

BRIEFING NOTE

COVID-19 Business Interruption Insurance – Welcome News for Policyholders, and Something for the Insurers

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Introduction

In our earlier briefing note ([COVID-19 Business Interruption Insurance – Contract Uncertainty: The FCA Commences Declaratory Proceedings](#)), we reported that the Financial Conduct Authority of the UK (the “FCA”) commenced declaratory proceedings to clarify the indemnity provided by disease and prevention of access policy extensions and how the amount of the indemnity payable for the resulting business interruption losses was to be calculated.

On 15 September 2020, the UK Commercial Court handed down its judgment on the Test Case (*The Financial Conduct Authority v Arch & Others* [\[2020\] EWHC 2448 \(Comm\)](#)). Although only 21 sample wordings were considered, the FCA estimates that some 700 types of policies issued by more than 60 different insurers to over 370,000 policyholders could be impacted by the judgment. Whilst the wording of any policy may be unique, the Court’s judgment will provide helpful guidance in determining and quantifying the indemnity provided by disease, prevention of access or hybrid extensions.

Non-Damage Business Interruption Cover

The Court was asked to consider three types of “non damage” cover, provided as policy extensions, that respond to financial losses (such as loss of profits and additional expenses commonly known as business interruption “BI” losses) incurred in circumstances in which the insured premises do not suffer physical damage, such as by fire or flood:

- Disease Extension: indemnity for BI resulting from the occurrence of a notifiable disease at or within a specified radius of the insured premises.
- Prevention of Access Extension: indemnity for BI resulting from the denial or hindrance of access to, or use of, the insured premises due to danger or public emergency necessitating government or local authority actions or restrictions.
- Hybrid Extension: indemnity for BI resulting from closures or restrictions imposed on the insured premises in response to an infectious or contagious disease.

Disease Extension

In applying the Disease Extension, the Court held that cover is triggered if there was: (i) an outbreak of the disease at the insured premises (or defined radius); (ii) the outbreak

interrupted/interfered with the insured business; and (iii) the composite peril (outbreak plus interruption/interference) caused the financial loss claimed by the policyholder.

The Court determined two important points in favour of policyholders. First, an outbreak of the disease occurred when persons who are symptomatic or asymptomatic (but diagnosed) attended the insured premises (or defined radius). Second, outbreaks at an insured location are an indivisible part of the epidemic, otherwise are separate but effective causes of national actions in response, such that multiple outbreaks of the disease do not prohibit recovery.

Taking these points together, notwithstanding the outbreak of the disease at other locations across the country, the extension is triggered when: (i) the disease occurred/manifested at the insured premises (or defined radius); (ii) the insured business was interrupted/interfered as a result of the local or national outbreak; and (iii) there is consequential financial loss.

Prevention of Access Extension

In applying the Prevention of Access Extension, the Court held that cover is triggered only if the relevant authority mandates by law the prevention or hindrance of access to, or use of, the insured premises, in response to the localised occurrence of the disease.

The Court determined two important points in favour of insurers. First, a government advisory was not mandatory. There needs to be an order with force of law preventing or limiting access to, or use of, premises. Second, government action in response to a nationwide epidemic was insufficient to trigger cover. The wordings tended to refer to specific events happening at a particular time and place, indicating an intention to cover localised events only.

Taking these points together, the extension is triggered when: (i) the disease occurred/manifested at the insured premises (or defined radius); (ii) the insured premises were closed by a legal order in response to that specific occurrence/manifestation; and (iii) there is consequential financial loss. However, if the insured premises were closed in response to a national epidemic, not a localised outbreak, then the extension is unlikely to respond.

Hybrid Extension

In applying the Hybrid Extension, the Court held that cover is triggered if the authority mandates the closure of, or restrictions to, the insured premises in response to occurrence or manifestation of the disease (at the insured premises (or defined radius) or elsewhere).

The Court determined one point in favour of insurers and one point in favour of policyholders. In favour of insurers, an action which prevents or limits access to, or use of, the insured premises requires an order with the force of law, rather than a mere advisory. In favour of policyholders, that action may be in response to a national epidemic, rather than a localised outbreak at the insured premises (or defined radius).

Taking these points together, the extension is triggered when: (i) the insured premises were closed by law in response to a local outbreak or national epidemic; and (ii) there is consequential financial loss.

The Trends Clause

If the extension is triggered, then the amount of the indemnity falls for consideration. The trends clause determines how the amount of the indemnity is to be calculated. The Court held that the purpose of the trends clause was to put the policyholder into the same financial position that it would have enjoyed if the insured peril had not occurred.

With reference to the Disease Extension, the (composite) insured peril was: (i) occurrence of the disease at the insured premises (or defined radius); and (ii) interruption/interference to the insured business. The outbreak of the disease had to be ignored entirely when calculating the financial loss and the amount of the indemnity.

With reference to the Prevention of Access Extension, the (composite) insured peril was: (i) the denial of access or prevention of use; (ii) by civil order; and (iii) by reason of a local outbreak, all of which had to be ignored when calculating the financial loss and the indemnity payable. The impact of the disease nationwide should be taken into account.

With reference to the Hybrid Extension, the (composite) insured peril was: (i) the closure to access or restriction of use; (ii) by civil order; and (iii) by reason of a national outbreak, all of which had to be ignored when calculating the financial loss and the indemnity payable.

In applying the trends clause, the Court determined that the earlier case of *Orient Express Hotels Ltd. v Assicurazioni Generali SpA* [2010] EWHC 1186 (Comm) had not been correctly decided. Specifically, it gave rise to the absurd result that the more serious or widespread the peril, the less cover was available and the smaller the amount of the indemnity.

Distinguishing *Orient-Express*, the Court held that in calculating the (hypothetical) income that would have been received but for the interruption/interference, the insured premise is not to be considered a COVID-free haven immune to the national epidemic and the authorities' actions in response. Instead, it is the income that would have been received if there had been no nationwide epidemic and no civil authority response. To suggest otherwise would render coverage "*illusory*" that "*cannot have been intended*" by the parties.

Burden of Proof

The Court did not issue guidance on how COVID-19 will be held to have occurred/manifested. That will have to be established with reference to specific evidence and national data.

Summary

The judgment is good news for policyholders who purchased the Disease Extension or the Hybrid Extension, providing cover in circumstances in which the policyholder can establish the occurrence/manifestation of the disease at the insured premises (or defined radius) or the closure of insured premises in response to the occurrence/manifestation of the disease. The disease as part of a wider epidemic will not prejudice cover and will be ignored when calculating the amount of the indemnity such that the policy limits may be achieved.

The judgment is more restrictive for policyholders who purchased the Prevention of Access Extension. Those policyholders will be required to show that access to, or use of the insured premises, was denied or restricted by a civil order issued in response to a localised outbreak at those premises and only that localised outbreak will be ignored in calculating the indemnity payable. The national epidemic will be considered and by impacting the hypothetical income of the business, will reduce the amount of the indemnity.

How We May Assist

Since the declaration of a pandemic, our lawyers have been assisting all stakeholders in the insurance industry, insurers, brokers and policyholders, with business interruption insurance claims arising from the pandemic. To date, we have assisted commercial, hospitality and retail property owners, as well as international construction companies, with advancing and supporting COVID-19 related claims and negotiating renewal premiums for insurance policies.

We would be delighted to assist you or your company in considering its insurance coverage.

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