Business Interruption and Coronavirus

1. One of the many issues that is likely to arise out of the current Coronavirus pandemic is the extent to which an insured may be entitled to claim on its insurance policy in respect of the closure or disruption of its business.

2. Business interruption cover is provided upon the occurrence of a specific insured event. The wording of each policy will, therefore, be critical. Health warning.

3. Often, business interruption policies will provide an indemnity where financial losses are suffered by a business consequential upon material damage to property. Clearly, such policies will not provide an indemnity where businesses are affected solely by reason of the consequences of regulatory responses to the pandemic.

4. However, certain policies do provide cover independently of any material damage to property often by way of an extension to damage cover.

5. Until recently the leading case on business interruption cover was the decision of the Hong Kong Court of Final Appeal in ***New World Harbourview Co Ltd v ACE Insurance Ltd*** [1] which remains persuasive authority on the issues it decided.

6. The issue in that case concerned the construction of two "Composite Mercantile Policies" issued by the Respondents, ACE Insurance Limited.

7. The Appellants owned a number of convention centres, hotels, car parks and other businesses. They made a claim on their policies and subsequently commenced proceedings to recover an indemnity in respect of losses sustained from interruption to their business caused by Severe Acute Respiratory Syndrome ("SARS") in 2003.

8. Each of the policies contained a clause which provided that:

   "This Policy is extended to insure actual loss sustained by the Insured, resulting from a Reduction in Revenue and increase in Cost of Working as a result of… infectious or contagious disease, … occurring on the Premises of the Insured or of notifiable human infectious or contagious disease occurring within 25 miles of the Premises."

[1] [2012] HKCFA 21, [2012] 1 Lloyd's IR 537

9. Such clause thus provided cover against loss of revenue and increase in cost of working as a result of the occurrence of disease upon the occurrence of two separate events:

   9.1. infectious or contagious disease on the Insured's premises; and

   9.2. notifiable human infectious or contagious disease occurring within 25 miles of the Premises.

10. The claim was brought under the second such limb.

11. The two issues before the Final Court of Appeal were:

   11.1. *"Whether, in common form and widely issued policies of the type in question, the provision of insurance cover in respect of loss sustained 'as a result of notifiable human infectious or contagious disease' is limited to cover losses resulting from infectious diseases which are by statute compulsorily notifiable or whether such cover extends to losses caused by diseases subject to administrative reporting requirements although not backed by statutory sanctions."*

   11.2. *"What is the commencement date of coverage under clause 14.5 of the Insurance Policies in respect of any claim made as a result of SARS?"*

12. On the first issue, the Final Court of Appeal approached the issue of construction of the policy as it would any issue of contractual construction. On that basis, it held that "*notifiable human infectious or contagious disease*" meant an infectious or contagious disease that was required by law to be notified to an authority.

13. On the second issue, the Final Court of Appeal held that the commencement date of coverage was the date upon which the disease became notifiable as a matter of Government ordinance. It followed that losses suffered by the Appellants from SARS prior to that date were not covered. Prior to that date the insured event had not occurred and the cover was not retrospective.

14. That case remains persuasive authority and was referred to in the recent test case to which I shall now turn.

15. On 15th September 2020 Flaux LJ and Butcher J handed down judgment in ***Financial Conduct Authority v Arch Insurance (UK) Limited and others***[2].

[2] [2020] EWHC 2448 (Comm)

16. The case was brought by the FCA, as a test case, to determine issues of principle in relation to policy coverage under various specimen policy wordings underwritten by the defendants that potentially provided an indemnity for BI losses arising in the context of the Covid-19 pandemic and legislative and administrative responses thereto.

17. Numerous different policies within each category were considered and the only reliable basis on which to advise your clients is a careful consideration of the lengthy judgment, which runs to no fewer than 580 paragraphs. That said it is hopefully possible to identify some general principles which may at least provide some assistance.

18. The judgment addressed the following issues

    18.1. The history of the pandemic;

    18.2. The Government measures and categories of business;

    18.3. Policy coverage – by far the longest section;

    18.4. Causation; and

    18.5. Finally, proof of prevalence.

Key Events

19. The Judgment first set out the history of the Pandemic. Of particular importance is that:

    19.1. On 5.3.20 Covid was made a notifiable disease and SARS-CoV-2 was made a "causative agent" in England by amendment to the Health Protection (Notification) Regulations 2010.

    19.2. On 6.3.20 the same was applied to Wales by amendment to the Health Protection (Notification) (Wales) Regulations 2010.

    19.3. On 11.3.20 the WHO declared Covid-10 to be a pandemic.

    19.4. On 16.3.20 the UK Govt provided guidance on social distancing for vulnerable people.

19.5. On 21.3.20 the first Health Protection (Coronavirus, Business Closure) (England) Regulations and equivalent regulations for Wales were made.

19.6. On 23.3.20 the PM announced that the population must stay at home and the closure of all shops selling non-essential goods and other premises including libraries and outdoor gyms.

19.7. On 25.3.20 the Coronavirus Act 2020 was passed.

19.8. On 26.3.20 the Health Protection (Coronavirus Restrictions) (England) Regulations 2020 were made (largely replacing the regulations made on 21.3) and similar regulations were made for Wales. Those Regulations were amended on several occasions. I shall refer to them as the Regulations.

19.9. On 4.7.20 the Regulations were revoked prospectively and replaced with more limited restrictions in the Health Protection (Coronavirus Restrictions) (No 2) (England) Regulations 2020.

Categories of Business

20. Within the judgment, and based on the Regulations a categorisation of various types of business was adopted as follows:

20.1. Category 1: businesses listed in Part 1 of Schedule 2 to the Regulations such as pubs, bars, cafes and restaurants, which were affected by Regulation 4(1) of the Regulations.

20.2. Category 2: businesses listed in Part 2 of Schedule 2 to the Regulations such as cinemas, theatres nightclubs, indoor gyms, beauty salons and spas and car showrooms affected by Regulation 4(4) of the Regulations.

20.3. Category 3: businesses listed in Part 3 of Schedule 2 to the Regulations referred to as "essential shops" such as food retailers, off-licences, pharmacies, petrol stations and car repair services excluded from the scope of Regulation 5(1) of the Regulations.

20.4. Category 4: businesses offering goods for sale or hire in a shop or providing library services referred to as "non-essential shops", not listed in Part 3 of

Schedule 2 to the Regulations and affected by Regulation 5(1) of the Regulations.

20.5. Category 5: business not referred to in the Regulations at all, including professional service firms as well as construction and manufacturing undertakings.

20.6. Category 6: businesses providing holiday accommodation, affected by Regulation 5(3) of the Regulations; and

20.7. Category 7: places of worship, which were affected by Regulation 5(5) of the Regulations together with nurseries and schools.

General Principles of Construction

21. The Court then proceeded to address general principles of construction and in particular ejusdem generis and noscitur a sociis (known by its associates) and contra proferentem. It noted that the applicable background or matrix of fact against which all contracts, including insurance policies, are to be construed includes the relevant legal background, in particular existing case law and the fact that both case and statute law develop over time. It follows that the parties are taken to have agreed that their policy of insurance will be interpreted in the light of the general law from time to time so that where a relevant expression had been given a settled meaning by the Courts, that expression would be construed in the same manner in the future.

Coverage

22. In addressing issues of coverage, the Court identified 3 groups of policy depending on the nature of the insuring clause:

22.1. Disease clause policies: being non-damage "extensions" to the standard Business Interruption cover (which is contingent on the occurrence of physical or material damage to the insured premises);

22.2. Hybrid clause policies: that is those where the insured peril is defined by reference both to restrictions on the premises and to the occurrence or manifestation of a notifiable disease; and

22.3. Prevention of access and similar clause policies: that is those clauses that provide cover where there has been a prevention or hindrance of access to or use of the insured premises as a consequence of government or local authority action or restriction.

Disease Clauses

23. The Court proceeded to determine issues of cover by reference to specific policy wording of policies underwritten by Argenta, MS Amlin Underwriting ("MSA"), QBE UK Ltd ("QBE") and Royal Sun Alliance.

24. Typically, such policies provided cover where there was interruption or interference with business caused by or following the occurrence of a notifiable disease on or within a given radius of the business premises or the discovery of an organism likely to give rise to a notifiable disease.

25. In order to advise it is always necessary to focus on the policy wording of the relevant policy. However, in terms of general principle, the Court held broadly as follows.

26. First, there is an **occurrence** of Covid 19 within a radius where at last one person is infected with the disease within that radius: it is not necessary that that person should have been diagnosed. The same is true if the wording refers to the **existence** of "*any notifiable disease within*" the applicable radius.

27. Second, where cover depends on the "**manifestation**" of a Notifiable Disease, the insured has to prove the presence of a person displaying symptoms or who, while being asymptomatic, has been diagnosed with the disease. However, the presence of someone who is asymptomatic and has not been diagnosed will not suffice.

28. Third, the word "**following**" imported some causal not mere temporal connection but not necessarily proximate causation.

29. Fourth, the word "***vicinity***", for the purposes of an insured event defined as "*business interruption or interference*" to the insured's business as a result of a notifiable disease occurring within the Vicinity of an Insured Location during the period of insurance, is wide enough to cover the entirety of England and Wales. Moreover, even if "vicinity"

is more narrowly defined, the cover is not limited to the BI consequential upon the Covid within that vicinity. I shall return to that in a minute.

30. Fifth, the **insured peril** was identified to be the composite peril of interruption or interference with the Business during the indemnity period "following", "as a result of/resulting from" or "in consequence of" one of the defined occurrences. Not just the occurrence within the vicinity.

31. Sixth, where cover is provided following any "**occurrence**" of a Notifiable Disease within a given radius, **cover** is not confined to the local effects of that occurrence but to the effects both within and outside the defined radius. Therefore, if for example, there were a single occurrence within the given radius, but the business suffered loss by reason of a general lockdown, the business is entitled to an indemnity against the consequences of the lockdown or the public response to the disease. The position is otherwise where the occurrence of the disease within the policy area is stated in the policy to be itself an "event". In such a case the cover is only for BI caused by the occurrence of the disease within the policy area.

32. Finally, in calculating the indemnity reference should be made to the contractual quantification machinery, even where that is primarily applicable to damage based perils i.e. loss caused by damage. That machinery should be taken to apply to the quantification of indemnities for business interruption with such modifications as may be required.

33. Therefore, a trends clause, couched in language designed to apply to a damage peril ought to apply. However, in construing any trends clause one has to exclude from the relevant counterfactual any part of the insured peril – that is the loss due to the occurrence of Covid both inside and outside of any given radius – within the indemnity period beginning with the first relevant occurrence of Covid. Such a clause might have to be read as if it provided along the following lines:

"… adjustments shall be made as may be necessary to provide for the trend of the Business and for variations in or other circumstances affecting the Business either before or after the occurrence of the insured peril or which would have affected the Business had the insured peril not occurred so that the figures thus adjusted shall represent as nearly as may be reasonably practicable the results which but for the

insured peril would have been obtained during the relative period after the occurrence of the insured peril."

34. The same is true of the application of the definition of "Standard Turnover". In calculating standard turnover, one removes the effects of Covid both inside and outside the relevant location.

Hybrid Policies

35. These policies define the insured event as BI caused by an inability to use premises due to restrictions following an outbreak of a notifiable disease. The Court proceeded to determine issues of cover by reference to specific policy wording of policies underwritten by Hiscox and Royal Sun Alliance.

36. I shall adopt the same approach and try to identify some issues of general application.

37. First, "***restrictions imposed***" mean something that is mandatory not advisory: i.e. the restriction must have the force of law. They must be imposed by a public authority even if that is not expressly stated in the policy wording. The restrictions are therefore those promulgated by SI and in particular the Regulations. Guidance and exhortation even by the PM do not suffice.

38. Second, "***unable to use***" means something more than "***hindered in using***". An insured might not be unable to use premises even though he cannot use all of them. However, the partial use might be so nugatory as to amount to an "*inability to use the premises*". Moreover, while the restrictions need not be directed specifically at the insured's premises, the restriction on persons leaving their home save with reasonable excuse, imposed by Regulation 6 of the Regulations will not, save in rare cases, suffice.

39. Third, "***an occurrence***" of a disease would include a pandemic. It is not confined to a localised outbreak. Thus, the occurrence of Covid 19 in the UK suffices for there to be an occurrence of a notifiable disease. Therefore, national restrictions imposed because of that outbreak "***followed***" the occurrence.

40. Fourth, policies that require **"*interruption***" rather than "*interruption or interference*" do not require complete cessation of business.

41. Fifth, "***enforced closure***" of premises occurs if all or part of those premises are closed under legal compulsion: i.e. closure which is or could be enforced legally. Where such "*enforced closure*" has to be for "*health reasons or concerns*" in or within a distance of the Vicinity the same wide meaning will be applied to Vicinity as for the disease policies but even if a narrower meaning were given to it, the health reasons or concerns would apply to all vicinities.

42. Sixth, the restrictions need not be due to the occurrence or manifestation of the disease within the defined geographical area. Provided there is the necessary occurrence/manifestation cover is provided where restrictions are imposed by reason of the widespread outbreak of the disease.

43. Seventh, as with the disease policies, the trends and counterfactual clauses, which apply in respect of quantification, do apply with such modifications as may be required even though they may not refer to "*restrictions*". Thus, the following wording would be added to the trends clauses:

> *"or if you had not been unable to use the insured premises due to restrictions imposed by a public authority following an occurrence of any human infectious or human contagious disease, an outbreak of which must be notified to the local authority*."

44. Finally, in applying the counterfactual, regard has to be had to the composite nature of the insured peril which typically includes 3 elements:

    44.1. Inability to use the insured premises;

    44.2. Due to restrictions imposed by a public authority;

    44.3. Following an occurrence/manifestation of the defined disease.

45. Therefore, all 3 elements have to be removed in constructing the applicable counterfactual.

Prevention of Access and similar wording

46. These policies identify the insured peril to be prevention or hinderance of access to or use of premises caused by government or local authority action or restriction. The Court proceeded to determine issues of cover by reference to specific policy wording of policies underwritten by Arch Insurance (UK) Ltd, Ecclesiastical Insurance Office plc, Hiscox, MSA, RSA and Zurich.

47. While the policies in this section had quite different provisions, I shall again attempt to identify some decisions of general principle.

48. First, "***prevention***" is not the same as "***hinderance***", which only requires proof of access being rendered particularly difficult. Where the insured peril includes "***prevention of access to the premises due to the actions or advice***" of a public authority, the insured must prove actual closure of the premises for the purpose of carrying on the business, which was being undertaken prior to public action or advice, consequential upon that public action or advice. It does not, however, require it to become legally or physically impossible to access premises. Thus, a publican may be entitled to visit his pub for maintenance but access to his business would be "prevented" if the pub had to close for business.

49. A contrast is to be drawn between the pub or restaurant, which falls within Category 1, which had a takeaway service prior to and one which opened such a service following lockdown. In the latter case, there is a fundamental change in the business sufficient to attract cover, as there is with a theatre or cinema, which falls within Category 2, that started remote performances during lockdown. In the former there is not. Likewise, Regulation 6 of the 26 March Regulations does not prevent access.

50. Category 3 essential shops can still trade even though customers were required only to purchase essentials. Category 4, non-essential shops were required to close by Regulation 5 of the Regulations. Therefore, access to them was prevented. Access to businesses not listed in the Regulations – that is Category 5 businesses e.g. professional firms, construction undertakings and manufacturers - was not prevented.

51. Second, where the insured peril requires the occurrence of an "***incident***", the insured has to prove the occurrence of an "event": that is something that happens at a particular time, at a particular place, in a particular way. That is particularly the case if the incident

has to occur within a specified distance of the insured premises. A pandemic, and therefore, Covid, is not an incident.

52. Third, as with the hybrid policies, where the peril is defined so that the "***restriction on access***" is "***imposed***" or "***ordered***" there must be a mandatory restriction. Where the action has to be by a "***competent local, civil or military authority***" that extends to central government action. The meaning of "***Action***" is clause specific. It may extend to "***advice***", where the action in question is only required to hinder access and use, but may not where the action is required to prevent access because advice does not have the force of law.

53. Fourth, also as per the hybrid policies, "***interruption***" in the insuring clause is generally to be construed so as to extend to disruption to or interference with that business. It is not confined to cessation. Thus, cover is provided to those businesses to which access is only permitted for a limited purpose: for example, the Category 1 pub or restaurant only permitted to sell food/drink for consumption away from the premises. It was not hindered in respect of Category 3 essential shops or Category 5 businesses not referred to in the Regulations. Regulation 6 does not hinder access but it may hinder use.

54. Fifth, where action has to be "***following a danger, disturbance or emergency in the vicinity of the premises***" that connotes a narrow, localised form of cover: e.g. a bomb scare or gas leak causing a localised evacuation – not a pandemic such as Covid justifying the imposition of national restrictions. "***Vicinity***" in this context connotes the area surrounding the premises unlike its meaning in the case of the disease policies. Localised measures might suffice, however, for cover. The position is to be contrasted with that which applies where it is the actions that have to be in the vicinity, where nationally applicable measures would suffice.

55. Sixth, in construing the trends provisions, the comparison required for the assessment or adjustment of the BI loss is between performance of the business as a consequence of the insured peril e.g. prevention of access to the premises due to the actions or advice of the government due to the emergency and what the performance of the business would have been but for that emergency and consequential government action/advice. However, any loss suffered before the government actions/advice due to the socio-economic consequences of the pandemic cannot be recovered.

Causation

56. The Court had already addressed causation to some extent when considering policy coverage and in particular the proper construction of trends clauses.

57. However, the judgment briefly addressed the issue again. The key question is what is the proximate cause of the loss? The answer is the insured peril. Therefore, in determining what BI has been caused, the counterfactual has to posit the business without the entirety of the insured peril occurring.

58. Thus, in the case of prevention of access policies, typically there would be 3 interconnected elements in the insured peril:

58.1. Prevention or hinderance of access to or use of premises;

58.2. By action or advice of government;

58.3. Due to an emergency which could endanger human life

So that the insured has to prove BI caused by that composite peril in order to obtain an indemnity.

59. The counterfactual, therefore, requires stripping out all of the three elements – not just prevention or hinderance - and asking what would have happened if none of those elements had occurred.

60. The same applies with hybrid policies save that the insured peril typically comprises the following 3 elements:

60.1. Inability to use the insured premises;

60.2. Due to restrictions imposed by a public authority;

60.3. Following the occurrence of an infectious or contagious disease.

61. The disease policies insure against the effects of Covid both inside and outside the relevant area and therefore the effects of the disease both inside and outside the area have to be stripped out in the relevant counterfactual. The proximate cause of the BI is the notifiable disease of which the individual outbreaks form indivisible parts. An

alternative though less satisfactory analysis is that each individual occurrence is an effective cause so that they were all effective because of the consequential national response. The effect is the same. In either event the national response has to be stripped out.

Prevalence

62. The Court considered the issue of the forms of evidence that might in principle satisfy the burden of proof on an insured to establish prevalence in a specific area. It was common ground that specific evidence, NHS Deaths Data, ONS Deaths Data and reported cases are in principle capable of demonstrating the presence of Covid. Other reliable statistical evidence also could be used.

Conclusion

63. Declarations and orders arising out of the judgment were made on 2nd October.

64. Following the judgment, the FCA has written to CEOs of BI policy insurers setting out its expectations. One point of note is that the FCA stated as follows:

> *"We also noted that the treatment of any forms of Government support as income for tax purposes may well differ from how the support should be assessed under a BI policy. Tax considerations typically do not form any part of the calculation of losses for business interruption policies. We therefore do not consider the Government's treatment of the Small Business, Retail, Hospitality and Leisure or Local Authority Discretionary grants for tax purposes is a proper basis for insurers treating those payments as turnover under the policies. Nor do we see that insurers can apply these amounts as savings against fixed business expenses. This is because the amounts received are not attributable to any particular business expense and policyholders will have used the grants in any number of ways."*

65. As the FCA recognises the judgment has brought a degree of clarity as to the proper treatment of BI claims but it remains to be seen whether any and if so which parts of the judgment will be the subject of an appeal.

66. In terms of appeals, it is understood that the Court has granted leapfrog certificates enabling the FCA and a number of insurers - Arch, Argenta, Hiscox, MSA, QBE UK and RSA - to apply directly to Supreme Court for permission to appeal.

67. Regular updates can be found on the FCA's website https://www.fca.org.uk/firms/business-interruption-insurance

68. In terms of the winners and losers, the insurers lost on many of the coverage and causation issues. However, the application of the trends clauses was a victory for them which might explain why the share price of some of the insurers rose following the judgment.

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