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**UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF CALIFORNIA**

ISLANDS RESTAURANTS, LP a
Delaware Limited Partnership; and CFBC,
LLC, a California Limited Liability
Company,

Plaintiffs,

v.

AFFILIATED FM INSURANCE
COMPANY, a corporation; and DOES 1
through 50, inclusive,

Defendants.

Case No.: 3:20-cv-02013-H-JLB

**ORDER GRANTING DEFENDANT’S
MOTION FOR JUDGMENT ON THE
PLEADINGS**

[Doc. No. 15.]

On September 15, 2020, Plaintiffs Islands Restaurants, LP and CFBC, LLC (“Plaintiffs”) filed a complaint against Defendant Affiliated FM Insurance Co. (“Defendant”) in the Superior Court of California, County of San Diego. (Doc. No. 22-1.) On October 14, 2020, Defendant removed the action. (Doc. No. 1.) On January 29, 2021,

1 Defendant filed a motion for judgment on the pleadings. (Doc. No. 15.) Plaintiffs filed a
2 response in opposition to Defendant’s motion on February 23, 2021. (Doc. No. 19.) On
3 March 1, 2021, Defendant filed a reply. (Doc. No. 20.) The Court held a hearing on the
4 matter on March 29, 2021. (Doc. No. 25.) Michael J. Bidart and Danica Crittenden
5 appeared for Plaintiffs, and Amy M. Churan and Daniel L. Allender appeared for
6 Defendant. (Id.) For the following reasons, the Court grants Defendant’s motion for
7 judgment on the pleadings.

8 **Background**¹

9 Plaintiff Islands Restaurants, LP (“Islands”) owns and operates approximately fifty
10 tropical-themed restaurants located in California, Arizona, and Hawaii. (Doc. No. 22-1 ¶¶
11 3-4.) In 2015, Islands partnered with Plaintiff CFBC, LLC, the owner and operator of
12 several French-style bakery cafes located in California. (Id. ¶ 42.) Prior to 2020, both
13 chains enjoyed “successful historical sales and customer traffic.” (Id. ¶ 44.)

14 But in early 2020, governments in the jurisdictions Plaintiffs operate issued various
15 closure orders (the “Closure Orders”), limiting Plaintiffs’ operations during the COVID-
16 19 pandemic. (Id. ¶¶ 61-116.) Plaintiffs summarized the impact of the Closure Orders in
17 their complaint. (Id. ¶¶ 61-62.) According to them, the Closure Orders initially prohibited
18 all dine-in services in March 2020, allowed for limited indoor and outdoor dine-in services
19 around May 2020, and then suspended all indoor dine-in services around July 2020. (Id.)
20 Plaintiffs allege that their compliance with these orders caused them to lose business
21 income. (Id. ¶¶ 44, 63-64.)

22 Before the COVID-19 pandemic, Plaintiffs purchased a commercial property and
23 general liability insurance policy (the “Policy”) from Defendant, with a coverage period
24 ranging from August 1, 2019 to August 1, 2020. (Id. ¶ 6.) The Policy generally covers
25 Plaintiffs’ property “against ALL RISKS OF PHYSICAL LOSS OR DAMAGE,” unless
26 the risk is otherwise excluded. (Id. ¶ 27 (emphasis in original).) The Policy also provides
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28 ¹ The following allegations are taken from Plaintiffs’ complaint unless otherwise provided.

1 “business interruption” coverage for certain losses incurred “as a direct result of physical
2 loss or damage of the type insured” to covered property. (Id. ¶¶ 29-30.) The policy does
3 not define “physical loss or damage.” (Id. ¶ 28.) These coverage provisions are subject to
4 exclusions for losses deriving from the “[l]oss of market or loss of use” of the covered
5 property or from the inability to use the covered property because of “contamination.” (Id.
6 ¶¶ 33-34.)

7 On March 27, 2020, Plaintiffs filed a claim under the Policy’s business interruption
8 coverage provision for losses resulting from the Closure Orders. (Id. ¶ 117.) Plaintiffs
9 clarified and conceded that they are not making a claim under any other coverage provision
10 of the Policy, including the Policy’s communicable disease provisions. After a substantial
11 back and forth between the parties, (id. ¶¶ 118-56), on July 25, 2020, Defendant denied
12 business interruption coverage for each of Plaintiffs’ restaurants because Plaintiffs’ losses
13 did not directly result from “physical loss or damage” and, regardless, were excluded under
14 the Policy’s loss of use and contamination exclusions, (id. ¶¶ 157-60). On September 15,
15 2020, Plaintiffs filed the instant action, alleging that Defendant breached the Policy by
16 denying their claim and, in so doing, also breached the implied covenant of good faith and
17 fair dealing. (Id. ¶¶ 166-78.)

18 Discussion

19 **I. Legal Standards**

20 **A. Motion for Judgment on the Pleadings**

21 Federal Rule of Civil Procedure 12(c) permits a district court to terminate a lawsuit
22 where the facts alleged in the pleadings demonstrate that the moving party is entitled to
23 judgment as a matter of law. See Daewoo Elecs. Am. Inc. v. Opta Corp., 875 F.3d 1241,
24 1246 (9th Cir. 2017). In reviewing a Rule 12(c) motion, a district court must accept as true
25 all facts alleged in the pleadings and draw all reasonable inferences in favor of the non-
26 moving party. See Gregg v. Hawaii Dep’t of Pub. Safety, 870 F.3d 883, 887 (9th Cir.
27 2017). But because “Rule 12(c) is ‘functionally identical’ to Rule 12(b)(6),” a court need
28 not accept legal conclusions as true. Cafasso, U.S. ex rel. v. Gen. Dynamics C4 Sys., Inc.,

1 637 F.3d 1047, 1054 n.4 (9th Cir. 2011) (citation omitted). In addition, a court may
2 consider documents incorporated into the complaint by reference and items subject to
3 judicial notice. See Coto Settlement v. Eisenberg, 593 F.3d 1031, 1038 (9th Cir. 2010).

4 **B. California Insurance Law**

5 In California, the interpretation of an insurance policy is a question of law for the
6 court. Powerine Oil Co., Inc. v. Superior Court, 118 P.3d 589, 597 (Cal. 2005). Such
7 interpretation must give effect to “the mutual intention of the parties at the time the contract
8 is formed” Waller v. Truck Ins. Exch., Inc., 900 P.2d 619, 627 (Cal. 1995). To
9 determine the intent of the parties behind an insurance contract, the Court “look[s] first to
10 the language of the contract in order to ascertain its plain meaning,” reading the language
11 in its “ordinary and popular sense, unless used by the parties in a technical sense or a special
12 meaning is given to them by usage.” Id. (internal citations and quotation marks omitted).
13 When a term is ambiguous, it should be liberally interpreted to protect the insured’s
14 reasonable expectation of coverage. La Jolla Beach & Tennis Club, Inc. v. Indus. Indem.
15 Co., 884 P.2d 1048, 1053 (Cal. 1994). But “[i]f [the] contractual language is clear and
16 explicit, it governs.” Minkler v. Safeco Ins. Co. of Am., 232 P.3d 612, 616 (Cal. 2010).
17 After all, “[a]n insurance company can choose which risks it will insure and which it will
18 not, and coverage limitations set forth in a policy will be respected.” Fidelity & Deposit
19 Co. v. Charter Oak Fire Ins. Co., 78 Cal. Rptr. 2d 429, 432 (Ct. App. 1998) (citing Legarra
20 v. Federated Mutual Ins. Co., 42 Cal. Rptr. 2d 101, 105 (Ct. App. 1995)).

21 **II. Breach of Contract**

22 In order to state a claim under the Policy’s business interruption coverage, Plaintiffs
23 must allege “physical loss or damage” to covered property. (Doc. No. 22-1 ¶¶ 29-30.)
24 Defendant argues that it properly denied Plaintiffs’ business interruption claim because
25 Plaintiffs’ temporary loss of use of their on-site dining facilities does not amount to
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1 “physical loss or damage.” (Doc. No. 15 at 8.)² On the other hand, Plaintiffs contend that
2 the Policy’s “physical loss or damage” requirement is at least ambiguous as to whether it
3 encompasses their circumstances. (See Doc. No. 19 at 4.) Thus, Plaintiffs reason, the
4 Court should deny Defendant’s motion because it should resolve this ambiguity in favor of
5 coverage. (Id.)

6 This Court recently dealt with a similar issue in Unmasked Management, Inc. v.
7 Century-National Insurance Co., 3:20-CV-01129-H-MDD, 2021 WL 242979 (S.D. Cal.
8 Jan. 22, 2021), appeal filed, No. 21-55090 (9th Cir. Feb. 5, 2021). There, restaurant owners
9 likewise argued that the loss of use of their dining facilities during the COVID-19
10 pandemic satisfied a physical loss or damage trigger in their business interruption policy.
11 Id. at *4. The Court, in accordance with California law, interpreted such a trigger to require
12 a “distinct, demonstrable, physical alteration” to property for coverage to attach. Id. The
13 Court then held that the restaurant owners’ alleged temporary loss of the ordinary use of
14 their properties did not satisfy this condition. Id. at *4-6. In so doing, the Court provided
15 the following discussion.

16 Physical loss or damage coverage limitations are commonplace in modern
17 insurance policies. MRI Healthcare Ctr. of Glendale, Inc. v. State Farm Gen.
18 Ins. Co., 115 Cal. Rptr. 3d 27, 37 (2010). Under California law, they generally
19 require that there be a “distinct, demonstrable, physical alteration” to the
20 property for coverage to attach. Id. at 38. “A direct physical loss
21 ‘contemplates an actual change in insured property then in a satisfactory state,
22 occasioned by accident or other fortuitous event directly upon the property
23 causing it to become unsatisfactory for future use or requiring that repairs be
24 made to make it so.’” Id. at 38 (citation omitted). In other words, “some
25 external force must have acted upon the insured property to cause a physical
26 change in the condition of the property, i.e., [the property] must have been
27 ‘damaged’ within the common understanding of that term.” Id.

28 ² Additionally, Defendant argues that, in any event, Plaintiffs fail to state a claim for business
interruption coverage because their losses are excluded under the Policy’s loss of use and contamination
exclusions. (Doc. No. 15 at 16-20.) Because the Court ultimately concludes that the Policy’s business
interruption coverage does not apply in the first place, the Court need not address these exclusions. Waller,
900 P.2d at 625 (“[W]hen an occurrence is clearly not included within the coverage afforded by the
insuring clause, it need not also be specifically excluded.” (citation omitted)).

1 The loss of use or functionality of the covered property alone is not sufficient
2 to trigger coverage. See id. at 37; see also Doyle v. Fireman's Fund Ins. Co.,
3 229 Cal. Rptr. 3d 840, 844 (Ct. App. 2018) (“[W]hen it comes to property
4 insurance, diminution in value is not a covered peril, it is a measure of a loss.”)
5 For example, in MRI Healthcare, the California Court of Appeal held that an
6 MRI machine’s inability to function properly after it was powered down did
7 not constitute a “direct physical loss.” 115 Cal.Rptr.3d at 38-39. Similarly,
8 Ward Gen. Ins. Servs., Inc. v. Employers Fire Ins. Co., 7 Cal. Rptr. 3d 844,
9 850-51 (2003), as modified on denial of reh’g (Jan. 7, 2004), held that the loss
10 of electronic information in a database did not to qualify as a direct physical
11 loss absent a showing that there was damage to tangible property. Further, in
12 Doyle, the court held that an insured’s financial loss resulting from the
13 purchase of counterfeit wine was not covered by his property insurance policy
14 because the wine was never stolen, destroyed, or physically altered. 229 Cal.
15 Rptr. 3d at 843-44.

16 Here, “Plaintiff[s]’ FAC attempts to make precisely this substitution of
17 temporary impaired use or diminished value for physical loss or damage in
18 seeking Business Income and Extra Expense coverage.” 10E, LLC v.
19 Travelers Indem. Co. of Connecticut, No. 2:20-CV-04418-SVW-AS, 2020
20 WL 5359653, at *4–5 (C.D. Cal. Sept. 2, 2020). Plaintiffs are not the first to
21 contend that their temporary and partial loss of use or functionality of their
22 property resulting from the Closure Orders and the COVID-19 pandemic
23 constitutes a “direct physical loss of or damage to” that property. Courts
24 applying California law have all but universally rejected these attempts as
25 lacking the requisite “distinct, demonstrable, physical alteration” necessary to
26 show physical loss or damage. See, e.g., Travelers Cas. Ins. Co. of Am. v.
27 Geragos & Geragos, No. CV 20-3619 PSG (EX), 2020 WL 6156584, at *4-5
28 (C.D. Cal. Oct. 19, 2020); Mudpie, Inc. v. Travelers Cas. Ins. Co. of Am., No.
20-CV-03213-JST, 2020 WL 5525171, at *3-5 (N.D. Cal. Sept. 14, 2020);
Pappy’s Barber Shops, Inc. v. Farmers Grp., Inc., No. 20-CV-907-CAB-
BLM, 2020 WL 5500221, at *4 (S.D. Cal. Sept. 11, 2020); 10E, 2020 WL
5359653, at *4-5. In fact, Plaintiffs point to no citable authority applying
California law holding these allegations are sufficient to state a claim under a
policy with a similar physical loss clause. Accordingly, to the extent that
Plaintiffs argue that they are entitled to coverage for the loss of use or
functionality of their property as a result of the Closure Orders or the COVID-
19 pandemic at large, they fail to plead a “distinct, demonstrable, physical
alteration,” as required under the Policy and California law. See MRI
Healthcare, 115 Cal.Rptr.3d at 38.

Id. (alterations in original).

1 The Court’s analysis in Unmasked Management equally applies here. Plaintiffs
2 essentially make the same allegations: that is, that their partial inability to use their
3 restaurants because of on-site dining restrictions imposed by COVID-19 related closure
4 orders constitutes “physical loss or damage” within the meaning of their business
5 interruption policies. (See, e.g., Doc. No. 22-1 ¶ 148.) Further, the language requiring
6 physical loss or damage in each policy is similar. Compare (*id.* ¶ 30 (requiring a “direct
7 result of physical loss or damage” to covered property)), with Unmasked Mgmt., 2021 WL
8 242979, at *1 (requiring a ““direct physical loss of or damage to’ the covered property”).
9 Nevertheless, Plaintiffs argue that the Court should not follow Unmasked Management, as
10 well as the many federal district court cases applying California law that held similarly,
11 because, according to Plaintiffs, the Court in that case: (1) did not consider whether the
12 policy language was ambiguous in this specific factual context; (2) erroneously concluded
13 that, absent a demonstrable physical alteration to property, only a permanent loss of
14 property would trigger coverage; and (3) did not explicitly address whether its
15 interpretation would defeat the reasonable expectations of the insured.³ (Doc. No. 19 at
16 15-16.) The Court is not persuaded by any of these arguments and will address each in
17 turn.

18 First, the Policy’s “physical loss or damage” requirement is not ambiguous. If a
19 policy term has been “judicially construed” in a “sufficiently analogous context,” that term
20 is “not ambiguous.” McMillin Homes Constr., Inc. v. Natl. Fire & Marine Ins. Co., 247
21 Cal. Rptr. 3d 825, 833 (Ct. App. 2019), review denied (Aug. 28, 2019). Insurance policies
22 commonly contain physical loss or damage coverage triggers. Doyle v. Fireman’s Fund
23 Ins. Co., 229 Cal. Rptr. 3d 840, 843 (Ct. App. 2018) (citation omitted); MRI Healthcare
24 Ctr. of Glendale, Inc. v. State Farm Gen. Ins. Co., 115 Cal. Rptr. 3d 27, 37 (Ct. App. 2010);
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27 ³ Plaintiffs also fault the Court for not discussing four “contrary decisions” that support their
28 arguments. (Doc. No. 19 at 16.) None of these decisions are persuasive because they did not apply
California law. Courts applying California law have all but unanimously held the opposite. Unmasked
Mgt., 2021 WL 242979, at *4-6 (citing cases).

1 Croskey, et al., California Practice Guide: Insurance Litigation ¶ 6:276 (The Rutter Group,
2 Aug. 2020 update) (“Property insurance policies normally cover ‘direct physical loss or
3 damage’ to the insured property, without further defining these terms.”); Plitt, et al., Couch
4 on Insurance § 1148:46 (3d ed., Dec. 2020 update) (explaining that “modern insurance
5 policies, especially of the all-risk type,” are “frequently” triggered by “physical loss or
6 damage”). California courts consistently interpret these coverage triggers to require a
7 “distinct, demonstrable, physical alteration” to property. See, e.g., MRI Healthcare, 115
8 Cal. Rptr. 3d at 38.

9 This case is also sufficiently analogous to those in which California courts have
10 arrived at this construction. As Plaintiffs point out, some of the California cases that
11 interpreted the meaning of similar physical loss or damage terms did so in the context of
12 property insurance, not business interruption insurance. (Doc. No. 19 at 14.) But this
13 distinction is not persuasive because property and business interruption coverage
14 commonly go hand in hand. See Croskey et al., supra ¶¶ 6:276.7-276.8 (noting that
15 business interruption coverage can supplement property insurance policies). In fact, the
16 Policy itself also has property insurance provisions, insuring Plaintiffs’ property against all
17 non-excluded risks of “physical loss or damage.” (Doc. No. 22-1, Ex. 2 at 22.) Plaintiffs
18 also attempt to distinguish the facts of this case from those requiring a physical alteration
19 because of the uniqueness of the COVID-19 pandemic. (Doc. No. 19 at 14.) Yet, Plaintiffs
20 fail to adequately explain why these factual distinctions necessitate a different
21 interpretation. (See id.) The Court sees no reason why California law’s physical alteration
22 requirement should not also apply in this case. Therefore, the Policy’s physical loss or
23 damage trigger is not ambiguous because it has been “judicially construed” in a
24 “sufficiently analogous” context. See McMillin, 247 Cal. Rptr. 3d at 833.

25 Second, the Court is not persuaded by Plaintiffs argument that “physical loss”
26 includes the temporary loss of use of their business premises for certain purposes. To
27 support their interpretation, Plaintiffs cite to Total Intermodal Services Inc. v. Travelers
28 Property Casualty Co. of America, CV-17-04908 AB (KSX), 2018 WL 3829767 (C.D. Cal.

1 July 11, 2018). In Total Intermodal the district court read a similar policy, requiring “direct
2 physical loss of or damage to” property, to cover the “physical loss of” or “physical damage
3 to” property because of the disjunctive phrasing of the clause. Id. at *3-4. The court then
4 reasoned that the “physical loss of” requirement could be satisfied if the insured was
5 permanently dispossessed of the covered property, even if that property was not damaged
6 or physically altered. Id. at *4.

7 Plaintiffs attempt to extend Total Intermodal to include the temporary deprivation of
8 the use of property. (Doc. No. 19 at 11-13.) Yet numerous district courts have rejected
9 this interpretation, including this Court and the district court that authored the Total
10 Intermodal decision in the first place. Unmasked Mgt., 2021 WL 242979, at *5 (citing
11 cases). Such an interpretation would unreasonably extend coverage beyond “manageable
12 bounds,” Mark’s Engine Co. No. 28 Rest., LLC v. Travelers Indem. Co., 2:20-CV-04423-
13 AB-SK, 2020 WL 5938689, at *4 (C.D. Cal. Oct. 2, 2020), appeal filed, No. 20-56031 (9th
14 Cir. Oct. 6, 2020) (citation omitted); Wellness Eatery La Jolla LLC v. Hanover Ins. Group,
15 20CV1277-AJB-RBB, 2021 WL 389215, at *6 (S.D. Cal. Feb. 3, 2021) (citation omitted),
16 because “potentially any regulation that limits a business’s operations would trigger
17 coverage,” Plan Check Downtown III, LLC v. AmGuard Ins. Co., 485 F. Supp. 3d 1225,
18 at *6 (C.D. Cal. 2020), appeal filed, No. 20-56020 (9th Cir. Oct. 2, 2020).⁴ Thus, Plaintiffs’
19 alternative interpretation of the Policy’s “physical loss or damage” clause does not render
20 the policy ambiguous. Cf. Doyle, 229 Cal. Rptr. 3d at 842 (“An insurance policy provision
21 is ambiguous when it is capable of two or more constructions, both of which are
22 reasonable.” (citation omitted)).

23 Third, because the Policy’s “physical loss or damage” clause is unambiguous, the
24 Court need not consider Plaintiffs’ arguments regarding their reasonable expectations of
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26 ⁴ For the same reason, the Court does not find persuasive Plaintiffs’ argument that an “idle period”
27 exclusion in the policy may be rendered superfluous if a physical alteration to the property is required.
28 (Doc. No. 19 at 12); Wellness Eatery, 2021 WL 389215, at *6 (“[T]he fact that some redundancy results
is not fatal’ where the ‘the court has adopted the only reasonable construction of the contract.’” (citation
omitted)).

1 coverage. Under California law, “an insured’s . . . objectively reasonable expectations may
2 be considered to resolve an ambiguous policy provision . . . but cannot be relied upon to
3 create an ambiguity where none exists.” Lee v. Fid. Natl. Title Ins. Co., 115 Cal. Rptr. 3d
4 748, 759 (Ct. App. 2010) (omissions in original) (citation and internal quotation marks
5 omitted). In sum, the Court grants Defendant’s motion with respect to Plaintiffs’ breach
6 of contract claim because Plaintiffs fail to allege the requisite “distinct, demonstrable,
7 physical alteration” to their property. Unmasked Mgmt., 2021 WL 242979, at *4-5.

8 **III. Breach of the Covenant of Good Faith and Fair Dealing**

9 Plaintiffs also allege a claim against Defendant for the breach of the implied
10 covenant of good faith and fair dealing. (Doc. No. 22-1 ¶¶ 166-73.) “Every contract
11 imposes upon each party a duty of good faith and fair dealing in its performance and its
12 enforcement.” Major v. W. Home Ins. Co., 87 Cal. Rptr. 3d 556, 567 (Ct. App. 2009), as
13 modified on denial of reh’g (Jan. 30, 2009). “[T]o establish the insurer’s ‘bad faith’
14 liability, the insured must show that the insurer has (1) withheld benefits due under the
15 policy, and (2) that such withholding was ‘unreasonable’ or ‘without proper cause.’” Id.
16 Here, because Plaintiffs are not “due” any benefits under the Policy’s general business
17 interruption provision, they fail to state a claim for bad faith. See id.; see also Waller, 900
18 P.2d at 639 (“It is clear that if there is no potential for coverage and, hence, no duty to
19 defend under the terms of the policy, there can be no action for breach of the implied
20 covenant of good faith and fair dealing because the covenant is based on the contractual
21 relationship between the insured and the insurer.”). Accordingly, the Court grants
22 Defendant’s motion for judgment on the pleadings as to Plaintiffs’ claim for breach of the
23 implied covenant of good faith and fair dealing.

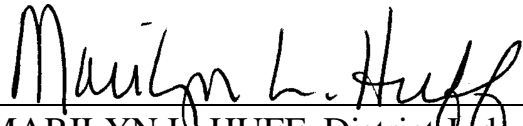
24 **Conclusion**

25 The Court complements the parties for their thoughtful discussion during the hearing
26 on this matter. The Court also sympathizes with Plaintiffs and other businesses suffering
27 financial hardships during the COVID-19 pandemic. Nevertheless, the issue before the
28 Court is whether Plaintiffs’ alleged losses are covered by the Policy, which they are not.

1 Therefore, the Court grants Defendant's motion for judgment on the pleadings. The Court
2 directs the Clerk to enter judgment in favor of Defendant and close the case.

3 **IT IS SO ORDERED.**

4 DATED: April 2, 2021

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6 MARILYN L. HUFF, District Judge
7 UNITED STATES DISTRICT COURT
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