COVID claims: business as (un)usual

What now for COVID-19 business interruption claims? Celso De Azevedo discusses the Supreme Court's judgment & the issues likely to drive future litigation

IN BRIEF

- Disputed issues in the draft Declarations Order.
- Undecided issues and FCA guidance.

On 15 January 2021, the Supreme Court handed down its judgment on the Financial Conduct Authority (FCA) Test Case (*The Financial Conduct Authority & Ors v Arch Insurance UK Ltd & Ors* [2021] UKSC 1, [2021] All ER (D) 40 (Jan)) dealing with non-damage clauses which extended the typical coverage under business interruption insurance. According to the FCA, the Test Case will affect approximately 370,000 policyholders. In February, the Association of British Insurers estimated at £2bn the value of business interruption claims incurred in 2020 due to COVID-19.

The case included 21 representative policy 'types' issued by the eight insurers which became the defendants in the proceedings before the High Court. There were three types of policy wordings covering losses which were caused by:

- an outbreak of disease within a specified radius (eg, 25 miles or one mile) of the insured premises;
- a prevention of access to the insured premises, following a public authority action which was taken due to (depending on the clause) a(n) 'emergency' or 'danger' or 'incident' or 'injury' occurring 'in the vicinity' or within a specified radius of the insured premises;
- hybrid clauses which combined an outbreak of disease with a public authority prevention of access to the insured premises.

After the decision of the High Court, permission was obtained for a leapfrog appeal to the Supreme Court, which decided as follows:

- Disease clauses and hybrid clauses—there was coverage for business interruption losses so long as there was at least one case of COVID-19 (after 5 March 2020, when COVID-19 became notifiable in the UK) within the 25 miles radius.
- Causation—there would be coverage under the disease and hybrid clauses even if the occurrence of COVID-19 within the specified radius did not satisfy the 'but for' test of causation. The fact that the business interruption losses were also caused by other (uninsured) effects of the COVID-19 pandemic, eg the nationwide outbreak outside the specified radius, did not exclude cover. All the individual cases of COVID-19 which had occurred by the date of any government measure were equally efficient combined 'proximate' causes.
- 'restrictions imposed'—in relation to prevention of access and hybrid clauses, there was coverage for a 'restriction imposed' by a competent authority: (a) due to an occurrence of COVID-19; and (b) resulting in an 'inability to use' the insured premises, if there was an instruction—as understood by a reasonable person—by a competent public authority: (i) which carried an imminent threat of legal compulsion; or (ii) that meant compliance was required without recourse to legal powers. There was no requirement that the instructions were legally binding.
- 'inability to use'—in hybrid clauses, the requirement of the policyholder's 'inability to use' the insured premises was satisfied where there was a complete and not merely partial inability to use the premises. However, this requirement was also satisfied where the 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 same analysis was held to apply to prevention of access clauses.
- Trends clauses and pre-trigger losses—the type of 'trends' and 'circumstances' which required adjustments to be made in the calculation of indemnifiable losses should not include circumstances arising out of the same underlying or originating cause as the insured peril (eg, the broader nationwide customers' fears of the COVID-19 pandemic). As a result, adjustments should only be made to reflect circumstances affecting the business which were unconnected with COVID-19.

The FCA estimated that the Supreme Court's judgment affected approximately 700 policy wordings and about 60 insurers. While the Supreme Court's judgment represents a welcome clarification of many disputed issues, which were comprehensively decided in favour of policyholders, a number of areas remain unclear. These uncertainties are likely to require further judicial scrutiny in future.

Disputed issues

Some of the areas of uncertainty may be exemplified by the ongoing dispute arising in the draft Declarations Order which has been published in draft by the FCA in its Test Case webpage, together with the written submissions by the parties. As in the case of the Declarations Order issued by the High Court, the latest Declarations Order was intended to summarise the Supreme Court's decision in an easily understandable manner.

In view of the lack of agreement, a hearing before the Supreme Court may be necessary for the parties to present oral arguments in respect of the disputed terms, which are digested below.

Restrictions imposed

Most salient in the draft Declarations Order is the disputed issue of what kind of 'instructions' by competent authorities may amount to 'restrictions imposed' or 'closure or restriction placed' or 'enforced closure'. It is disputed whether there is coverage for restrictions where there were only broad instructions by the government directed at the general public and not at a specific category of businesses, eg that individuals must keep two metres apart (the two-metre rule).

Manifestation

The meaning of 'occurrence' or 'manifestation' of COVID-19 within a specified radius of the insured premises is disputed in instances where 'a person travelled through that geographical area and had no contact with anyone living in the area'. The Supreme Court held that an 'occurrence' or 'manifestation' of COVID-19 is proved wherever a person displayed symptoms of, or was diagnosed

with, COVID-19 within the specified radius. It is disputed whether this broad interpretation might encompass contactless travel through the geographical radius area.

Trends clause—counterfactual

Overruling the case of *Orient-Express Hotels Ltd v Assicurazioni Generali SpA* [2010] EWHC 1186, [2010] All ER (D) 282 (May) the Supreme Court held that in the calculation of the business interruption losses, the trends clause did not allow circumstances to be taken into account which arose out of the same underlying or originating cause as the insured peril. For instance, in disease and hybrid clauses, the reduction in trade due to customers' fears of the COVID-19 pandemic (rather than due to instructions to close businesses) should not be taken into account to reduce the quantification of the indemnity. This is a circumstance arising out of the same underlying cause, COVID-19, as the insured peril. However, it is disputed whether this interpretation in respect of the disease and hybrid clauses which were under appeal before the Supreme Court will also apply, more broadly, to any prevention of access clauses, such as those which were considered only by the High Court and were not subject to the appeal.

Undecided issues

In addition to those issues under dispute in the draft Declarations Order, there are other issues which remain unresolved despite the two court judgments in the FCA Test Case.

Causation

Non-damage extension clauses relating to an occurrence (eg, a notifiable disease or some other event) 'at the premises' were not part of the FCA Test Case. Nevertheless, it may be argued that the restrictive interpretation of coverage given by the High Court to 'in the vicinity' clauses could be expanded, by analogy, to 'at the premises' clauses since they evince a similar localised connotation.

The decision of the High Court is more restrictive than the reasoning of the Supreme Court as regards causation. The High Court held that in relation to any prevention of access clauses which require an 'emergency' or 'danger' or 'incident' or 'injury' that must occur 'in the vicinity' of the premises, the government action in imposing restrictions must be proved to have resulted solely from the local occurrence of disease. The action must not be partly due to the nationwide outbreak of the disease.

This is a very restrictive interpretation of the causation requirement since it would be very rare that any government action was not taken, at least in part, due to the nationwide outbreak.

By contrast, the Supreme Court adopted a much wider interpretation of causation in relation to the 25-mile radius requirement in the disease and hybrid clauses which were under appeal. The Supreme Court held that coverage in these clauses only required that there was at least one occurrence of disease within the specified radius, even if the government action (and the losses) was also due to the combined effect of the nationwide outbreak.

It is difficult to reconcile the decision of the High Court which held that 'in the vicinity' clauses provided only a localised cover, with the Supreme Court's broader approach to causation which held that each case of COVID-19 within the localised 25-mile radius was a proximate cause of the relevant government actions.

Aggregation

The Supreme Court went further than the High Court by holding that each occurrence of the notifiable disease was a separate but equally efficient proximate cause of loss. However, it is unclear whether this broad interpretation by the Supreme Court may apply to the issue of whether each occurrence of COVID-19 in several locations or during different time periods is, or not, a separate insured event for the purpose of applying deductibles and policy limits. These aggregation issues will have to be considered on a case-by-case basis in future litigation.

FCA guidance

The FCA's 'Final guidance: Business interruption insurance test case—proving the presence of coronavirus (COVID-19)' (the guidance) (*bit.ly/3cmdW3P*) came into effect on 3 March 2021 and will cease to have effect on 31 January 2022. The guidance provides that its content 'does not prevent policyholders using other sources of evidence or putting forward their own arguments regarding the sources of evidence'.

The guidance is designed for proving the presence of COVID-19 in business interruption insurance clauses that require:

- the presence of disease within a particular distance, zone or radius from the premises (eg, within a 25-mile or one-mile radius);
- the presence of disease within a vicinity or area where an event (eg, 'emergency' or 'danger' or 'incident' or 'injury') that occurs within such area would be reasonably expected to have an impact on the policyholder; and
- the occurrence of a notifiable disease without specifying a particular vicinity or area within which the disease needs to occur.

However, the guidance is not binding and may be challenged by insurers. Further, it is likely the tension between the restrictive interpretation of causation by the High Court as compared with the Supreme Court's broader interpretation has not been dealt with in the guidance because the FCA anticipates further litigation will be necessary. **NLJ**

Celso De Azevedo is an international re/insurance and commercial dispute resolution lawyer, 36 Commercial (*https://36group.co.uk/commercial*).