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IN THE COURT OF APPEALS OF NORTH CAROLINA

No. COA23-305

Filed 21 November 2023

Mecklenburg County, No. 21 CVS 9525

CATO CORPORATION, a Delaware corporation, et al., Plaintiffs-Appellants,

v.

ZURICH AMERICAN INSURANCE COMPANY, a New York corporation,
Defendant-Appellee.

Appeal by Plaintiffs-Appellants from Order entered 10 January 2023 by Judge
Forrest Donald Bridges in Superior Court, Mecklenburg County. Heard in the Court
of Appeals 1 November 2023.

Robinson, Bradshaw & Hinson, P.A. by R. Steven DeGeorge and Benjamin C. DeCelle, and Kozyak Tropin & Throckmorton LLP, by Benjamin J. Widlanski and Gail A. McQuilkin, pro hac vice, for Plaintiffs-Appellants.

Brooks, Pierce, Mclendon, Humphrey & Leonard, L.L.P., by Gary S. Parsons and Kimberly M. Marston; Teague Campbell Dennis & Gorham, LLP, by William A. Bulfer, Megan N. Silver, and Daniel T. Strong; and Akerman LLP, by Anthony W. Morris, pro hac vice, for Defendant-Appellee.

ARROWOOD, Judge.

Cato Corporation, et al. (“plaintiffs”) appeal from an order entered pursuant to
North Carolina Rule of Civil Procedure 12(b)(6) dismissing plaintiffs’ Amended

Complaint against Zurich American Insurance Company (“defendant”). For the reasons explained below, we affirm the trial court’s decision.

I. Background

Plaintiffs operate more than 1,300 clothing stores in North Carolina and thirty-six other states. Plaintiffs purchased a commercial property insurance policy (“the policy”) from defendant in July 2019. The policy’s insuring agreement states, “This Policy Insures against direct physical loss of or damage caused by a Covered Cause of Loss to Covered Property, at an Insured Location . . . all subject to the terms, conditions and exclusions stated in this Policy.” The policy defines “Covered Cause of Loss” as “[a]ll risks of direct physical loss of or damage from any cause unless excluded.” The policy does not define the language “direct physical loss of or damage.”

Under the policy, defendant is required “to pay for the actual Time Element loss the Insured sustains, as provided in the Time Element Coverages, during the Period of Liability.” The policy’s time element coverages included gross earnings, extra expenses, and leasehold interest. “Period of liability” is defined in the policy as “the period starting from the time of physical loss or damage . . . and ending when with due diligence and dispatch the building and equipment could be repaired or replaced, and made ready for operations under the same or equivalent physical and operating conditions that existed prior to the damage.”

On 14 June 2021, plaintiffs filed a complaint in Superior Court, Mecklenburg County, asserting that defendant failed to honor its contractual obligations under the

policy defendant sold to plaintiff. Plaintiffs filed an amended complaint on 11 March 2022. The amended complaint’s allegations in pertinent part states:

95. An actual and bona fide justiciable controversy exists between [plaintiffs] and [defendant] as to their respective rights and obligations under [the policy] that provides coverage for business earnings loss and extra expense incurred in that:
 - a. [Plaintiffs] . . . incurred physical loss or damage to the Covered Properties from the COVID Virus, pandemic and governmental orders;
 - b. [Plaintiffs] . . . incurred time element earnings loss and extra expenses due to the COVID Virus, pandemic, and governmental orders;
 - c. Due to the nature of its business operations, [plaintiffs] suffered an involuntary physical loss or damage to Covered Properties that resulted from the COVID Virus, pandemic, and governmental orders;
 - d. [Plaintiffs] contend[] that the COVID Virus, pandemic and governmental orders trigger coverage under [the policy’s] time element loss provision, which does not include an exclusion for a pandemic;
 - e. {Plaintiffs} further contends that the COVID Virus, pandemic, and governmental orders trigger “additional coverage” under [the policy]; and
 - f. [Defendant] disputes that [plaintiffs’] lost earnings, and extra expense from time element loss . . . and any other coverages provided for in [the policy], provide coverage related to the COVID Virus, pandemic, and governmental orders.

. . . .

106. [Defendant] has refused performance under [the

policy]. Specifically, in its March 17, 2021 reservation of rights letter . . . [defendant] wrongfully failed to affirm coverage for unexpected and unexcluded causes of loss . . . due to the COVID Virus, pandemic, governmental orders, and related circumstances. [Defendant's] reservation of rights letter . . . constitutes a constructive denial of coverage under [the policy].

On 11 April 2022, defendant moved to dismiss plaintiffs' amended complaint. In its motion, defendant stated the complaint failed to state a claim upon which relief can be granted "pursuant to the express written terms, conditions, limitations, and exclusions of the Policy." Defendant's motion was heard on 10 November 2022. In a 10 January 2023 order, the trial court dismissed the claim, finding that

North State Deli v. Cincinnati Ins. Co., 875 S.E.2d 590 (2022) is authoritative and warrants dismissal of [p]laintiffs' Amended Complaint.

[T]he Court of Appeals in *North State* concluded that the relevant provisions of the policies are unambiguous and that, in order for a loss to be covered by the policy, the loss must have resulted from physical harm to the property of the insured. Although Plaintiffs alleged in the Amended Complaint that the COVID-19 virus caused physical damage to the covered properties, this allegation is not sufficient to overcome the overwhelming body of case law in which this same issue has been considered. In such cases, courts have concluded that, under the plain language of the policies, only direct, accidental, physical loss or damage to the property is covered.

Plaintiffs filed a notice of appeal on 7 February 2023.

II. Discussion

Plaintiffs contend that the trial court erred by misreading this Court's precedent to allow defendant's wrongful denial of coverage for physical loss or damage caused by the COVID-19 virus ("the virus"). As such, plaintiffs assert that they sufficiently alleged that the virus caused "physical damage to the Covered Properties." Plaintiffs also contend that "the phrase 'direct physical loss or damage' in the Zurich policy is ambiguous" and "mandates that the language be construed in [plaintiffs'] favor[.]"

A. Standard of Review

"On a Rule 12(b)(6) motion to dismiss, the question is whether, as a matter of law, the allegations of the complaint, treated as true, state a claim upon which relief can be granted." *Wood v. Guilford Cnty.*, 355 N.C. 161, 166 (2002) (citation omitted). "For purpose of the motion, the well-pleaded material allegations of the complaint are taken as admitted; but conclusions of law or unwarranted deductions of fact are not admitted." *Sutton v. Duke*, 277 N.C. 94, 98 (1970) (cleaned up).

Dismissal pursuant to Rule 12(b)(6) is appropriate when any of the following three conditions are satisfied: "(1) the complaint on its face reveals that no law supports the plaintiff's claim; (2) the complaint on its face reveals the absence of facts sufficient to make a good claim; or (3) the complaint discloses some fact that necessarily defeats the plaintiff's claim." *Wood*, 355 N.C. at 166 (citation omitted).

"[D]etermining the meaning of language in an insurance policy presents a question of law for the Court." *Accardi v. Hartford Underwriters Ins. Co.*, 373 N.C.

292, 295 (2020) (citation omitted). On appeal, we review these questions of law de novo. *Register v. White*, 358 N.C. 691, 693 (2004). “The party seeking coverage under an insurance policy bears the burden to allege and prove coverage.” *N.C. Farm Bureau Mut. Ins. Co. v. Martin*, 376 N.C. 280, 285 (2020) (cleaned up).

B. Case Precedent and Complaint Allegations

Plaintiffs contend that the trial court misread this Court’s precedent in its ruling and that they sufficiently alleged that the virus caused physical damage to their properties. We disagree.

1. Case Precedent

In *North State Deli, LLC v. Cincinnati Ins. Co.*, this Court interpreted the policy language, “accidental physical loss or accidental physical damage.” 284 N.C. App. 330, 332 (2022). In its ruling favoring the defendant, this Court held that “[p]laintiffs’ desired definition of ‘physical loss’ as a general ‘loss of use’ is not supported by our caselaw or the unambiguous language in the Policies” and that “only *direct*, accidental, *physical* loss or damage to the property is covered.” *Id.* at 334 (alterations in original); see also *Four Roses, LLC v. First Protective Ins. Co.*, 284 N.C. App. 561, 2022 WL 2813270, at *3 (2022) (unpublished) (holding that the trial court did not err in granting defendant’s 12(b)(6) motion because the plaintiff failed to allege “‘direct physical loss’ to the dwelling itself as required by the plain and unambiguous terms of the Policy.”).

Lastly, in *Harry's Cadillac-Pontiac-GMC Truck Co. v. Motors Ins.*—a case relied upon by *North State Deli* and *Four Roses*—plaintiff argued “its inability to gain access to the dealership due to the snowstorm rendered the business as lost to plaintiff as it would have been had the storm leveled the premises, and that this loss triggered coverage.” 126 N.C. App. 698, 699–700 (1997) (cleaned up).

In *Harry's Cadillac*, this Court interpreted the policy language, “direct physical loss of or damage” by incorporating language from the policy’s definition for “Period of Restoration.” *Id.* at 701–02. Specifically, the insurance “policy defined ‘Period of Restoration’ as the period between the date of direct physical loss or damage and the date when the property should be repaired, rebuilt, or replaced with reasonable speed and similar quality.” *Id.* (cleaned up). The *Harry's Cadillac* Court thus ruled that “only those losses requiring repair, rebuilding, or replacement” are covered by the policy. *Id.* at 702.

By incorporating the “Period of Restoration” provision, *Harry's Cadillac* explained that the policy required that the property in question be “tangibly altered” to trigger coverage. *See Palm & Pine Ventures, LLC v. Certain Underwriters at Lloyd's London*, No. 2:20-CV-00077-M, 2022 WL 533073, at *5–6 (E.D.N.C. Feb. 22, 2022) (unpublished) (“*Harry's Cadillac* resolves the parties’ underlying dispute about whether the property must be tangibly altered” and “[p]laintiffs have not presented, nor has the court found, persuasive evidence that the Supreme Court of North Carolina would discard this tangible alteration requirement.”); *see also Uncork &*

Create LLC v. Cincinnati Ins. Co., 27 F.4th 926, 933 (4th Cir. 2022) (holding that the insurance policy did not apply to plaintiff's claim because "the Covid-19 virus [did not cause] present or impending material destruction or material harm that physically altered the covered property requiring repairs or replacement so that they could be used as intended."); *Death & Taxes, LLC v. Cincinnati Ins. Co.*, No. 5:21-CV-125-D, 2022 WL 337196, at *1 (E.D.N.C. Feb. 2, 2022), *aff'd*, No. 22-1237, 2023 WL 2182888 (4th Cir. Feb. 23, 2023) (unpublished) ("Numerous courts have construed materially indistinguishable insurance policy language during the COVID-19 pandemic and have overwhelmingly concluded that such policy language requires tangible, physical destruction of property."); *Golden Corral Corp. v. Illinois Union Ins. Co.*, 559 F. Supp. 3d 476, 486 (E.D.N.C. 2021), *aff'd*, No. 21-2119, 2022 WL 3278938 (4th Cir. Aug. 11, 2022) (explaining that "[t]he 'Period of Recovery' provision comports with a reading of the [other relevant] clauses that requires a showing of tangible, physical loss, damage, or destruction."). While these federal cases are not controlling legal authority, we find them helpful in our analysis.

Here, plaintiffs claim that the trial court misread *North State Deli* because, in that case, the insureds did not allege that their loss resulted from physical harm to their property; rather, the insureds merely alleged that the government closure orders "resulted in loss of business." *North State Deli*, 284 N.C. App. at 333–34. However, in this case, because plaintiffs allege the virus caused physical damage to its Covered Properties, plaintiffs assert that *North State Deli* "does not control the

outcome[.]” Plaintiffs assert in their reply brief that *Harry’s Cadillac* and *Four Roses* also do not control because—like in *North State Deli*—“[t]here were no allegations that the covered properties suffered actual physical loss or damage.” We are not persuaded.

The policy’s language—“direct physical loss of or damage”—is precisely the same language interpreted in *Harry’s Cadillac*. Further, the policy’s definition for “period of liability” is substantially similar to the definition for “period of restoration” in *Harry’s Cadillac*. Specifically, like in *Harry’s Cadillac*, the “period of liability” ends when the property “could be repaired or replaced, and made ready for operations[.]” Therefore, when construing the policy as a whole and bringing its “period of liability” provision into harmony with the other provision, it is clear that tangible alteration to the property is necessary to trigger coverage. *See Wachovia Bank & Tr. Co. v. Westchester Fire Inc. Co.*, 276 N.C. 348, 355 (1970) (“Where the immediate context in which words are used is not clearly indicative of the meaning intended, resort may be had to other portions of the policy and all clauses of it are to be construed, if possible, so as to bring them into harmony.”)

2. Allegations that the COVID-19 Virus Caused Physical Damage

Plaintiffs alleged the virus “caused tangible physical transformation of the air and surfaces at [plaintiffs’] Covered Properties” and “adhered to all objects and surfaces in the Covered Properties, and poisoned the atmospheres[.]” Additionally, plaintiffs alleged the virus “transformed Covered Properties into dangerous vectors

of illness and disease, and required ongoing remediation and reconfiguration of the physical loss and damage to the Covered Properties.” Plaintiffs also alleged that routine cleaning failed to eliminate the virus and that the use of “harsh and abrasive chemicals . . . cause[d] additional physical damage.”

Plaintiffs’ allegations are “unwarranted deductions of fact[.]” *Sutton*, 277 N.C. at 98. Although the properties may have required “reconfiguration” or rearrangement to facilitate social distancing, the record does not indicate any “physical transformation” of plaintiffs’ properties. See *Uncork & Create LLC v. Cincinnati Ins. Co.*, 498 F. Supp. 3d 878, 883 (S.D.W. Va. 2020), *aff’d*, 27 F.4th 926 (4th Cir. 2022) (“COVID-19 does not threaten the inanimate structures covered by property insurance policies, and its presence on surfaces can be eliminated with disinfectant.”); see also *Golden Corral Corp.*, 559 F. Supp. 3d at 487 (“[A]lthough virus particles may have landed on some of Golden Corral’s covered property or nearby property, Golden Corral still has its property and COVID-19 has not caused the property to need rebuilding, repair, or replacement.”); *Colectivo Coffee Roasters, Inc. v. Soc’y Ins.*, 401 Wis. 2d 660, 672, 974 N.W.2d 442, 447 (2022) (“As the overwhelming majority of the other courts that have addressed the same issue have concluded, the presence of COVID-19 does not constitute a physical loss of or damage to property because it does not ‘alter the appearance, shape, color, structure, or other material dimension of the property.’”). Again, we find these cases from other courts helpful in our analysis.

Plaintiffs' claim that the virus required them to use "harsh and abrasive chemicals[.]" which created additional physical damage is also without merit. Even if the use of these chemicals in fact physically damaged the property, the virus did not directly cause the damage, the cleaning did. Further, plaintiffs' claim that the virus "poisoned the atmospheres" also fails because "atmospheres" or "air" do not constitute "covered property" under the policy.¹

Accordingly, under the plain language of the policy, binding precedent, and persuasive case law in the Fourth Circuit and other jurisdictions, the trial court's dismissal was proper in that plaintiffs failed to allege that the virus caused a direct physical loss of or damage to its properties.

C. Interpretation of "Direct Physical Loss of or Damage"

Plaintiffs contend that the phrase "direct physical loss [of] or damage" in the policy is ambiguous and therefore must be construed to provide coverage for "loss of use." We disagree.

"North Carolina courts have long held that any ambiguity or uncertainty as to the words used in the policy should be construed against the insurance company and in favor of the policyholder or beneficiary." *Accardi*, 373 N.C. at 295 (citation

¹ Section 3.01 of the policy limits "covered property" to (1) "[t]he Insured's interest in buildings (or structures)[.]" (2) "[t]he Insured's interest in Personal Property[.]" (3) "Property of Others" in limited situations, and (4) "Personal Property of officers and employees of the Insured."

omitted). “If a court finds that no ambiguity exists, however, the court must construe the document according to its terms.” *Id.* (citation omitted).

“Ambiguity is not established by the mere fact that the insured asserts an understanding of the policy that differs from that of the insurance company.” *Id.* (citing *Wachovia Bank & Tr. Co.*, 276 N.C. at 354). “Rather, ambiguity exists if, in the opinion of the court, the language is ‘fairly and reasonably susceptible to either of the constructions for which the parties contend.’” *Id.* (quoting *Wachovia Bank & Tr. Co.*, 276 N.C. at 354). “If the policy fails to define a term, the court must define the term in a manner that is consistent with the context in which the term is used, and the meaning accorded to it in ordinary speech.” *Id.* (citation omitted).

Further, “[w]here the immediate context in which words are used is not clearly indicative of the meaning intended, resort may be had to other portions of the policy and all clauses of it are to be construed, if possible, so as to bring them into harmony.” *Wachovia Bank & Tr. Co.*, 276 N.C. at 355 (citation omitted). “Each word is deemed to have been put into the policy for a purpose and will be given effect, if that can be done by any reasonable construction in accordance with the foregoing principles.” *Id.* (citation omitted).

Here, as this Court’s precedent makes clear, the phrase “direct physical loss of or damage” is unambiguous in that it does not encompass a “loss of use.” *See North State Deli*, 284 N.C. App. at 334 (“Plaintiffs’ desired definition of ‘physical loss’ as a general ‘loss of use’ is not supported by our caselaw or the unambiguous language in

the Policies.”); *Harry’s Cadillac*, 126 N.C. App. at 702 (holding “that, under the language of the business interruption clause of the policy, [which is cabined by the phrase ‘direct physical loss of or damage,’] coverage is provided only when loss results from suspension of operations due to damage to, or destruction of, the business property by reason of a peril insured against.”).

Federal Circuit cases also agree that substantially similar policy language does not provide coverage for “loss of use” of property. *See Uncork and Create LLC*, 27 F.4th at 933 (holding that the policy’s coverage does not apply to claims “for financial losses in the absence of any material destruction or material harm” and “observ[ing] that our holding is consistent with the unanimous decisions by our sister circuits, which have applied various states’ laws to similar insurance claims and policy provisions.”).²

Plaintiffs also contend that the phrase “direct physical loss of or damage” is ambiguous because the word “physical” modifies “loss” but not “damage.” Thus, plaintiffs argue, “coverage does not require ‘physical’ alteration of the Covered Properties.” We do not need to address this modification issue because, as discussed above, when the “period of liability” provision is incorporated with the phrase “direct

² The only North Carolina case plaintiffs point to in support of their contention that the policy encompasses a “loss of use” is an unpublished one this Court is not bound by. *See Great Am. Ins. Co. v. Mesh Cafe, Inc.*, 158 N.C. App. 312, 2003 WL 21267942 (2003) (unpublished).

physical loss of or damage[,]” and the policy is construed harmoniously, tangible alteration is necessary.³

Lastly, because the policy is unambiguous and plaintiffs failed to sufficiently allege “physical loss of or damage” to their property, determining whether coverage is barred by a policy exclusion is not needed. *See Fortune Ins. Co. v. Owens*, 351 N.C. 424, 430 (2000) (“A party seeking benefits under an insurance contract has the burden of showing coverage” and “[u]ntil a prima facie case of coverage is shown, the insurer has no burden to prove a policy exclusion.” (citations omitted)). Accordingly, the phrase “direct physical loss of or damage” in the policy is not ambiguous and need not be construed in favor of plaintiffs.

III. Conclusion

For the foregoing reasons, the trial court’s order is affirmed.

AFFIRMED.

Judges CARPENTER and FLOOD concur.

Report per Rule 30(e).

³ Although we do not address the modification issue, we note that in *SAS Int’l, Ltd. v. Gen. Star Indem. Co.*, the First Circuit adopted the lower court’s interpretation “that the word ‘physical’ modifies both ‘loss’ and ‘damage,’ and that each term, as modified, requires ‘tangible damage.’” *SAS Int’l, Ltd. v. Gen. Star Indem. Co.*, 36 F.4th 23, 25–26 (1st Cir. 2022) (citing *SAS Int’l, Ltd. v. Gen. Star Indem. Co.*, 520 F. Supp. 3d 140, 143 (D. Mass. 2021)).