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Analysis of the Supreme Court's decision in the FCA Covid-19 Test Case

1. The Supreme Court has handed down its eagerly anticipated judgment in *Financial Conduct Authority v Arch Insurance (UK) Ltd and others* [2021] UKSC 1. The Court has ruled largely in favour of policyholders and, while it accepted some of the insurers' arguments, in no case has that acceptance affected the outcome of the appeal.

2. The Supreme Court addressed six issues:

    a. interpretation of "disease clauses" (which cover business interruption losses resulting from any occurrence of a notifiable disease within a specified distance of insured premises) [48-95];
    b. interpretation of "prevention of access" clauses (which cover business interruption losses resulting from public authority intervention preventing access to, or the use of, business premises) and "hybrid clauses" (which contain both disease and prevention of access elements) [96 – 159];
    c. the question of what causal link must be shown between business interruption losses and the occurrence of a notifiable disease (or other insured peril specified in the relevant policy wording) [160 – 250];
    d. the effect of "trends clauses" (which prescribe a standard method of quantifying business interruption losses by comparing the performance of a business to an earlier period of trading) [251 – 288];
    e. the significance in quantifying business interruption losses of effects of the pandemic on the business which occurred before the cover was triggered ("Pre-Trigger Losses") [289 – 296]; and
    f. in relation to causation and the interpretation of trends clauses, the status of the decision of the Commercial Court in Orient-Express Hotels Ltd v Assicurazioni Generali SpA (trading as Generali Global Risk) [2010] EWHC 1186 (Comm) ("Orient-Express") [297 – 312].

3. **Facts**: In March 2020, the UK Government began to take a series of measures to combat the transmission of COVID-19. These included informal announcements and instructions from the Prime Minister as well as the passage of primary and secondary legislation through the UK Parliament and devolved administrations. The present appeals considered the impact of these actions and measures on 28 clauses in the 21 lead policies written by the Appellant Insurers. The FCA and the Appellant Insurers agreed to submit those policy wordings for consideration with the aim of addressing issues arising from similar policies prevalent in the insurance industry.

4. **Disease clauses**: The Supreme Court took the wording of the relevant insuring clause in the RSA 3 policy as an exemplar: "any … occurrence of a Notifiable Disease within a radius of 25 miles of the Premises". At first instance, the Divisional Court construed the peril insured by the clause broadly, such that the policy responded to business interruption losses resulting from the COVID-19 pandemic provided there had been an occurrence (meaning at least one case) of the disease within the relevant geographical radius. Whilst Lord Briggs and Lord Hodge agreed with the court below, Lord Hamblen and Lord Leggatt (with whom Lord Reed agreed) disagreed and accepted the argument advanced by the insurers: each case of illness sustained by a person as a result of COVID-19 is a separate "occurrence"; and the clause only covers business interruption losses resulting from cases of disease which occur within the relevant radius. Given the ultimate battle over the scope of cover, it is a somewhat pyric victory in light of the Supreme Court's conclusions in respect of causation.

5. **Prevention of Access Clauses and Hybrid Clauses**: Such clauses specify a series of requirements which must all be met before the insurer is liable to pay, a frequent requirement being "restrictions imposed" by a public authority following an occurrence of a notifiable disease. The Supreme Court disagreed with the view of the Divisional Court that this requires a measure expressed in mandatory terms which has the force of law. Rather, it is sufficient that there is an instruction given by a public authority which carries the imminent threat of legal compulsion or is in mandatory and clear terms and indicates that compliance is required without recourse to legal

powers. The Supreme Court also gave its views on the meaning of a requirement that business interruption loss is caused by the policyholder's "inability to use" the insured premises, it took a broad view concluding that it may be satisfied where a policyholder is unable to use the premises for a discrete business activity or is unable to use a discrete part of the premises for its business activities - "prevention of access" to the premises was interpreted in a similar broad manner.

6. **Causation**: The Divisional Court found as a matter of fact that the public health measures were taken in response to information about all the cases of COVID-19 in the country as a whole. It went on to hold, and the Supreme Court agreed, that all the individual cases of COVID-19 which had occurred by the date of any Government measure were equally effective "proximate" causes of that measure (and of the public response to it). It is therefore sufficient for a policyholder to show that at the time of any relevant Government measure there was at least one case of COVID-19 within the geographical area covered by the clause. As a consequence, the Supreme Court agreed with the FCA's central argument in relation to the radius provisions that 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 [195].

7. **Trends clauses**: The Supreme Court has held that these clauses should not be construed so as to take away cover provided by the insuring clauses - rather they 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" (i.e. in the present case the COVID-19 pandemic and its effects).

8. **Pre-Trigger Losses**: In light of its conclusions in respect of trends clauses the Supreme Court reversed the Divisional Court's decision to permit adjustments to be made

under the trends clauses to reflect a measurable downturn in the turnover of a business due to COVID-19 before the insured peril was triggered.

9. **The *Orient-Express***: The Supreme Court held that the first instance decision of Hamblen J (as he then was) was wrongly decided and should be overruled. The case, which concerned Business Interruption losses to a hotel in New Orleans following Hurricane Katrina, formed a key part of the insurers' arguments on causation and trends clauses. Lord Leggatt was also involved in the *Orient Express* as arbitrator, and their judgment rather charmingly concluded with a reference to what Justice Jackson said in *McGrath v Kristensen*, 340 US 162, 177-8 (1950), concurring in a decision which contradicted an opinion he had given when Attorney General, including the following: "*Perhaps Dr Johnson really went to the heart of the matter when he explained a blunder in his dictionary - 'Ignorance, sir, ignorance.' But an escape less self-depreciating was taken by Lord Westbury, who, it is said, rebuffed a barrister's reliance upon an earlier opinion of his Lordship: 'I can only say that I am amazed that a man of my intelligence should have been guilty of giving such an opinion.' If there are other ways of gracefully and good naturedly surrendering former views to a better considered position, I invoke them all.*"

Comment

10. It should be noted that there were some policies and clauses on which the FCA lost at first instance and did not appeal, albeit that it did appeal against conclusions in respect of certain words within those clauses insofar as they raised common issues with policies on which there were appeals. The Supreme Court decided not to address those clauses as it was academic given that there was no appeal against the overall unfavourable result.

11. The Supreme Court was clear that it should be borne in mind that it was only deciding a test case, the object being to achieve the maximum clarity possible for the maximum number of policyholders and their insurers, consistent with the need for expedition and proportionality. The claim was brought against only eight insurers and

consideration limited to a representative sample of 21 standard form business interruption policies. As a consequence, whilst a number of general points of principle have been decided it is unlikely to be the end of the matter for many insurers and their policyholders. Ultimately the specific wording of any particular policy remains king. Each policy should be carefully scrutinised, in the knowledge that there is still scope for legal argument.

12. This is further complicated by the fact that the claim was commenced on 9 June 2020. There have of course been many developments in respect of the pandemic and the response to it since that were not before the court and may give rise to points of dispute. Nevertheless, the judgment contains a number of helpful examples which may help to provide more clarity in particular contexts.

13. A number of policies included unclear wording in relation to the mechanics or nature of intervention required to trigger POA or Hybrid clauses. By way of example, the RSA 3 policy defined "Notifiable Disease" as "any human infectious or human contagious disease … an outbreak of which the competent local authority has stipulated shall be notified to them." However, COVID-19 was made a notifiable disease by amendment to the Health Protection (Notification) Regulations 2010 on 6 March 2020, not by the stipulation of a local authority. The Supreme Court concluded that a reasonable reader would understand the wording as intended to refer to those diseases which are classified as "notifiable diseases" by the 2010 Regulations – such that cover could not be denied on this basis.

14. RSA 3 included a general exclusion: "*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*." As is commonly the case, the general exclusion was to be found in a different part of the policy to the disease extension. Faced with the apparent tension, the Supreme Court held that 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".

15. The Supreme Court also offered useful guidance on the "inability to use" policy requirement. The FCA proffered an example of a bookshop, required to close with the loss of all its walk-in customer business, representing some 80% of its income. The fact that it could continue to use the premises for telephone orders, representing 20% of its income, did not alter the fact that there was an inability to use its premises for a discrete part of its business activities. The Supreme Court considered that there would potentially be an "inability to use" the premises for the discrete business activity of selling books to walk-in customers. Similarly, a department store which had to close all parts of the store except its pharmacy would potentially have an "inability to use" a discrete part of its business premises. An example which potentially covers both cases would be a golf course which is allowed to remain open but with its clubhouse closed so that there is an "inability to use" a discrete part of the golf club for a discrete but important part of its business, namely the provision of food and drink and the hosting of functions. It is to be noted that the FCA accepted that there is only cover for that part of the business for which the premises cannot be used. For example, a restaurant which also offers a takeaway service decides to close down the whole business it could only claim in relation to the restaurant part of the business (a point equally applicable to prevention of access cases).

16. One of the potentially legally significant aspects of the decision is the Supreme Court's conclusion that satisfaction of the "but for" test of causation is neither a necessary nor sufficient test for legal causation. To illuminate the point, the Supreme Court set out a hypothetical, in which 20 individuals combine to push a bus over a cliff. Assume it is shown that only 13 or 14 people would have been needed to bring about that result. In the Supreme Court' view, even though it could not be said that the

participation of any given individual was either necessary or sufficient to cause the destruction of the bus, it would still be appropriate to describe each person's involvement as a cause of the loss. In the context of multiple concurrent causes, there is no general answer to the question as to whether a single event should be regarded as a cause of a loss – it depends on the context in which the question is asked. In disputes over liability under an insurance policy, the relevant context is "what risks the insurers have agreed to cover". It comes down to the intentions of the parties, objectively ascertained [190]. It will be interesting to see what impact the judgment has beyond the context of insurance law.

17. In reaching its view, the Supreme Court noted that much time has been spent attempting to delineate the causal consequences of specific language in policies, such as "following", "arising from" or "as a result of". The Supreme Court accepted that sometimes the policy language may indicate that a looser form of causal connection will suffice than would normally be required, such as use of the words "directly or indirectly caused by …": see eg *Coxe v Employers' Liability Assurance Corpn Ltd* [1916] 2 KB 629. However, the Supreme Court stated "it is rare for the test of causation to turn on such nuances". As such, causation is not so much a question of linguistic analysis, rather "at issue is the legal effect of the insurance contract, as applied to a particular factual situation."

18. In determining whether there has been an occurrence within the relevant radius, a realistic view should be taken, they should not be read in a narrow or literal way [209]. The Supreme Court had little difficulty in dispatching the hypotheticals advanced on behalf of insurers involving passengers on trains and fishermen passing the Scilly Isles. In the Supreme Court's view, the parties to the policy would not have intended that such events would not constitute a trigger.

Conclusion

19. The Supreme Court's judgment is likely to assist many, although not all, policy holders who held business interruption insurance prior to the pandemic. However, as the

Supreme Court has emphasised, the specific policy wording is key and each claim will need to be considered on its merits. Outside of the business interruption context, the decision also contains important guidance on the approach that courts will now take to the construction of insurance policies, arguably signalling a purposive approach that, while not inconsistent with previous authority, might generally be said to be more favourable to policy holders. The full impact of the decision may therefore be much wider than the immediate policy context.

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