More news from the English Court on Business Interruption Insurance and COVID-19

Poonam Melwani QC & Tim Marland

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In two recent decisions, ***The Financial Conduct Authority v Arch Insurance (UK) Ltd and others*** [2020] EWHC 2448 (Comm) ('the FCA Test Case') and ***TKC London Limited v Allianz Insurance Plc*** [2020] EWHC 2710 (Comm) ('TKC'), the English Court has considered various standard form business interruption wordings and the extent to which they respond to the Covid-19 pandemic and ensuing government measures to contain the spread of the virus, notably the enforced closure of businesses. The FCA Test Case considered the engagement of various 'non-damage' business interruption extensions to traditional cover. TKC confirms the prevailing orthodoxy, at least in this jurisdiction, that 'traditional' business interruption insurance does not respond to business interruption losses caused by the temporary closure of the business where there has been no physical damage.

(1) The FCA Test Case

The FCA test case has been the subject of a proliferation of articles and comment since the judgment was produced. As the overall result was something of a 'score draw' and given its undoubted significance, the judgment is unsurprisingly the subject of appeal. It is not the intention of this article to review the judgment as a whole, but to focus on two aspects which are of wider application than the specific context of the non-damage extensions under consideration. These are: (1) the proper approach to the construction of exclusions within a policy of insurance (2) the Court's consideration of ***Orient-Express Hotels Ltd v Assicurazioni Generali SpA*** [2010] EWHC 1186 (Comm)

Exclusions in insurance policies

At paragraphs [62] to [79] the FCA Test Case provides a useful and detailed exposition of the approach to construction of insurance policies and the provisions therein, including exclusion clauses. There has in the past often been a tendency to approach exclusion clauses in insurance policies in the same manner as contractual exemptions from liability *ie* to adopt a narrow construction, to apply (where appropriate) the *contra proferentem* approach *etc.* In the FCA Test Case the Court confirmed that *contra proferentem* is now largely obsolete (*"it is clear that that principle, if it still has any validity..."* para.[71]). The Court held that the approach to construction of exclusion clauses in insurance policies was "correctly summarised" by Peter MacDonald Eggers QC sitting as a Deputy High Court Judge in ***Crowden v QBE Insurance (Europe) Limited*** [2017] EWHC 2597 (Comm). In that case the judge held that:

"65. In my judgment, applying this approach [ie the Impact Funding approach], the Court must adopt an approach to the interpretation of insurance exclusions which is sensitive to their purpose and place in the insurance contract. The Court should not adopt principles of construction which are appropriate to exemption clauses - i.e. provisions which are designed to relieve a party otherwise liable for breach of contract or in tort of that liability - to the interpretation of insurance exclusions, because insurance exclusions are designed to define the scope of cover which the insurance policy is intended to afford. To this end, the Court should not automatically apply a contra proferentem approach to construction. That said, there may be occasions, where there is a genuine ambiguity in the meaning of the provision, and the effect of one of those constructions is to exclude all or most of the insurance cover which was intended to be provided. In that event, the Court would be entitled to opt for the narrower construction. This result may be achieved not only by the application of the contra proferentem approach, but also the approach adopted by Lord Clarke, JSC in Rainy Sky SA v Kookmin Bank [2011] UKSC 50; [2011] 1 WLR 2900, that in the case of ambiguity, the Court may opt for the more commercially sensible construction, at paragraph 21: "If there are two possible constructions, the court is entitled to prefer the construction which is consistent with business common sense and to reject the other". That said, as Lord Clarke, JSC also said, at paragraph 23 of his judgment: "Where the parties have used unambiguous language, the court must apply it". This would, however, be subject to considerations of absurdity or where something plainly has gone wrong with the language of the contract."

This aspect of the judgment is unlikely to be the subject of the appeal and thus is likely to be the 'touchstone' for

construction of such clauses going forward.

The Orient-Express case

This involved a hotel in the French Quarter of New Orleans. The hotel's owners made a claim for material damage and business interruption following extensive damage in consequence of Hurricanes Katrina and Rita. The hotel was closed for some months and there were significant business interruption losses.

Insurers resisted liability under the main provisions of the business interruption insurance on the ground that the insured could not recover in respect of loss which would have occurred even absent physical damage to the hotel itself. Since the hurricanes had devastated the whole of the surrounding area of New Orleans, the insured would have suffered the same business interruption loss even if the hotel had remained undamaged, since no one would have visited the hotel given the devastation in the vicinity. This was relevant to the standard trends clause in the policy, which provided:

"...adjustments shall be made as may be necessary to provide for the trend of the Business and for variations in or special circumstances affecting the Business either before or after the Damage or which would have affected the Business had the Damage not occurred so that the figures thus adjusted shall represent as nearly as may be reasonably practicable the results which but for the Damage would have been obtained during the relative period after the Damage."

The dispute was initially referred to arbitration. The panel in effect applied a "but for" test of causation and determined that *"it is necessary to assess the BI loss on the hypothesis that the hotel was undamaged but the City of New Orleans was devastated as in fact it was"*. On appeal, Hamblen J (as he then was) affirmed the arbitrator's decision.

As noted in the FCA Test Case (at [528]) this result has been the subject of academic criticism, perhaps best encapsulated by Professor Merkin as a *"curious outcome that, the greater the damage to the vicinity and thus of the risk of depopulation, the less prospect there is of any recovery by the assured"*

The Court in the FCA Test Case concluded that the hurricanes were an integral part of the insured peril and thus that when construing "had the Damage not occurred" in the trends clause *"both the damage to the hotel and the hurricanes and their effect generally were to be stripped out"* (paragraph [527]).

Although in the event the Court held that **Orient-Express** was not necessary for its evaluation of the clauses before it, *"if we had thought that the decision in Orient Express somehow dictated the consequences in terms of cover and the counterfactual analysis for which the insurers contend in the present case, we would have reached the conclusion that it was wrongly decided and declined to follow it."* (paragraph [529]).

The Court's approach to counterfactuals is one of the grounds of appeal for insurers in the leapfrog appeal to the Supreme Court and so it remains possible that the **Orient-Express** approach will be reinstated. In addition, on the approach taken by the Court, the analysis of **Orient-Express** was strictly speaking *obiter* and so it remains open for insurers to argue that it is the correct approach in spite of this judgment.

(2) The TKC case

The Claimant insured is the owner of a crêperie in Kensington which was forced to close as the result of the legislation passed by the UK Government in March of this year. It was insured by Allianz under a Commercial Combined policy of insurance, which included in pertinent part a Property Damage All Risks section ('the PD Section') and a section entitled Business Interruption Estimated Revenue All Risks ('the BI Section'). The BI Section was traditional orthodox Business Interruption cover and there was no Disease Extension or similar.

The PD Section defined 'Damage' as *"Accidental Loss or destruction of or damage to Property Insured"*. The BI section provided cover for *"Business Interruption by any Event"* and Event was in turn defined as *"Accidental Loss or destruction of or damage to property used by the Insured at the Premises for the purpose of the Business"*. The word 'physical' did not appear and it was common ground that the relevant qualifier of 'loss' was 'loss of' rather than 'loss to'.

TKC's primary case was that the closure of its premises amounted to loss of property within the meaning of the BI Section. Allianz applied for summary judgment on the basis that 'loss' in context required physical loss and that temporary loss of use did not qualify. In any event, as there was no claim under the PD Section, there could be no claim under the BI Section *inter alia* because of the Basis of Settlement provisions which, in common with most orthodox BI policies, required that:

at the time of any event

(A) There is an insurance in force covering the interest of the Insured in the property at the Premises against such Event and that

(i) payment has been made or liability has been admitted for payment, or

(ii) payment would have been made or liability would have been admitted for payment but for the operation of the proviso in such insurance including liability for claims below a specified amount ..

The judge (Richard Salter QC sitting as a Deputy Judge of the High Court) accepted that the cover under the Policy was broad, and that what had occurred satisfied the requirement of being an 'event' (uncapitalised) in the definition of Business Interruption. However, he held that 'loss' did not cover mere temporary deprivation of the use of property and thus that this was not Business Interruption caused by an Event (capitalised and defined as above). The question of whether more permanent deprivation of use, or deprivation of use where recovery was uncertain, would *prima facie* constitute 'loss' was left open. The closure of premises by government edict in response to Covid-19, where it was obvious that such would not be a permanent closure, did not therefore trigger coverage under the Policy. This was confirmed by the fact that there was no claim under the PD Section of the Policy and accordingly the Basis of Settlement provisions of the BI Section were not met.

This result will be welcomed by insurers as confirmation that, in this jurisdiction at least, 'traditional' Business Interruption insurance requires a trigger of physical 'damage' and that such policies do not respond to the general measures introduced in respect of the pandemic. Whilst this perhaps leaves open the issue of premises/businesses where there has been an actual Covid outbreak or confirmed 'contamination' by Covid, the reality is that, as often as not, there will be a pollution/contamination exclusion in place, rendering the question of *prima facie* coverage moot.

POONAM MELWANI QC and TIM MARLAND

Poonam Melwani QC

"Her strengths include an intelligent, thorough and detail-driven approach and a capacity to handle complex, high-value matters." (Legal 500, 2021)

Poonam Melwani QC is a commercial silk who practises across the full spectrum of commercial, insurance, energy and shipping law, providing advisory and advocacy services. Praised as "... always in demand, she is as good on her feet as she is adept at mastering complex legal, factual and expert material...." (Chambers UK), Poonam has been ranked as a 'Leading Silk' over many years by the Legal Directories. She represents clients in a wide variety of jurisdictions and arbitral regimes including ICC, LCIA, LMAA and ad hoc, as well as English High Court Litigation, mainly in the Commercial Court and the Appellate Courts. Poonam has been shortlisted for Shipping Silk of the Year at the Legal 500 UK Awards 2020.

> view Poonam's full profile poonam.melwani@quadrantchambers.com

Tim Marland

"A silk in all but name. A real all-rounder who understands the industry, and an opponent who should be feared." (Legal 500, 2021)

Tim is ranked as 'Star Individual' for Aviation in Chambers & Partners 2019 and is consistently recommended as a leading junior by Chambers & Partners and the Legal 500 legal directories where he is praised as: "Our go-to barrister for high profile cases. I can't think of any other barristers ahead of him; he's very client-focused and knows the insurance market well." "Active, prominent and very good; he's very established in this field and is an excellent barrister." "He's good at giving strong, commercial, practical and down-to-earth advice.." and "is able to guide a court through complex case law in a very simplistic way and convey technical points that would otherwise take days at trial". Tim is one of only seven members of the Bar listed in Who's Who Legal Global Guide 2019 under Aviation – Contentious and is currently the only member of the Bar with the top ranking Global Elite Thought Leader in that category.

> view Gaurav's full profile tim.marland@quadrantchambers.com