FORUM OF INSURANCE LAWYERS

Informing Progress - Shaping the Future

FOIL UPDATE 15 January 2021

Update – Business Interruption Test Cases

The Financial Conduct Authority v Various Insurers (2021) UKSC 1

These appeals related to the proceedings brought by the Financial Conduct Authority (the "FCA") under the Financial Markets Test Case Scheme pursuant to an agreement made with eight insurance companies to resolve issues of general importance on which immediately relevant and authoritative English law guidance was needed.

The court below (the "court") had considered 21 sample insurance policy wordings. The court accepted many of the FCA's arguments about the effect of these wordings but the FCA appealed on certain issues on which it did not succeed, as did the Hiscox Action Group (the "Hiscox Interveners"). Six insurance companies (the "Insurers") appealed against the decision of the court on other issues and also responded to the FCA's appeal.

Because of the importance and urgency of the issues raised, the appeals were "leapfrogged" to the Supreme Court, which addressed the following issues:

(i) the interpretation of "disease clauses" (which covered business

IN BRIEF

These appeals clarified whether a variety of insurance policy wordings covered business interruption losses resulting from the COVID-19 pandemic .

The UKSC substantially allowed the FCA's appeal and dismissed the Insurers' appeals

interruption losses resulting from any occurrence of a notifiable disease within a specified distance of insured premises);

(ii) the interpretation of "prevention of access" clauses (which covered business interruption losses resulting from public authority intervention preventing access to, or the use of, business premises) and "hybrid clauses" (which contain both disease and prevention of access elements);

(iii) the question of what causal link must be shown between business interruption losses and the occurrence of a notifiable disease (or other insured peril specified in the relevant policy wording);

(iv) the effect of "trends clauses" (which prescribed a standard method of quantifying business interruption losses by comparing the performance of a business to an earlier period of trading);

(v) the significance in quantifying business interruption losses of effects of the pandemic on the business which occurred before the cover was triggered ("Pre-Trigger Losses"); and

(vi) in relation to causation and the interpretation of trends clauses, the status of the decision of the Commercial Court in *Orient-Express Hotels Ltd (2010).*

Disease clauses

The Supreme Court considered the wording in an RSA policy ("RSA 3") as an exemplar. This clause (like many other disease clause wordings) covered business interruption losses resulting from any occurrence of a notifiable disease within a specified geographical radius (typically 25 miles) of the insured premises. The court had interpreted the clause as covering business interruption losses resulting from COVID-19 (which was made a notifiable disease on 5 March 2020) provided there had been an occurrence (meaning at least one case) of the disease within the geographical radius.

Although they ultimately reached a similar conclusion to the court about the scope of the cover (because of their analysis of causation – see below), Lord Hamblen and Lord Leggatt did not accept that this was the meaning of the words used. They accepted the Insurers' arguments that: (i) each case of illness sustained by a person as a result of COVID-19 was a separate "occurrence"; and (ii) the clause only covered business interruption losses resulting from cases of disease which occurred within the radius. Other disease clause wordings should be interpreted in a similar way. Lord Briggs and Lord Hodge would also have upheld the court's interpretation of the clause, but otherwise agreed with the main judgment.

Prevention of access and hybrid clauses

Prevention of access and hybrid clauses specified a series of requirements which must all be met before the insurer was liable to pay. Some clauses applied only where there were "restrictions imposed" by a public authority following an occurrence of a notifiable disease. The court held that this requirement was satisfied only by a measure expressed in mandatory terms which had the force of law. The Supreme Court rejected this interpretation as too narrow and held that an instruction given by a public authority might amount to a "restriction imposed" if it carried the imminent threat of legal compulsion or was in mandatory and clear terms and indicated that compliance was required without recourse to legal powers. The Supreme Court did not rule on whether individual measures satisfied this test but indicated that the argument was stronger in relation to some general measures, such as certain instructions in mandatory terms from the Prime Minister. The Hiscox wordings provided cover only where business interruption loss was caused by the policyholder's "inability to use" the insured premises. The court held that this meant complete

and not merely partial inability to use the premises. The Supreme Court agreed that inability rather than hindrance of use must be established but held that this requirement might be satisfied where a policyholder was unable to use the premises for a discrete business activity or was unable to use a discrete part of the premises for its business activities.

The Supreme Court interpreted wording requiring "prevention of access" to the premises in a similar manner.

Causation

In the way in which the majority of the Supreme Court interpreted the disease clauses (see above), a key question was whether business interruption losses consequent on public health measures taken in response to COVID-19 were, in law, caused by cases of the disease that occurred within the specified radius of the insured premises. The court found that the relevant measures were taken in response to information about all the cases of COVID-19 in the country as a whole; and the Supreme Court held, in agreement with the court, that all the individual cases of COVID-19 which had occurred by the date of any Government measure were equally effective "proximate" causes of that measure (and of the public response to it). It was therefore sufficient for a policyholder to show that at the time of any relevant Government measure there was at least one case of COVID-19 within the geographical area covered by the clause.

In reaching this conclusion, the Supreme Court rejected the Insurers' arguments: (i) that one event could not in law be a cause of another unless it could be said that the second event would not have occurred in the absence of ("but for") the first; and (ii) that cases of disease occurring inside and outside the specified radius should be viewed in aggregate, so that the overwhelmingly dominant cause of any Government measure would inevitably have been cases of COVID-19 occurring outside the geographical area covered by the clause.

The Supreme Court explained why the "but for" test of causation was sometimes inadequate and that there could be situations (of which the present case was one) where a series of events all caused a result although none of them was individually either necessary or sufficient to cause the result by itself.

The Supreme Court rejected the "weighing" approach as unworkable and unreasonable. In relation to the prevention of access and hybrid clauses, the Supreme Court held that business interruption losses were covered only if they resulted from all the elements of the risk covered by the clause operating in the required causal sequence. However, the fact that such losses were also caused by other (uninsured) effects of the COVID-19 pandemic did not exclude them from cover under such clauses.

Trends clauses

Almost all the policy wordings contained "trends clauses" which provided for business interruption losses to be calculated by adjusting the results of the business in the previous year to take account of trends or other circumstances affecting the business in order to estimate as nearly as possible what results would have been achieved if the insured peril had not occurred. The Supreme Court held that these clauses should not be construed so as to take away cover provided by the insuring clauses and that the trends and circumstances for which the clauses required adjustments to be made did not include circumstances arising out of the same underlying or originating cause as the insured peril (i.e., in the present case effects of the COVID-19 pandemic).

Pre-Trigger Losses

The court, subject to qualifications, permitted adjustments to be made under the trends clauses to reflect a measurable downturn in the turnover of a business due to COVID-19 before the insured peril was triggered. The Supreme Court rejected this approach. In accordance with its interpretation of the trends clauses, adjustments should only be made to reflect circumstances affecting the business which were unconnected with COVID-19.

Status of Orient-Express

The *Orient-Express* case concerned a claim for business interruption loss arising from hurricane damage to a hotel in New Orleans. The policy contained a trends clause with similar wording to those in the present case. A panel of three arbitrators accepted the insurer's argument that the cover did not extend to business interruption losses which would have been sustained anyway as a result of damage to the city of New Orleans even if the hotel itself had not been damaged. The Insurers had relied on this decision to support their arguments on causation of loss and the effect of the trends clauses in the present case. The Supreme Court concluded that the Orient-Express case was wrongly decided and should be overruled.