentions of the high-level Bermuda excess policies, a threshold requirement for coverage.

Expected or Intended/ maintenance Deductible

It is not unusual for a particular drug to be subject to a certain “noise level” of claims, and then encounter a spike in the number and magnitude of claims. Recognizing this phenomenon, the Bermuda forms contain a specialized definition of “expected or intended” injury, which has been nicknamed the “maintenance deductible.” Like most insurance policies, the Bermuda forms preclude coverage for expected

or intended injury. However, where the insured has historically experienced a certain rate of claims, and then faces claims “fundamentally different in nature or at a level or rate vastly greater in order of magnitude,” the noise level claims will not necessarily be deemed expected or intended so as to preclude coverage for the spike in claims. Form XL 004, Article III(L)(1)(c), quoted in Jacobs, *supra*, §7.05, at 108.

Choice of Law/forum Selection

The Bermuda forms’ choice of law provisions require the application of New York law to coverage issues. Form XL 004, Articles VI(N) and VI(O), quoted in Jacobs, *supra*, §3.01, at 29. The Bermuda forms, however, contain some exceptions to New York law with respect to indemnity for punitive damages (which is prohibited under New York public policy) and regulatory issues. Form XL 004, Article VI(O), quoted in Jacobs, *supra*, §3.01, at 29; Schroeder, *supra* (noting that SELIC-02 form similarly provides for indemnity for punitive damages).

The Bermuda forms contain a mandatory arbitration provision, with the arbitration to take place in England or Bermuda under the procedural rules of those countries. Form XL 004, Article VI(N), quoted in Jacobs, *supra*, §3.01, at 30 (requiring arbitration in England); compare SELIC-02 (requiring arbitration in Bermuda). Thus, to date, there have been no reported judicial opinions interpreting the provisions of the Bermuda forms. Cases decided under New York law are relevant to substantive coverage issues, and England’s Arbitration Act, revised in 1996, governs procedural aspects of the arbitration. Jacobs, *supra*, §§3.04–3.18, at 31–38.

E&O Coverage for Businesses that Fail to Implement a Pandemic Contingency Plan

There are a number of E&O products available for general or miscellaneous errors and omissions where there is an alleged act, error or omission in providing a professional service. The scope and limitations of such insurance products could ultimately be subjected to a test of whether they extend coverage for a business’ failure to implement a pandemic contingency plan that ultimately results in damages to an individual, another business or an investor.

D&O Claims

A bird-flu pandemic could lead to financial devastation for business due to a health crisis, lack of production, work-force absence, inside information, failure to disclose, etc. The valuation of a company can shrink dramatically in the midst of such a crisis. For example, negative publicity about a drug, especially when coupled with lawsuits alleging bodily injury caused by the drug, can lead to a drop in stock price. The drop in stock prices can lead to suits by, among others, two groups: stockholders and retirement plan participants and beneficiaries. Stockholder suits may allege violations of the Securities Exchange Act of 1934, breach of fiduciary duty, abuse of control, gross mismanagement and waste of corporate assets, and may seek contribution and indemnity from the company’s directors. *See, e.g.,* Verified Shareholder’s Derivative Complaint at 3, *Kaufman v. Gilmartin*, Case No. 04-5566 (MLC) (D. N.J., filed Nov. 12, 2004); Verified Shareholder Derivative Complaint, *Jennett v. Gilmartin*, Case No. 04-5481 (SRC) (D. N.J., filed Nov. 8, 2004). Since manufacturers have marketed products directly to patients, it is not surprising that recent suits have included allegations that patients’ injuries were caused by the manufacturers’ advertising of drugs. *Id.* Such claims may implicate directors and officers (D&O) policies. Such claims against pharmaceutical manufacturers serve as a backdrop for what pharmaceutical companies or medical professionals or businesses could face in an avian flu crisis, or what other companies’ directors and officer could possibly face in the wake of devaluation arising from what they knew or should have known, or how they acted or failed to act, in response to an avian flu pandemic.

On a similar note, retirement plan suits typically allege violations of the Employee Retirement Income and Security Act of 1974, 29 U.S.C. §1001, *et seq.* (ERISA). While such claims may implicate D&O policies, some D&O policies contain an exclusion for ERISA-related claims. As discussed below, ERISA suits may also implicate employee benefits liability policies.

D&O Coverage

Most D&O policies, including excess D&O policies, provide coverage for “all Loss which... Directors and Officers shall

become legally obligated to pay in respect of... Claims” for “Wrongful Acts.” Oil Casualty Insurance, Ltd. *Excess Directors and Officers Liability Insurance Policy*, available at <http://www.ocil.bm/> (last visited Mar. 13, 2005). “Wrongful Acts” are typically defined to mean “any error, misstatement or misleading statement, act or omission, or neglect or breach of duty” by the director or officer. *Id.*

D&O policies typically contain two major coverage provisions, “Directors and Officers Liability Coverage” and “Corporate Reimbursement Coverage.” *Id.* Some primary policies add a third coverage provision for “Entity Coverage.”

- **Directors and Officers Liability Coverage**, nicknamed “A-Side” coverage, is implicated in claims by individual directors and officers for losses for which the corporation does not indemnify them. *Id.*
- **Corporate Reimbursement Coverage**, also known as “B-Side” coverage, is implicated in claims by the corporation for amounts that the corporation lawfully expends in indemnifying directors and officers for losses. *Id.*
- **Entity Coverage**, or “C-Side” coverage, is implicated in claims made against the corporation for wrongful acts committed by directors and officers. Increasingly, insurers are offering Entity Coverage as a means of avoiding disputes concerning allocation of defense and settlement costs where claims against insured directors and officers are joined with claims against the uninsured corporation. Justice H. Walter Croskey, *et al., California Practice Guide: Insurance Litigation* (The Rutter Group), ¶7:1578, at 7F-8 (2004).

Stockholder suits against pharmaceutical manufacturers have named individual directors and officers, as well as the corporation, as defendants. *Kaufman v. Gilmartin, supra; Jennett v. Gilmartin, supra.* Thus, it is likely that each of the above provisions will be implicated in claims for coverage.

Exclusions

Several D&O exclusions could be placed at issue in a D&O insurance response to an avian flu pandemic and resulting claims against directors and officers. This list is not exhaustive, but is a reference to exclu-

sions that could possibly be placed at issue to question whether coverage is precluded for claims against directors and officers.

Known Claims Exclusion

D&O policies preclude coverage where a director or officer knew of facts that could give rise to a claim, if publicly known. *American Guar. & Liab. Ins. Co. v. Fojanini*, 90 F. Supp. 2d 615, 619 (E.D. Pa. 2000), *reconsideration granted in part*, 99 F. Supp. 2d 558 (E.D. Pa. 2000). Applications for some D&O policies may require disclosure of “any knowledge or information of any act, error, omission or other circumstance,” which could give rise to a claim. *Id.*

Dishonesty Exclusion

Under most D&O policies, no coverage is afforded for claims based on “dishonesty, fraudulent or criminal acts” of the directors and officers. Language in most “dishonesty” exclusions requires a “final adjudication... establish[ing]... acts of active and deliberate dishonesty...” Oil Casualty Insurance, Ltd. *Excess Directors and Officers Liability Insurance Policy, supra*. Thus, mere allegations of dishonesty are insufficient to preclude coverage; rather, an adjudication of dishonest conduct is necessary. *PepsiCo, Inc. v. Continental Cas. Co.*, 640 F. Supp. 656, 659 (S.D.N.Y. 1986).

Continuous Wrongful Act Exclusion

Most D&O policies bar coverage for “Wrongful Acts” that are “directly or indirectly part of a series of continuous Wrongful Acts... or part of a series of continually repeated, related, or connected Wrongful Acts...” that began prior to inception. Oil Casualty Insurance, Ltd. *Excess Directors and Officers Liability Insurance Policy, supra*. Because the manufacture of a drug, with the attendant clinical testing and FDA approval requirements, by definition, can involve a series of activities, this exclusion could apply to bar coverage for suits against directors and officers in the pharmaceutical arena.

Employee Benefits Liability Claims

ERISA suits by retirement plan participants and beneficiaries can implicate not only the manufacturer’s D&O coverage, as discussed above, but its employee benefits liability (EBL) coverage as well.

EBL Coverage

EBL policies typically provide coverage for claims against the insured by employees or their beneficiaries for “injury caused by any negligent act, error or omission of the insured... in the administration of the insured’s ‘employee benefit program.’” ISO Form CG 77 10 (Ed. 09 86).

The term “employee benefit programs” is often defined to mean “group life insurance, group accident or health insurance, profit sharing plans, pension compensation insurance, unemployment compensation, social security and death benefits insurance.” *Id.* A retirement plan would fall within this definition only if it qualifies as one of the enumerated programs, most likely a profit sharing plan, pension compensation insurance, or social security insurance. Whether the plan at issue qualifies depends, in turn, on how it is structured.

The term “administration” includes counseling employees on benefits, interpreting the employee benefit programs, handling records, and issues effecting enrollment, termination or cancellation. *Id.* However, tasks related to investment or disposition of assets in the employee benefit program are specifically excluded from the definition of administration. *Id.*; see *Maryland Cas. Co. v. Economy Bookbinding Corp. Pension Plan & Trust*, 621 F. Supp. 410 (D. N.J. 1985) (virtually identical definition of administration “limits coverage to liability incurred in relatively routine, ministerial acts” and not for decisions made in managing a plan’s investments). Thus, to the extent that ERISA suits allege misconduct in investing plan assets in the company’s own stock, which lost value, such claims fall outside the scope of coverage.

Exclusions

EBL policies contain several exclusions that may preclude coverage for ERISA suits.

Stock Performance and Stock Participation Exclusions

Many EBL policies preclude coverage for claims based on “[f]ailure of stock shares to perform as represented by the insured,” or “[a]dvice given by an insured to an employee to participate or not to participate in stock subscription plans.” *Jasco Tools, Inc. v. American Mfrs. Mut. Ins. Co.*, 259 A.D.2d 1027, 1028–1029, 688 N.Y.S.2d

317, 318–319 (construing CGL exclusions for “negligence, errors or omissions in the Administration of Employee Benefit Programs,” failure of an investment to perform as represented and for claims based on investment or non-investment of funds).

Failure to Comply with Law Exclusion

EBL policies may exclude coverage for

A moderate avian flu outbreak similar to the 1957 and 1968 flu pandemics has the potential to have a significant impact on life insurance companies.

claims based on “failure to comply with any law concerning worker’s compensation, unemployment insurance, social security, disability benefits or any similar law.” ISO Form CG 77 10 09 86. While this exclusion does not specifically list ERISA, insurers can argue that it qualifies as “any similar law.” *Cf. General Reins. Corp. v. St. Jude Hospital*, 107 Cal. App. 4th 1097, 1108 (2003) (upholding exclusion for failure to comply with “any Workers Compensation law”).

Dishonesty Exclusion

Under most EBL policies, no coverage is afforded for “[a]ny dishonest, fraudulent, criminal or malicious act.” ISO Form CG 77 10 09 86. As with a comparable exclusion in D&O policies, mere allegations of dishonesty are insufficient to preclude coverage, and an adjudication of dishonest conduct is necessary.

Intentional Conduct

Even though EBL policies do not necessarily contain a specific “intentional conduct” exclusion, some courts have held that EBL insuring clauses, which provide coverage for “any negligent act, error or omission,” limit coverage to negligent conduct and afford no coverage for intentional conduct.

Intermountain Gas Co. v. Industrial Indem. Co. of Idaho, 125 Idaho 182, 186, 868 P.2d 510, 514 (App. 1994); *Baylor Heating & Air Conditioning v. Federal Mut. Ins. Co.*, 987 F.2d 415 (7th Cir. 1993).

Conclusion

In the wake of Hurricane Katrina, there were multiple bad faith lawsuits filed against insurers before a single claim was even denied. The Northridge, California earthquake and terrorist attacks on the World Trade Center are also stark reminders of the extreme catastrophes that can

occur and that, in turn, translate into insurance disputes involving billions of dollars and millions of lives.

Thus, catastrophic losses—or even mass exposure to allegedly harmful substances with no manifest injury—often result in mass tort litigation. Recent decades have seen a dramatic increase in mass tort litigation. Such litigation then tends to spawn other litigation in that it is likely to generate a host of claims for coverage under a variety of insurance policies, including third-party liability claims, D&O claims, E&O claims and first-party claims. Given the

magnitude that a potential bird flu pandemic would carry with it, if history is any indicator, insurance benefits would likely become the subject of litigation as would insurers' handling of claims. The potential magnitude and variety of claims that would accompany a modern-day pandemic could be of biblical proportions. Hopefully, such a pandemic will never arrive or, if it does, modern medicine will have preempted or mitigated the scope of any such catastrophe on our day-to-day lives. 