UK Supreme Court Concludes FCA Business Interruption Hearing

23 November 2020

The UK Supreme Court concluded hearing appeals over the United Kingdom's Financial Conduct Authority's (the "FCA") business interruption insurance test case on 19 November 2020, which the FCA described in its written statements to the Supreme Court as "probably the most important insurance decision of the last decade". This follows the judgment of the High Court handed down on 15 September 2020 (see here). The insurers appealing to the Supreme Court on the test case included: Hiscox, QBE, Arch, Argenta Syndicate Management, MS Amlin and RSA. The six insurers and the FCA were granted "leapfrog certificates" to appeal to the Supreme Court, and therefore bypassed the Court of Appeal, after the High Court judgment. Following the High Court's judgment, Ecclesiastical and Zurich (two of the original defendant insurers) decided not to pursue an appeal to the Supreme Court. This Update considers the key issues under consideration before the Supreme Court.

FCA Grounds of Appeal. The High Court judgment handed down in September found coverage was available under many, but not all, of the 21 non-damage business interruption policy wordings considered by the court. The FCA highlighted four grounds of appeal before the Supreme Court, which it identifies as providing "substantial obstacles to indemnity for a large number of insureds":

- Whether in adjusting a claim under the prevention of access/hybrid wordings,[1] an insurer can in principle reduce the indemnity payable where one element of a composite insured peril has caused a reduction in revenue prior to the policy being triggered by the occurrence of other elements of the composite peril. The FCA asked the Supreme Court to approve of the approach taken by the High Court to the *Orient Express* case.

[1] Hybrid wordings being those clauses that refer to both restrictions on access to insured premises and the occurrence or manifestation of a notifiable disease.

- Whether policies requiring the "actions" of a public authority[2] are triggered by instructions or advice of the government falling short of legislation and not having the force of law.[3]

- The FCA argued that partial closure of a business or premises (rather than total closure) should be sufficient for the purposes of wordings requiring "prevention of access" or "inability to use".[4]

- The High Court reached a different conclusion in two of the QBE policies in comparison with the other disease clauses put before the Court.[5] The FCA asked the Supreme Court to reverse the High Court's judgment in this respect and to find that loss would be covered under these clauses where Covid-19 is "manifested" within the policy radius (i.e., 25 miles).

The Insurers' Key Issue – Causation. Given the number of insurers and policies, it is unsurprising that a variety of nuanced and policy-specific grounds of appeal have been presented to the court. For the purposes of this Update, we have focused on the key themes that permeate this test case, which fundamentally relate to the issue of causation, which impacts, amongst others, the determination of coverage and the trends clauses included in certain of the policies. On the issue of causation, the insurers raised the following grounds of appeal across their submissions, which are generally applicable to the policies:

- What constitutes the scope of the insured peril;

- The interpretation of trends clauses;

- The relevance of and use of the Orient Express case;

- The issue of proximate causation;

- The "indivisible cause";

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2 Or that restrictions have been "imposed" or closure "enforced".

3 Hiscox did note in its written submissions that the Health Protection (Coronavirus, Restrictions) (England) Regulations 2020, which prevented people from leaving their homes without reasonable excuse, was not directed at premises and that a restriction under the policies would need to be directed towards the insured and its use of the premises.

4 Hiscox, for example, has argued that on its plain meaning the term "interruption" means to stop or break (when compared with the word "interference").

5 QBE2 and QBE3.

- The interpretation that each of the cases of Covid-19 around the UK constituted separate concurrent proximate causes of the national restrictions; and

- The correct counterfactual for the purposes of the trends clause and "but for" test.

In addition to these, certain grounds of appeal relating to the interpretation of the individual policies were raised.

The High Court found in its judgment that the pandemic and the UK government's response to it could be considered a single cause of losses. This resulted in establishing coverage for a significant number, though not all, of the policies in this test case.

The insurers have argued that a policyholder is only entitled to recover those business interruption losses that are the product of the correct causal sequence. Although this is largely dependent on the individual policy wordings, the general principle enumerated is that the loss must follow on from the specific insured peril. The insurers challenged the High Court's reference of a "part of an indivisible cause", arguing that an event either is or is not a proximate cause of another. Indeed, counsel for the insurers reminded the Court that business interruption is not part of the insured peril; it is the damage for which an indemnity is given if it is caused (in law) by an insured peril. The insurers went on to argue that, taking the example of the occurrence of Covid-19 within a certain geographical limit, it would be impermissible for the Court to aggregate individual cases of Covid-19 across the country (one of which is within the relevant area) in order to contend that cover for the consequences of the pandemic within the set radius has been triggered.

The use of words such as "following" in the policies has been interpreted by the insurers as importing a requirement to apply the "but for" test. This test operates such that cover is not provided where the loss would have been suffered in any event, even if it was proven that the relevant insured peril occurred. The FCA, unsurprisingly, did not concur with this analysis and argued that competing causes that fell within the ambit of the insured peril cannot be separated out.

The insurers also went on to challenge the findings of the High Court that, where premises have closed as a result of the government's action or advice in response to the pandemic, the loss should be adjusted on the assumption that there was no pandemic and no action or advice. The insurers argued that in doing so, the insured would be able to recover losses that they would have suffered in the absence of the specific causal sequence (i.e., that were not insured perils).

The Supreme Court has also been asked to consider the High Court's conclusions of a key case from 2010 - the *Orient Express* case. Two of the judges hearing the appeal - Lord

Hamblen and Lord Leggatt - were involved in making the original decision. The insurers have generally noted that the legal analysis from the High Court, distinguishing the test case from *Orient Express*, was flawed, and that the principles from the original judgment should be applied. The effect of this is that only the relevant insured peril (for example, the local manifestation of Covid-19) should be stripped out when considering the correct counterfactual for the purposes of "trends" clauses. The FCA continued to reject this analysis.

Counsel for the insurers have continued to argue that the effect of the High Court's judgment is to effectively rewrite insurance clauses - in one case, it was argued that under the interpretation accepted by the High Court, Covid-19 cases could be "harvested by some magical process" to be linked to a business closure, when the losses were actually "attributable to the Government lockdown". As such, there was no causal connection between cases of Covid-19 occurring and businesses closing. In contrast, the FCA accused insurers of "trying to escape from the consequences of the policies they have written" and stated that instead insurers should have been prepared for a large-scale public authority response when writing business interruption coverage for diseases.

This test case has progressed from the FCA's initial announcement in May 2020 to the Supreme Court, with what has been described as "astonishing" speed, as part of an attempt by the industry and the regulator to find clarity for all parties. A final ruling from the Supreme Court may have a considerable influence on the scale of business interruption-related losses in the United Kingdom. As such, the financial stakes are high for insurers and policyholders alike. The Supreme Court concluded the hearings by noting that while they have taken steps to ensure that the judges have more time to devote to writing the judgment as quickly as can be managed (given the practical importance of the test case), they were unable to say whether the judgment will be handed down before Christmas.

However, the impact of this test case has implications beyond the judgment and the financial fallout for the defendant insurers and/or policyholders. The Chairman of the Lloyd's of London insurance market, Bruce Carnegie-Brown, has said that the pandemic fallout "is a bit of a wake-up call for the industry in terms of the wordings in its claims" and called for greater simplification and clarity in policy wordings. We have already seen some UK insurers rewriting their policies to clarify the coverage that the policies are providing and expect to see greater attention paid to this going forward.

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