No. 20-16858

IN THE

UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT

MUDPIE, INC.,

Plaintiff-Appellant,

v.

TRAVELERS CASUALTY INSURANCE COMPANY OF AMERICA,

Defendant-Appellee.

On Appeal from the United States District Court for the
Northern District of California
No. 4:20-cv-03213, The Honorable John S. Tigar

BRIEF OF THE AMERICAN ASSOCIATION FOR JUSTICE AS AMICUS CURIAE IN SUPPORT OF PLAINTIFF-APPELLANT'S PETITION FOR REHEARING EN BANC

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CORPORATE DISCLOSURE STATEMENT

Pursuant to Federal Rule of Appellate Procedure 26.1, amicus curiae the American Association for Justice certifies that it is a non-profit voluntary national bar association. There is no parent corporation or publicly owned corporation that owns 10% or more of this entity's stock.

Respectfully submitted this 5th day of November, 2021.

/s/ Jeffrey R. White

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IDENTITY AND INTEREST OF AMICUS CURIAE

The American Association for Justice ("AAJ") is a national, voluntary bar association established in 1946 to strengthen the civil justice system, preserve the right to trial by jury, and protect access to the courts for those who have been wrongfully injured. With members in the United States, Canada, and abroad, AAJ is the world's largest plaintiff trial bar. AAJ's members primarily represent plaintiffs in personal injury actions, employment rights cases, consumer cases, and other civil actions, including in business interruption coverage cases. Throughout its 75-year history, AAJ has served as a leading advocate for the right of all Americans to seek legal recourse for wrongful conduct.[1]

This case is of acute interest to AAJ and its members. Many AAJ members represent plaintiffs in business interruption cases arising from the COVID-19 pandemic, including in California. AAJ is concerned that without certification to the California Supreme Court, California will not be given the opportunity to weigh in on an important matter of state law. And, the California court's answer to the proposed question could determine the outcome of this matter, which will have a

[1] All parties have consented to the filing of this brief. No party or party's counsel authored this brief in whole or in part. No person, other than amicus curiae, its members, and its counsel, contributed money that was intended to fund the preparation or submission of this brief.

major impact on many small businesses throughout California that have been irreparably harmed as a result of the pandemic, and similar court cases.

INTRODUCTION AND SUMMARY OF ARGUMENT

AAJ respectfully addresses this Court in support of Plaintiff-Appellant's Petition for Rehearing En Banc ["Petition"].

Much of the substantive law that governs the lives of ordinary Americans and small businesses is state law, as developed by state courts. In diversity cases such as this one, *Erie* commands that the federal court ascertain and apply substantive state law as declared by the state supreme court. Where, as here, the state supreme court has not addressed a state law issue, the task of the federal court becomes more problematic for cooperative federalism.

The panel endeavored to discern how the California Supreme Court would construe a provision in a widely used commercial insurance contract by relying on intermediate appellate opinions addressing differently worded provisions in other circumstances. The panel also failed to take note of the extent to which other courts around the country have interpreted the same language differently, and failed to apply California's rule that ambiguous insurance provisions be construed in favor of the insured.

The panel also declined to make use of a certified question, which has been called a "wonderful device" that "enables us to obtain a definitive answer when Erie

charts a perilous course through uncharted waters." *Walters v. Inexco Oil Co.*, 670 F.2d 476, 478 (5th Cir. 1982) (Brown, John R., J.). The Petition in this case illustrates the sound reasons why federal judges "should hesitate to 'trade judicial robes for the garb of prophet' ... when an available certification procedure renders the crystal ball or divining rod unnecessary.". *Boardman v. United Servs. Auto. Ass'n*, 470 So. 2d 1024, 1043 (Miss. 1985) (quoting John R. Brown, *Certification—Federalism in Action*, 7 Cumb. L. Rev. 455 (1977)).

AAJ urges this Court to grant the Petition.

ARGUMENT

I. THE PANEL ERRED IN HOLDING THAT UNDER CALIFORNIA LAW COVERAGE OF "DIRECT PHYSICAL LOSS OF" INSURED PROPERTY DOES NOT INCLUDE LOSS OF THE USE OF THAT PROPERTY DUE TO GOVERNMENTAL ORDERS.

In an effort to combat the COVID-19 pandemic, California officials issued stay-at-home orders that forced non-essential businesses to suspend their operations. As a result, Plaintiff Mudpie, Inc., a San Francisco children's retailer, lost the use of its physical storefront premises and suffered significant losses. *Mudpie, Inc. v. Travelers Cas. Ins. Co. of Am.*, No. 20-16858, 2021 WL 4486509, at *2 (9th Cir. Oct. 1, 2021).

Mudpie, like many small businesses in California, had purchased an all-risk comprehensive commercial insurance policy, issued by Travelers, that promised to

cover loss of business income caused by "direct physical loss of or damage to" the insured property. *Mudpie*, 2021 WL 4486509, at *3. After Travelers denied Mudpie's claim, Mudpie filed a putative class action seeking damages for breach of contract and other relief. *Mudpie*, 2021 WL 4486509, at *2. The district court granted Travelers' motion to dismiss, and a panel of the Ninth Circuit affirmed. The panel concluded that, under applicable California law, "direct physical loss" does not include mere loss of use of the insured property in the absence of "physical alteration" of the property. *Mudpie*, 2021 WL 4486509, at *4-*5.

AAJ submits that the panel erred in its *Erie*-mandated prediction of how the California Supreme Court would construe the policy language at issue here.

The federal court's responsibility in this diversity case, as the panel correctly stated, is "to follow the decisions of the state's highest court," as the ultimate arbiter of state law, and where "the state supreme court has not spoken on an issue, we must determine what result the court would reach based on state appellate court opinions, statutes and treatises." *Mudpie*, 2021 WL 4486509, at *3 (quoting *Diaz v. Kubler Corp.*, 785 F.3d 1326, 1329 (9th Cir. 2015)).

Rather than endeavor to predict how the California Supreme Court would construe the determinative contractual text, the panel looked to intermediate appellate court opinions that addressed "similar" but clearly inapposite policy provisions. See *Mudpie*, 2021 WL 4486509, at *4.

The panel relied most heavily on *MRI Healthcare Center of Glendale, Inc. v. State Farm General Insurance Co.*, 115 Cal. Rptr. 3d 27 (Ct. App. 2010). The appellate court there construed a policy provision that was entirely different from that involved this case. MRI Healthcare sought coverage for losses it suffered when it had to ramp down its MRI machine during roof repairs, and the machine failed to ramp back up. The California court of appeal upheld summary judgment for the insurer. However, unlike Mudpie's policy covering "physical loss *of*" its storefront, MRI Healthcare's policy covered "accidental direct physical loss *to* business personal property." *Id.* at 31 (emphasis added). That textual difference, as the California court of appeal pointed out, was historically important and crucial to its decision. *Id.* at 37.

Secondly, unlike Mudpie's policy, covering the "physical loss of or damage to" its property, the MRI Healthcare policy did not explicitly cover "damage" as a separate category. The California court viewed "loss to" as synonymous with "damage to," holding that, to show a "loss" to the property "some external force must have acted upon the insured property to cause a physical change in the condition of the property, i.e., it must have been 'damaged' within the common understanding of that term." *Id.* at 38. In the case before this Court, the policy's disjunctive use of loss *or* damage indicates coverage of losses, such as the loss of physical use of the property, as a separate category from physical damage. Blindly

applying *MRI Healthcare* to determine coverage under Mudpie's very different policy would require the court to treat "physical loss" as redundant surplusage. The panel essentially rewrote the terms of the insurance contract. Rather than give effect to the plain meaning of coverage of "physical loss of *or* damage to property," the court limited coverage to "physical loss of *and* damage to property."

Finally, the California court of appeal held that there was no physical "damage" within the meaning of the policy because the "loss" – the MRI was turned off and could not be turned back on – was not due to any external force, but "emanated from the inherent nature of the machine itself." *Id.* Mudpie, by contrast, has alleged that its loss of the use of its retail store was due to the external force of the shutdown orders imposed by governmental officials.

In short, nothing in the *MRI Healthcare* decision indicates that the California Supreme Court would rely on that decision to limit "physical loss of" property to instances of physical alteration of the property.

The panel relied on two other intermediate appellate decisions. Both are also inapplicable here. In *Doyle v. Fireman's Fund Insurance Co.*, 229 Cal. Rptr. 3d 840 (Ct. App. 2018), Doyle acquired a collection of purportedly rare vintage wines that turned out to be counterfeit, and he sought coverage under a "Valuable Possessions" property insurance policy. The court held that plaintiff's economic loss was not covered in the absence of physical damage to the property. However, the court's

rationale was that the policy by its terms covered only "losses *to* the wine; Fireman's Fund was not insuring against any losses *to* Doyle's finances." 229 Cal. Rptr. 3d at 843 (emphasis in original). In the case before this Court, the opposite is true: Travelers *has* insured Mudpie against financial losses due to loss *of* the insured property.

Ward General Insurance Services, Inc. v. Employers. Fire Insurance Co., 7 Cal. Rptr. 3d 844 (Ct. App. 2003), is inapplicable here as well. The appellate court there held that a loss of data that occurred when the insured's computer crashed was not a "physical loss" because plaintiff "did not lose the tangible material of the storage medium [the computer's hard drive]. Rather, plaintiff lost the stored *information*," which has no material existence. 7 Cal. Rptr. 3d at 851 (emphasis in original). In other words, the court's focus was on the word "physical," not "loss." In the case before this Court, Plaintiff did lose the use of tangible physical property—its insured storefront.

Because the district court in this diversity case failed to properly ascertain what interpretation the Supreme Court of California would give to the exact provision at issue here, and instead relied on inapplicable decisions by intermediate appellate courts, AAJ submits that rehearing en banc is warranted and appropriate.

II. THE SUPREME COURT OF CALIFORNIA WOULD CONSTRUE THE LANGUAGE OF THE INSURANCE CONTRACT IN FAVOR OF COVERAGE.

A. Courts in California and Around the Country Have Held that "Physical Loss Of" Insured Property Includes the Loss of Use of Insured Property Due To a Government-Ordered Shutdown.

Even if the panel's interpretation of the policy language at issue here is plausible, it is certainly not the only reasonable reading of the policy language.

Indeed, another U.S. District Court for the Central District of California decision has given the identical policy language the opposite construction. In *Total Intermodal Services Inc. v. Travelers Property Casualty Co. of America*, No. CV 17-04908 AB (KSx), 2018 WL 3829767 (C.D. Cal. Jul. 11, 2018), a container of specialty printer equipment intended for plaintiff's customer in Santa Ana, California was mistakenly shipped to Shanghai, held there by Chinese customs authorities, and eventually destroyed. Total Intermodal filed a claim for the value of the cargo under its insurance policy covering "direct physical loss of or damage to" covered property. *Total Intermodal*, 2018 WL 3829767, at *2.

The district court in that case denied Travelers's motion for summary judgment, holding that "Coverage for 'Direct Physical Loss Of ... Covered Property' Does Not Require Damage to the Covered Property." *Total Intermodal*, 2018 WL 3829767, at *2. The court explained that "to interpret 'physical loss of' as requiring 'damage to' would render meaningless the 'or damage to' portion of the same clause,

thereby violating a black-letter canon of contract interpretation—that every word be given a meaning." *Total Intermodal*, 2018 WL 3829767, at *3.

The court in *Total Intermodal* made it clear that, although the insured's property was destroyed in that case, the crucial factor in coverage in that case was the insured's loss of possession or use of its property.

> [T]he issue here is simply whether the phrase "loss of" includes physical dispossession in the absence of physical damage. The Court therefore uses the word "includes" to make clear that its construction is non-limiting.

Total Intermodal, 2018 WL 3829767, at *4 n.4.

AAJ suggests that the court's reasoning in *Total Intermodal* reflects the proper interpretation of "physical loss of *or* damage to property." At the very least, the decision demonstrates that the panel's interpretation is not the only reasonable one; the phrase is ambiguous, and Plaintiff's interpretation is also reasonable. Courts across the country have construed identical language to permit coverage of business losses caused by governmental COVID-19 closure orders.

For example, the district court in *Studio 417, Inc. v. Cincinnati Insurance Co.*, 478 F. Supp .3d 794 (W.D. Mo. 2020), held that plaintiffs had sufficiently alleged "direct physical loss" caused by "the COVID-19 pandemic and Closure Orders" which "prohibited or significantly restricted access to Plaintiffs' premises." *Id.* at 803 & n.6.

Other state and federal courts around the country have arrived at similar interpretations of the identical policy language. For example, in *Elegant Massage, LLC v. State Farm Mutual Automobile Insurance Co.*, 506 F. Supp. 3d 360 (E.D. Va. 2020, the district court determined that plaintiffs "experienced a direct physical loss when the property was deemed uninhabitable, inaccessible, and dangerous to use by the Executive [Shutdown] Orders." *Id.* at 376. Similarly, in *Dino Palmieri Salons, Inc. v. State Automobile Mutual Insurance Co*., No. CV-20-932117, 2020 WL 7258114, at *5 (Ohio Ct. Com. Pl. Nov. 17, 2020), the court found that "Plaintiffs' allegations . . . plausibly allege that access to their premises was prohibited [by government order] to such a degree as to trigger the civil authority coverage," which required "direct physical loss." *See also Independence Barbershop, LLC v. Twin City Fire Ins. Co.*, 499 F. Supp. 3d 331, 336 (W.D. Tex. 2020) (District court "might be receptive" to the argument that "having to . . . close one's business because of government orders intended to stop the spread of a disease caused by a virus" may be a covered loss.).

Likewise, the court in *North State Deli, LLC v. Cincinnati Insurance Co.*, No. 20-CVS-02569, 2020 WL 6281507, at *3-4 (N.C. Super. Ct. Oct. 9, 2020), issued partial summary judgment for the insured plaintiff seeking business interruption coverage. The court held that government orders restricting access to non-essential businesses constituted "direct physical loss" of the insured's premises. *North State*

Deli, 2020 WL 6281507, at *3-4. *See also Blue Springs Dental Care, LLC v. Owners Ins. Co.*, 488 F. Supp. 3d 867, 871 (W.D. Mo. 2020) (Plaintiffs adequately alleged a "direct physical loss" by alleging that "COVID-19 and the Stay Home Orders have forced them to suspend most of their business operations and deprived them of the use of their dental clinics.").

At the very least, this growing list of decisions demonstrates that "direct physical loss" is an ambiguous term in Travelers's policy and that Plaintiff's interpretation of that term is a reasonable one. *Hill and Stout PLLC v. Mut. of Enumclaw Ins. Co.*, No. 20-2-07925-1 SEA, 2020 WL 6784271, at *3 (Wash. Super. Ct. Nov. 13, 2020) (Court "finds that the phrase 'physical loss of['] is ambiguous.").

As the Eighth Circuit has pointed out, in a case involving insurance coverage of direct physical losses, "[t]he fact that several jurisdictions have reached divergent conclusions about the meaning of [a term] is evidence of the term's ambiguity." *Macheca Transp. v. Philadelphia Indem. Ins. Co.*, 649 F.3d 661, 668 (8th Cir. 2011).

B. Under California Law, Ambiguous Terms Are To Be Construed in Favor of Coverage.

The California Supreme Court "generally interpret[s] the coverage clauses of insurance policies broadly, protecting the objectively reasonable expectations of the insured." *AIU Ins. Co. v. Super. Ct.*, 799 P.2d 1253, 1264 (Cal. 1990). *See also Wildman v. Gov't Emps. Ins. Co.*, 307 P.2d 359, 362 (Cal. 1957) ("If semantically permissible, the contract will be given such construction as will fairly achieve its

object of securing indemnity to the insured for the losses to which the insurance relates."). As the California Supreme Court has stated in response to a certified question from this Court, any ambiguity in an insurance policy "must be construed in favor of coverage that a lay policyholder would reasonably expect." *Minkler v. Safeco Ins. Co. of Am.*, 232 P.3d 612, 614 (Cal. 2010). Consequently, it is clear that the California Supreme Court would have construed the policy language at issue in this case in favor of coverage of Mudpie's claim. Rehearing is therefore warranted.

III. REHEARING IS WARRANTED AND APPROPRIATE TO CERTIFY TO THE CALIFORNIA SUPREME COURT THE QUESTION OF THE PROPER INTERPRETATION OF THE DETERMINATIVE COVERAGE LANGUAGE.

If a state's highest court has not spoken on a determinative issue of state law, and "if state law permits it, we may exercise our discretion to certify a question to the state's highest court." *Vazquez v. Jan-Pro Franchising Int'l, Inc.*, 939 F.3d 1045, 1048-49 (9th Cir. 2019) (internal citations omitted).

In this case, Mudpie suggested to the panel that it certify the following question to the California Supreme Court:

> Could business interruption insurance for all risks of "direct physical loss of or damage to" covered property be reasonably construed to insure against the loss of business property to generate income as a direct result of state and local orders suspending, or severely curtailing, operations of non-essential businesses amid the COVID-19 pandemic?

The panel declined to certify this question, relying instead on inapposite opinions of intermediate California appellate courts. *Mudpie*, 2021 WL 4486509, at

*4 n.3. Where state law is unclear, the use of a certified question to obtain an authoritative declaration of state law "rests in the sound discretion of the federal court." *Lehman Bros. v. Schein*, 416 U.S. 386, 391 (1974). This Court has stated that the factors which guide its exercise of that discretion are:

> (1) whether the question presents "important public policy ramifications" yet unresolved by the state court; (2) whether the issue is new, substantial, and of broad application; (3) the state court's caseload; and (4) "the spirit of comity and federalism."

Vazquez, 939 F.3d at 1048 (quoting *Murray v. BEJ Mins., LLC*, 924 F.3d 1070, 1072 (9th Cir. 2019) (en banc)). Those factors weigh in favor of certifying the question proposed by Mudpie.

A. The Proposed Certified Question Has Important Public Policy Ramifications.

Certification is particularly appropriate "where the issues of law are complex and have 'significant policy implications.'" *McKown v. Simon Prop. Grp. Inc.*, 689 F.3d 1086, 1091 (9th Cir. 2012) (quoting *Perez-Farias v. Global Horizons, Inc.*, 668 F.3d 588, 593 (9th Cir. 2011)).

Small businesses like Mudpie are the primary customers who buy business interruption insurance. There are approximately 31.7 million small businesses in the U.S., employing more than 60 million people. Oberlo, *How Many Small Businesses Are There in the US in 2020*, https://www.oberlo.com/statistics/number-of-small-business-in-the-us#:~:text=In%202020%2C%20the%20number%20of,period%20

from%202017%20to%202020 (last visited Nov. 1, 2021). Over 4 million of those businesses are located in California, the most of any state. *Id*.

But the average small business has only $10,000 in monthly expenses and less than one month of cash on hand at any given time. Alexander Bartik, et al., *How Are Small Businesses Adjusting to COVID-19? Early Evidence From a Survey*, National Bureau of Economic Research, Working Paper Series No. 26989 (Apr. 18. 2020), *available at* https://hbswk.hbs.edu/item/how-are-small-businesses-adjusting-to-covid-19-early-evidence-from-a-survey. They are therefore especially vulnerable to losses due to the government's pandemic-related shutdown orders. Many small businesses purchased business interruption insurance precisely so that the losses from a temporary shutdown would not force them to shut their doors permanently.

During the first year of the coronavirus pandemic, an estimated 200,000 businesses closed permanently. Ruth Simon, *Covid-19's Toll on U.S. Business? 200,000 Extra Closures in Pandemic's First Year*, Wall St. J. (Apr. 16, 2021), *available at* https://www.wsj.com/articles/covid-19s-toll-on-u-s-business-200-000-extra-closures-in-pandemics-first-year-11618580619#.

When "small businesses close en masse, an entire sector of the economy suffers," according to one expert. Emily Flitter, *'I Can't Keep Doing This:' Small-Business Owners Are Giving Up*, N.Y. Times (Jul. 13, 2020), *available at* https://www.nytimes.com/2020/07/13/business/small-businesses-coronavirus.html.

"That leads to a big drag on the eventual recovery, . . . [and] is going to make things far worse than they otherwise need to be" for the whole economy. *Id.* (internal quotation marks omitted).

As this Court has acknowledged, insurance policies often use the same or similar terms of coverage, so that a question of the proper judicial interpretation of such terms is often "one of considerable importance to insureds and insurers alike." *Minkler v. Safeco Ins. Co.*, 561 F.3d 1033, 1035 (9th Cir. 2009). Due to the widespread use of business interruption policies similar to the policy involved here, the interpretation of "direct physical loss of or damage to" insured property carries important public policy considerations that could "have a dramatic impact on public policy in California as well as a direct impact on countless citizens of that state." *Kilby v. CVS Pharmacy, Inc.*, 739 F.3d 1192, 1196 (9th Cir. 2013).

B. The Proposed Certified Question Raises Issues that Are Substantial and of Broad Application.

Many of the 4 million small businesses operating in California and their employees may have to depend on the protection they reasonably thought they had purchased with their business interruption insurance premiums to tide them over temporary business losses due to government shutdown.

This Court has indicated that where a judicial resolution of state law issues "will have profound legal, economic, and practical consequences for employers and employees throughout the state of California and will govern the outcome of many

disputes in both state and federal courts in the Ninth Circuit[,] . . . these questions are worthy of decision by the California Supreme Court." *Mendoza v. Nordstrom, Inc.*, 778 F.3d 834, 841 (9th Cir. 2015). *See also Peabody v. Time Warner Cable, Inc.*, 689 F.3d 1134, 1137-38 (9th Cir. 2012) (Where state law issues will affect "many employers and employees throughout California, we believe that the Supreme Court of California . . . is better qualified to answer the certified question in the first instance." (citation and quotation marks omitted)).

C. The Proposed Certified Question Will Not Adversely Affect the California Supreme Court's Caseload.

The Supreme Court of California, like many courts around the country, faces a challenging docket. However, an authoritative decision by that court will result in greater efficiency in resolving the large number of claims that can be expected under business-interruption policies.

D. Certifying the Proposed Question Will Promote the Spirit of Comity and Federalism.

As this Court has observed, where an unsettled issue of state law has potential importance to California businesses and employees, "'[c]omity and federalism counsel that the California Supreme Court, rather than this court, should answer' the certified question." *Vazquez*, 939 F.3d at 1048-49 (quoting *Robinson v. Lewis*, 795 F.3d 926, 928 (9th Cir. 2015)).

Of particular import in this case is avoiding the harm to healthy federalism from "the existence of parallel state and federal proceedings that address the same legal question [which] presents the risk of inconsistent judgments as to the proper interpretation" of the business interruption policy terms. *Doyle v. City of Medford*, 565 F.3d 536, 544 (9th Cir. 2009).

This case, as well, presents an added potential for harm to federalism and comity. If this Court does not make use of the certified question procedure to obtain an authoritative interpretation of the determinative business interruption policy terms in this case, the parties favored by the panel's ruling will consistently file in or remove to federal court, depriving the California Supreme Court of the opportunity to decide an important question of state law affecting numerous state businesses and employees.

Consequently, granting of Mudpie's Petition for Rehearing En Banc is warranted and appropriate, either to reconsider the panel's determination of how the California Supreme Court would construe the policy language at issue in this case or to certify the question to the California Supreme Court to obtain an authoritative declaration of state law on this matter of great importance to California businesses and their employees.

CONCLUSION

For the foregoing reasons, AAJ urges this Court to grant the Petition for Rehearing En Banc.

Respectfully submitted,

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Date: November 5, 2021

CERTIFICATE OF COMPLIANCE

I HEREBY CERTIFY that this brief complies with the type-volume limitation of Federal Rule of Appellate Procedure 29(a)(5) and Circuit Rule 29-2 because this brief contains 3,955 words, excluding the parts of the brief exempted by Federal Rule of Appellate Procedure 32(f). I further certify that this brief complies with the typeface requirements of Federal Rule of Appellate Procedure 32(a)(5) and the type style requirements of Federal Rule of Appellate Procedure 32(a)(6) because this brief has been prepared in a proportionally spaced typeface using Microsoft Word 2016 in 14-point Times New Roman type style.

Date: November 5, 2021

/s/ Jeffrey R. White
JEFFREY R. WHITE

CERTIFICATE OF SERVICE

I, Jeffrey R. White, counsel for amicus curiae and a member of the Bar of this Court, certify that on November 5, 2021, I electronically filed the foregoing document with the Clerk of Court for the United States Court of Appeals for the Ninth Circuit by using the appellate CM/ECF system. I also certify that the foregoing document is being served on this day on all counsel of record via transmission of the Notice of Electronic Filing generated by CM/ECF. All participants in this case are registered CM/ECF users.

/s/ Jeffrey R. White
JEFFREY R. WHITE