



Hype it or Hate it: How Relevant Is the *MDS Inc. v. Factory Mutual Insurance Inc.* Decision to Covid-19 Business Interruption Claims?

By Alex Reyes and Sonya Katrycz

In standard BI policies, proof of direct physical loss of or damage to the insured property is a threshold requirement to engage coverage. Historically, the physical loss or damage requirement has lent itself to a relatively straightforward interpretation in cases involving tangible, measurable damage to the insured property, such as fires and floods. Claims for BI insurance resulting from COVID-19, however, ask insurers to determine whether impaired function or loss of use of the premises as a result of an unseen viral threat constitutes physical loss or damage within the meaning of the policy so as to engage coverage.

A recent decision of the Ontario Superior Court of Justice in *MDS Inc. v. Factory Mutual Insurance Inc.*, 2020 ONSC 1924 [“*MDS*”], has attracted significant attention for its potential impact on this question. The case considers the availability of business interruption insurance in the context of leak-induced corrosion at a nuclear facility, and has generated some optimism for business owners eager to access the same type of insurance in relation to coronavirus business loss. But, while the facts in *MDS* have some interesting parallels to COVID-19 related business losses, there are a number of key differences that make it an imperfect analog. We advise caution.

The *MDS* Decision

The plaintiff, MDS, was in the business of selling radioisotopes which it obtained through a primary supplier, the Nuclear Research Universal Reactor (NRU). The plaintiff purchased an insurance policy from Factory Mutual which included, among other things, all-perils coverage against business interruption losses. The policy extended coverage to interruptions sustained by MDS’ suppliers, including the NRU. When the NRU experienced an unanticipated leak of heavy water which contained radioactive material, the facility was proactively shutdown and the plaintiff lost more than \$121 million in revenue.

The plaintiff subsequently claimed BI coverage for its business losses under the policy. Factory Mutual denied coverage on the basis that the leak was caused by corrosion, which was an excluded source of loss under the policy. The plaintiff argued that the corrosion exclusion did not apply but, even if it did, there was an exception for “resulting physical damage” caused by corrosion which brought the losses back within coverage. Factory Mutual argued that loss of use of the insured premises did not constitute “resulting physical damage” within the meaning of the policy.

The Court ultimately agreed with the plaintiff. It held that the corrosion exclusion did not apply since the exclusion only applied to non-fortuitous corrosion and, based on the expert evidence (including the insurer’s own expert witness), the corrosion in this case was fortuitous and not caused by regular wear and tear.

Despite its finding that the corrosion exclusion did not apply, the Court also considered whether, assuming the corrosion exclusion did apply, the “resulting physical damage” exception to the exclusion applied to bring the losses back within coverage. The Court noted that the policy did not define “resulting physical damage” or “physical damage”, and that previous Canadian jurisprudence was



unsettled on the meaning of this phrase for BI policies. After reviewing Canadian and American cases which suggested competing interpretations (a narrow versus broad interpretation, respectively), and considering the reasonable expectation of the parties for this particular policy, the Court favoured a broad interpretation of the meaning “physical damage” which included loss of use of the insured premises.

We note that the decision is currently under appeal.

Does *MDS* Assist Insureds Making a COVID-19 Related BI Claim?

Some commentators have suggested that *MDS* may stand for a general proposition that businesses forced to shut down, even in the absence of tangible physical damage, are entitled to business interruption coverage and therefore will be of assistance to insureds making COVID-19 related BI claims. However, we caution that there are a number of reasons that *MDS* will be of limited assistance to insureds making such claims.

First, given the variance in policy wordings between insurers, every insurance policy must be assessed on its own terms and conditions. *MDS* involved a unique policy and a unique set of facts. In *MDS*, the plaintiff obtained an all-risk policy that expressly covered a loss of business income arising from a failure of a third party supplier (the NRU) to supply a product. The case also involved a loss that originated from a physical event (a heavy water leak), with the question of the meaning of “physical damage” only relating to a specific exception to an exclusion. In this context, the Court reasoned that a broad interpretation of the phrase, together with the reasonable expectation of the parties for this particular policy, warranted interpreting “physical damage” in the exception to the exclusion to include a loss of use of insured property. The court’s reasoning on this narrow issue cannot be said to apply broadly to the interpretation of “physical loss or damage” in all BI policies generally. In fact, many policies contain specific exclusions for “loss of use” and/or “loss of occupancy”.

Second, since the Court’s decision in this case was based primarily on its finding that the corrosion exclusion did not apply to exclude coverage, its comments regarding the interpretation of “physical damage” under the policy are arguably *obiter* and may be considered to have limited precedential value.

Further, since *MDS* is not a case that involved a virus or microorganism, it does not address many of the anticipated challenges insureds will face in making a COVID-19 BI claim, including the difficulty proving the presence of COVID-19 on the premises, and the applicability of an infectious/communicable disease exclusion or contamination exclusion that may exclude coverage for COVID-19. It is anticipated that these issues remain significant hurdles for insureds making a COVID-19 related BI claim to overcome.

Finally, it is important to keep in mind the BI policies typically cover only the period of the time it takes to restore the premises and usually include a one or two week waiting period deductible. For businesses that suspend operations due to the presence of COVID-19 on insured property, in practice, the length of time required to sanitize the insured’s premises may be less than the waiting period deductibles common to such policies.



Although *MDS* may suggest a willingness by the court to consider non-tangible losses as “physical damage” in certain instances, we continue to expect that the insureds will have significant challenges in making successful COVID-19 related BI claims.

ZTGH’s Coverage Practice Group will continue to closely monitor the legal and business implications associated with the COVID-19 pandemic and report on further developments.

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Alex’s clients rely on his detail-oriented, creative and practical solutions to their legal problems. With a broad and varied insurance litigation practice, Alex has a breadth of knowledge in a number of practice areas. He defends a wide range of personal injury claims on behalf of insurers and self-insured clients, including motor vehicle liability, occupiers’ liability, commercial general liability, and product liability matters. He also has significant experience defending professional negligence claims, including claims against lawyers, financial advisors, health practitioners, and insurance brokers. In addition, Alex has a special interest in representing insurers on coverage matters, life and critical disability claims, and fraudulent investigations. Alex has appeared as counsel before all levels of Court in Ontario, as well as FSCO and WSIAT. Alex was called to the bar in 2011.

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