COVID-19 Business Interruption Insurance claims – Has the UKSC gone off-road to meet the High Court in town?

Financial Conduct Authority (Appellant) *v* Arch Insurance (UK) Ltd and others [2021] UKSC 1

The judgment delivered by the UKSC on 15/1/21 in the above case is very interesting and is considered by many as a landmark decision on insurance law but more so on causation.

The case concerned the examination of the scope of cover of various business interruption policies issued by eight insurance companies in UK who are considered to be leading providers of business interruption insurance, following the rejection of thousands of claims by policy holders for indemnity against losses caused by the interruption of their businesses due to COVID-19 measures and restrictions published and/or issued in the UK for the handling of the pandemic crisis.

The action was originally brought to the High Court by the Financial Conduct Authority under the Financial Markets Test Case Scheme for the benefit of the policy holders and was decided, on most of the issues which have been raised, in favour of the FCA. Both the insurers as well as the FCA appealed against the decision on various grounds. Groups of persons who were obviously considered as having a locus standi had also intervened in the proceedings and submitted their arguments.

The FCA also challenged the decision of the court below, *inter alia*, that only the restrictions which had the force of law could trigger the cover and the conclusion that the trends clauses should be interpreted so as to include the effects of the insured peril in calculating the losses incurred by the policy holders.

The various standard type insurance clauses were separated into four different categories. These were:

i) "Disease clauses" (clauses which, in general, provide cover for business interruption losses resulting from the occurrence of a notifiable disease, such as COVID-19, at or within a specified distance of the business premises);

ii) "Prevention of access clauses" (clauses which in general, provide cover for business interruption losses resulting from public authority intervention preventing or hindering access to, or use of, the business premises);

iii) "Hybrid clauses" (clauses which combine the main elements of the disease and prevention of access clauses);

iv) "Trends clauses" (clauses which in general, provide for business interruption loss to be quantified by reference to what the performance of the business would have been had the insured peril not occurred).

The UKSC dealt, *inter alia*, with questions of construction of the insurance policies and causation.

It was also necessary to consider whether the consequences of particular measures which could not be said to have the force of law should have any different bearing on the triggering of the cover. On this issue, the UKSC disagreed with the court below that only measures which had the force of law would suffice. The UKSC held that the test in interpreting the words used is *how they would be understood by a reasonable person*. A reasonable policyholder would understand the word "imposed", without more, as making cover conditional on the existence *or immediate prospect* of a valid legal basis for the restriction. It was held that a mandatory instruction given by a public authority in the anticipation that legally binding measures would follow shortly afterwards, or would do so if compliance was not obtained was capable of being a *"restriction imposed"* (within the meaning of the wording of particular insurance policies) regardless of whether it was legally capable of being enforced. However, the UKSC sustained the view of the court below that enforced closure of an insured location would not include advice or exhortations, or social distancing and stay at home instructions (as, for example, the Prime Minister's statement of 16 March 2020 which did not, in the opinion of the UKSC, cause prevention of access to the relevant insured business premises).

Reiterating that the core principle is that an insurance policy [like any other contract] must be interpreted objectively by asking what *a reasonable person*, with all the background knowledge which would reasonably have been *available to the parties when they entered into the contract*, would have understood the language of the contract to mean, the UKSC applied the rules of interpretation to each different type of clauses.

Disease Clauses

The extension of cover for business interruption of the RSA[i] 3 policy (disease type of clause) provided the following:

"We shall indemnify you in respect of interruption or interference with the Business during the Indemnity Period following, inter alia any occurrence of a Notifiable Disease at the Premises and occurrence of a Notifiable Disease within a radius of 25 miles of the Premises".

The same Policy defined "Notifiable Disease" as *illness sustained by any person resulting from any human infectious or human contagious disease an outbreak of which the competent local authority has stipulated shall be notified to them.*

It was agreed that by 6 March 2020, COVID-19 had been designated as a notifiable disease in all parts of the UK within the meaning of the above definition.

The UKSC sought to define what is meant by the phrase *"any … occurrence of a Notifiable Disease within a radius of 25 miles of the Premises"* and what *causal link* was required in order to entitle a policyholder to be indemnified under the clause.

The court below had previously decided that it would not make sense for the cover to be confined to the effects only of the local occurrence of a Notifiable Disease. That would mean that there would be no effective cover if the local occurrence were a part of a wider outbreak and where, precisely because of the wider outbreak, it would be difficult or impossible to show that the local occurrence made a difference to the reaction of the authorities and/or the public. In the opinion of the court below, the parties must have contemplated that the authorities would be likely to take action in response of an outbreak of a notifiable disease as a whole and not to particular parts of an outbreak and it would therefore be irrelevant to any action whether cases fell within or outside a line 25 miles away from the insured premises.

Citing **Charter Reinsurance Co Ltd v Fagan [1997] AC 313** with approval, the UKSC said that it is not legitimate for a court to force upon the words of a clause a meaning which they cannot fairly bear. To do that, is to substitute for the bargain actually made with one which the court believes could better have been made.

It was held instead, that it is only an *occurrence within* the specified area that is an *insured peril* and not anything that occurs outside that area. The word occurrence like its synonym "event", has a widely recognised meaning in insurance law which accords with its ordinary meaning as "something which happens *at a particular time*, *at a particular place*, *in* a *particular way*". Each case of illness sustained therefore, should be regarded as a separate *occurrence*.

The clause was properly interpreted, as a matter of plain language, as providing cover for business interruption caused by any cases of illness resulting from COVID-19 that occur *within* a radius of 25 miles of the premises from which the business is carried on and did not cover interruption caused by cases of illness resulting from COVID-19 that occur *outside* that area and these cases should not be part of the insured peril. In the opinion of the UKSC, this interpretation was supported by the definition of "indemnity period" in the policy.

On the above basis, the reasoning of the court below was not approved (interestingly however, the UKSC arrived at the same result due to its analysis on causation, see below).

The insurers also contended, that under the policy wording the disease clause does not provide any cover at all for business interruption resulting from COVID-19 because any loss caused by an occurrence of a notifiable disease is excluded from cover if the disease amounts to an "*epidemic"* on the basis of an

exclusion clause. The exclusion clause provided that *the insurance by this Policy does not cover any loss or Damage due to contamination pollution soot deposition impairment with dust chemical precipitation adulteration poisoning impurity epidemic and disease or due to any limitation or prevention of the use of objects because of hazards to health.*

In rejecting the above argument, the UKSC held that in the case of an insurance policy of this kind which is sold to small/medium enterprises, the person to whom the document should be taken to be addressed is not a pedantic lawyer who will subject the entire policy wording to a minute textual analysis. It is an ordinary policyholder who, on entering into the contract, is taken to have read through the policy conscientiously in order to understand what cover they were getting. In par. 78 of the judgment the court expressed the following opinion:

"78. The notion that such a policyholder who is presumed to have reached p 93 of the RSA 3 policy wording would understand the general exclusion of contamination or pollution and kindred risks on that page to be removing a substantial part of the cover for business interruption loss that was ostensibly conferred on p 38 is as unreasonable as it is unrealistic. The reasonable reader would naturally assume that, if the intention had been to put a further substantive limit on the risk of business interruption specifically insured by the extension for infectious diseases in addition to the geographical and temporal limits stated in the extension itself, this would have been done transparently as part of the wording of the extension and not buried away in the middle of a general exclusion of contamination and pollution risks at the back of the policy. The reference in the exclusion to "disease" would reinforce the understanding that the general exclusion could not have been intended to apply to the cover for business interruption caused by an infectious disease, as it would obliterate that cover."

The QBE[ii] 1 relevant (disease type) clause covered *any human infectious or human contagious disease (excluding Acquired Immune Deficiency Syndrome (AIDS) or an AIDS related condition) an outbreak of which the local authority has stipulated shall be notified to them manifested[iii] by any person whilst in the premises or within a twenty-five (25) mile radius of it*.

The QBE2 and QBE 3 clauses were interpreted in line with the RSA 3 interpretation.

The prevention of access and hybrid clauses

The hybrid clauses have been so called because one element of the peril insured against by these clauses is the occurrence of a notifiable disease. Unlike the disease clauses, however, this element is combined with other elements which narrow the consequences of disease covered by this type of clause.

Hiscox[iv] 1-4 clauses provided that:

"We will insure you for your financial losses and other items specified in the schedule, resulting solely and directly from an interruption to your activities caused by (inter alia) your inability to use the insured

premises due to restrictions imposed by a public authority during the period of insurance following … an occurrence of any human infectious or human contagious disease, an outbreak of which must be notified to the local authority".

Hiscox argued that despite the absence of any radius provision or other words which require the occurrence of disease to be within a specified distance of the insured premises, the word "occurrence" in this wording means something limited, small-scale, local and specific to the policyholder or its business or premises and thus does not apply to the COVID-19 pandemic. This argument was rejected on the basis that if the intention of the insurer had been to restrict the scope of the clause to any occurrence(s) of disease at or near the insured premises, the clause would have said so specifically. It was held therefore that Hiscox agreed to cover effects on the insured business of cases of a notifiable disease irrespective of where they occur.

Hiscox's argument that the restrictions should be interpreted such that only restrictions directed at the insured premises would trigger the cover was also rejected. UKSC accepted that a restriction which had the effect of keeping the public out of the insured premises *even if it was not directed at the insured premises* would qualify as a restriction.

As to the term *"inability to use"* the court accepted that an *impairment* or *hinderance* in use would not suffice, however it did not accept that the term was so wide as to mean inability to use any part of the premises for any business purpose. It was considered that the requirement was satisfied either if the policyholder is unable to use the premises for a *discrete part of its business* activities *or* if he is unable to use a *discrete part of its premises* for its business activities. In both those situations there is a complete inability of use in that in the first situation, there is a complete inability to carry on a discrete business activity and in the second, there is a complete inability to use a discrete part of the business premises.

The Arch[v] wording provided indemnity *for prevention of access to the Premises due to the actions or advice of a government or local authority due to an emergency which is likely to endanger life or property …"*

For the same reasons given in relation to Hiscox 1-4 clauses, it was held that the Arch wording may, depending on the facts, cover prevention of access to a discrete part of the premises and/or for the purpose of carrying on a discrete part of the policyholder's business activities. In both the situations contemplated, access to a discrete part of the premises or access to the premises for a discrete purpose will have been completely stopped from happening.

Causation

Disease Clauses

The insurers contended, inter alia, that the policyholders should establish causation between the illnesses sustained by any person resulting from COVID-19 *within a radius of 25miles* from the insured premises, and that the *"but for" test* should be applied or alternatively that a single or small number of cases of disease occurring within the specified radius was not sufficient. They also argued that it could not be said that the loss was proximately caused by an insured peril.

The UKSC considered the "but for" test to be inadequate in establishing whether an insurer is liable under an insurance contract. Where the context is a claim under an insurance policy, judgements of fault or responsibility are not relevant. All that matters is what risks the insurers have agreed to cover.

In par. 181 of the judgment the UKSC stated the following:

"The most conspicuous weakness of the "but for" test is not that it wrongly excludes cases in which there is a causal link, but that it fails to exclude a great many cases in which X would not be regarded as an effective or proximate cause of Y. If, for example, a cargo is lost when a ship sinks, an unlimited number of circumstances could be identified but for which the loss would not have occurred. These will include some which may be plausible candidates for selection as a proximate cause - for example, the unseaworthy state of the vessel or exceptionally severe weather conditions. But they will also include an endless number of other circumstances. For example, it might equally be said that the loss would not have occurred but for the decision to manufacture the vessel, the decision of the owner or charterer to deploy the vessel on this particular route, the buyer's decision to purchase the cargo and the seller's decision to ship the cargo on that particular vessel, and so on. The main inadequacy, in other words, of the "but for" test is not that it returns false negatives but that it returns a countless number of false positives. That explains why it is often - and for most purposes correctly - described as a minimum threshold test of causation."

The UKSC said that as a general approach to the question of causation in marine insurance cases, the common law developed the test of *"proximate cause"* which [except as the policy otherwise provides] makes the insurer liable for any loss proximately caused by a peril insured against, but, subject as aforesaid, he is not liable for any loss which is not proximately caused by a peril insured against. The starting point for the inquiry is to identify, by interpreting the policy and considering the evidence, whether a peril covered by the policy had any causal involvement in the loss and, if so, whether a peril excluded or excepted from the scope of the cover also had any such involvement. The question whether the occurrence of such a peril was in either case the proximate (or "efficient") cause of the loss involves making a judgment as to whether it made the loss *inevitable then in the ordinary course of events*.

In par. 191 of the judgment UKSC states the following:

"…there is nothing in principle or in the concept of causation which precludes an insured peril that in combination with many other similar uninsured events brings about a loss with a sufficient degree of inevitability from being regarded as a cause - indeed as a proximate cause - of the loss, even if the occurrence of the insured peril is neither necessary nor sufficient to bring about the loss by itself. It seems incontrovertible that in the examples we have given there is a causal connection between the event and the loss."

The UKSC distinguished between the case where two concurrent equally effective causes, one of which is an insured peril and the other *is not*, contribute to the loss and the case where one of these causes is a peril *expressly excluded*.

On the above basis, the UKSC found that *in relation to the disease clauses*, the parties could not reasonably be supposed to have intended that cases of disease outside the radius could be set up as a countervailing cause which displaces the causal impact of the disease *inside* the radius. To apply a "but for" test in a situation where cases of disease inside and outside the radius are concurrent causes of business interruption loss would give the insurer similar protection to that which it would have had if loss caused by any occurrence of a notifiable disease outside the specified radius had been expressly excluded from cover. If the insurers had wished to impose such an exclusion, it was incumbent on them to include it in the terms of the policy.

Whereas the court below held that the disease clauses covered the effects of each case of the disease wherever in the country it occurs, provided that at least one case occurs within the radius specified in the clause the UKSC (arriving at the same result) adopted a different reasoning, namely that only the effects of any case occurring within the radius are covered *but* those effects include the effects on the business of restrictions imposed in response to multiple cases of disease any *one* or more of which occurs within the radius. On the proper interpretation of the disease clauses, in order to show that loss from interruption of the insured business was proximately caused by one or more occurrences of illness resulting from COVID-19, the UKSC held that it is sufficient for the policyholder to prove that the interruption was a result of Government action taken in response to cases of disease *which included at least one case of COVID-19 within the geographical area covered by the clause*.

The UKSC thought that trying to answer the question as to what would be the relative (causative) potency of insured and uninsured cases of disease would in many situations unworkable.

Prevention of access and hybrid clauses

Applying the same reasoning, *regarding prevention of access and hybrid clauses* the UKSC decided that it will be sufficient to prove that the interruption was a result of closure or restrictions placed on the premises in response to cases of COVID-19 which included *at least one case manifesting itself within a radius of 25 miles of the premises.* It was accepted that the peril covered by the clause is itself a composite one comprising elements that are required to occur in a causal sequence in order to give rise to a right of indemnity. The elements of the insured peril in their *correct* causal sequence, were: (A) an

occurrence of a notifiable disease, which causes (B) restrictions imposed by a public authority, which cause (C) an inability to use the insured premises, which causes (D) an interruption to the policyholder's activities that is the sole and direct cause of financial loss.

It was held however that the last element in the causal chain is just as much part of the insured peril as the other elements and the insured peril should be treated as the risk of *all elements* occurring *in causal sequence* and not the risk of any one or more of the elements occurring.

Hiscox's reliance on the words "solely and directly" as one of its grounds of appeal for arguing that the extent of the indemnity provided is only in respect of losses proximately caused by the insured peril alone and nothing else was, in the opinion of the court, out of place. The UKSC decided that an interpretation which would treat the cover as so limited and uncommercial in its scope required clear words in the Policy. In the Court's opinion it would undermine the commercial purpose of the cover to treat such potential effects as diminishing the scope of the indemnity. The underlying reason was that although not themselves covered by the insurance, *such effects are matters arising from the same original fortuity which the parties to the insurance would naturally expect to occur concurrently with the insured peril*. In that sense they are not a separate and distinct risk.

In conclusion, the public authority clause in the Hiscox policies indemnifies the policyholder against the risk of all the elements of the insured peril acting in *causal combination* to cause business interruption loss; but it does so r*egardless of whether the loss was concurrently caused by other (uninsured but non-excluded) consequences* of the COVID-19 pandemic which was the underlying or originating cause of the insured peril.

Regarding the Arch *prevention of access clause*, the UKSC accepted the insurer's arguments that the clause does not cover loss of turnover caused by an emergency or by Government actions or advice in response to an emergency but which has not brought about by prevention of access to the premises. It was accepted that it is only loss *occasioned by prevention of access to the premises* that is covered by the clause. However, if the concurrent causes arose out of the same underlying or originating cause, namely the COVID-19 pandemic, on the correct interpretation of the Arch wording, such loss would be covered by the policy.

It was further held that the RSA 1 clause properly interpreted, covered loss caused by the two elements of the insured peril operating in the required causal sequence, but does so regardless of whether any other (uninsured *but non-excluded*) consequences of the same underlying fortuity (the COVID-19 pandemic) were concurrent causes of the loss.

Trends Clauses

These clauses related to the quantification of the loss. The UKSC rejected the application of the *but for* test in connection with this issue as well.

The only remaining question was whether trends clauses in issue on the appeals should be construed so that the standard turnover or gross profit derived from previous trading is adjusted only to reflect circumstances which are unconnected with the insured peril and not circumstances which are inextricably linked with the insured peril in the sense that they have the same underlying or originating cause.

Overruling the judgment of the Court of Appeal in **Orient-Express Hotels Ltd v Assicurazioni Generali SpA (trading as Generali Global Risk) [2010] EWHC 1186**, the UKSC held that the trends or circumstances for which adjustments may be made do not include trends or circumstances caused by the insured peril (or its underlying or originating cause). Furthermore, the aim of any adjustment is to seek to ensure that the adjusted figures will represent as nearly as possible the results which would have been achieved during the indemnity period *had the insured peril (and its underlying or originating cause) not occurred.*

Landmark decision on Causation?

It seems clear that the UKSC has not dispensed with the *but for test* where questions of responsibility and fault are in issue. The causal link in insurance law was always established in insurance law by reference to the doctrine of *proximate cause* and indeed the causation analysis in the above case relates to matters of insurance law. The principle that the insured would not be precluded from recovering where two or more effective causes (one of which is insured and one which isn't) contribute to the loss has been stated in the case law before, so as the distinction between this scenario and the scenario where one of these *effective* causes is excluded by the policy wording.

It could be said however that the establishment of a causal link between the insured peril (*as this has been "narrowly" identified by the UKSC in comparison with the broader insurance peril identified by the court below*) and the loss, would seem far fetched under any other circumstances or set of facts. The contribution of the *insured peril* to the loss could be so minimal in some instances (or geographical aeras) so that the causation principles applied, or arguably overstretched by the UKSC may have the same effect as -at least indirectly- widening the scope of the insured peril or cover to the extent of the insured peril which was identified by the court below. In that respect, it could be said that the reasoning of the High Court may offer a more straight-forward approach as to what would have been contemplated by the parties to the insurance contract in a Covid-19 like scenario.

What may also be worth noting is that in the hypothetical scenario where in two distinct 25mile radius areas, say A and B respectively, A being the area which has not witnessed a case of "sustaining" or "manifesting" of the disease albeit hosting a much larger number of policyholders than area B (hosting for example only one policyholder), only the policyholder in area B would be able to recover his loss caused by the government measures which were taken in response to Covid 19 while the policyholders in area A would have no redress (this remark relates to insurance policies defining geographical areas, as described above).

However, the UKSC's judgment in the above case provides a superb in-depth analysis of the argumentation, the legal principles discussed and their application to the special facts of the case.

It will be interesting indeed to see how the cases of different type of businesses would turn on the evidence presented in circumstances under which the application of the legal principles emanating from the judgment do not, without more, resolve the dispute.

Nicos Avraamides, Partner
L. Papaphilippou & Co, LLC

[i] Royal & Sun Alliance Insurance PLC

[ii] QBE UK Ltd

[iii] The difference with RSE 3 wording was that the word *"manifested"* (as opposed to *"sustained"* of the RSA3) required that the person concerned must either have displayed symptoms of the disease or have been diagnosed as having the disease (for example by means of a test).

[iv] Hiscox Insurance Company Ltd

[v] Arch Insurance (UK) Ltd