Business Interruption Insurance – FCA Test Cases for Covid 19 losses

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Introduction

In our article published on 3 June 2020, we reported and commented on the FCA’s proposal for test court cases on the availability of business interruption insurance for Covid 19 losses mainly for the benefit of SMEs. The aim of the test cases is to save time and legal costs and provide some level of consistency in claims handling between different insurers and policy wordings.

Process

The FCA selected 21 “lead” policies underwritten by eight insurers that it believed captured the majority of the key issues that could be in dispute between policyholders and their insurers\(^1\). These policies provided stand-alone business interruption cover.

The hearing of the test cases took place in late July 2020 before two judges who formerly practiced in the field of insurance, namely Lord Justice Flaux (now a court of appeal judge) and Mr Justice Butcher (now a judge in the commercial court). Policyholders’ interests were represented by leading counsel instructed by the Financial Conduct Authority. Insurers instructed their own leading counsel.

Judgment

Judgment was handed down on 15 September 2020. The judgment is declaratory in the sense that it determines the availability of cover only for the policies in the test cases based on the court’s interpretation of the wording of each policy. It does not determine the availability of cover under any other policies (unless written on the same terms). Nor does it determine whether there is in fact cover for individual policyholders which will depend on the actual facts of each case.

The relevant provisions of the lead policies essentially fell into three categories: (i) what the FCA termed “disease clauses”; (ii) what were referred to as “hybrid clauses”; and (iii) clauses covering prevention of access to insured premises and similar perils. The court dealt with the three categories in turn and considered the terms of each policy separately (noting that questions of policy coverage cannot be determined in the abstract).

Overall, policyholders were probably the winners but, as in all matters of insurance, the devil will be in the detail of the individual policies (unless they formed part of, or are on the same terms as, the test cases) and the actual facts of each case.

The judgment mainly focused on disease clauses and prevention of access and other similar clauses:

Disease clauses

Generally speaking, these policies provide cover in respect of business interruption in consequence of or following or arising from the occurrence of a notifiable disease within a specified radius of the insured premises (often 25 miles). Interestingly, and by way of example, a 25-mile radius was said to be an area of about 2,000 square miles or an area the size of Oxfordshire, Berkshire and Buckinghamshire combined.

The court considered that what was being insured was business interruption arising from a notifiable

\(^1\) The policies are underwritten by Amlin, Arch, Argenta, Ecclesiastical, Hiscox, QBE, RSA and Zurich
disease of which there was an occurrence within the relevant policy area and that there would have been an "occurrence" of COVID-19 within a relevant policy area when at least one person who was infected with Covid 19 (diagnosable rather than diagnosed) was in the relevant area.

One policy required an occurrence of disease within the “vicinity” of an insured location. The court held that vicinity in relation to a disease such as Covid 19 should be widely construed to mean an extensive area, possibly embracing the whole country.

On the other hand, some policies may have disease clauses that indicate that business interruption cover is intended to be confined to the results of specific (relatively) local cases, in particular where the policy refers to “incidents” within a relevant area or particular “events” i.e. matters occurring at a particular time, in a particular place and in a particular way. In these cases, the local incident or event must have caused the business interruption or interference.

**Prevention of Access clauses and similar wordings**

Generally speaking, these policies provide cover where there has been a prevention of access to or use of the premises as a consequence of government or local authority restriction.

The court held that where the effect of the actions of government was that businesses had to completely close or cease business, there was a prevention of access. Thus, in relation to the government’s 21 or 26 March 2020 Regulations (for example that nightclubs, theatres, cinemas, gyms and leisure centres should close), there was prevention of access.

Only total closure will amount to prevention of access. If a new business was commenced (for example take-away) there would still have been a prevention of access as the business specified in the policy wording could no longer be carried on from the premises.

However, a mere hindrance or impediment in the use of premises or reduced footfall resulting from Covid 19 would not amount to a prevention of access and would not be covered (unless the policy extended cover to hindrance in access). Thus, professionals working from home rather than the office would not have resulted from any Government order to close and were thus permitted to remain open even if they were not used by staff or visited by clients.

The same considerations would apply to closure of premises on Government “advice” (given on 20 or 23 March 2020) if “advice” is covered by the policy.

Where the policy wording refers to an “incident” (which the court considered was synonymous with an “event”) and imposes a geographical restriction that the incident occurs “within a one mile radius of the insured premises” or “within the vicinity of the insured premises” the court was of the view that the clause was intended to cover local incidents, citing the paradigm examples of a bomb scare or a gas leak or a traffic accident.

On the other hand, where the policy provides cover in cases where there is Government action “in the vicinity" of the insured location, actions of the Government taken nationally and affecting all insured businesses will inevitably be in the vicinity of the insured premises if they lead to prevention of access to insured locations.
Next Steps

Policyholders will be anxious to know whether their business interruption policies will respond to claims following the court’s judgment on the test cases.

According to the FCA’s finalized guidance to insurers given in June 2020, insurers should by 8 July 2020 have completed a review of their policy wordings and identified clauses which might be affected by the outcome of the test cases. They should now handle and assess all outstanding potentially affected claims in line with their regulatory duties, applying the judgment in the test cases so far as relevant. Having brought the test cases, we expect the FCA to closely monitor the timely handling of claims and the correct and fair application of the guidance given by the judgment.

Of course, many important issues remain to be resolved. For example, depending on the wording of the policy, policyholders may be required to prove the prevalence of the Covid 19 disease in a particular area at a given time. The amount of recoverable loss on a valid claim is also likely to be an area of contention.

Furthermore, due to the amounts involved and the public interest in the issue, the court’s judgment may be appealed with the permission of the court at first instance or the Court of Appeal in the normal way.