BUSINESS INTERRUPTION INSURANCE CLAIMS ARISING FROM COVID-19

David Berkley QC &
Neil Fawcett

Business Interruption Insurance Claims arising from COVID-19

By David Berkley QC and Neil Fawcett

This guide is intended to act as an aide-memoire to Part III of the 'Staying Virtually Up-to-Date' Series delivered by 3PB's Commercial Team on 13th May 2020. Thank you for joining us!

Whilst every effort has been taken to ensure the accuracy of the contents of this guide, Parliament resumed last week and the position in relation to Covid-19 is rapidly changing. This document should not be used as a substitute for obtaining legal advice.

To discuss this or any other matter further with David or Neil, please contact their clerks below.

David Fielder david.fielder@3pb.co.uk

James Parks james.parks@3pb.co.uk

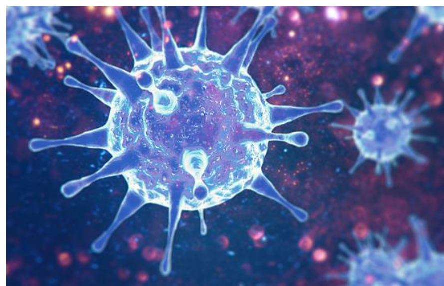
INTRODUCTION

Businesses across the country remain shut down and face mounting losses affecting not just cash-flow, but their very survival.

Although the UK government's furlough scheme provides for 80% of staff wages, businesses have been left with no provision for what amounts in many cases to the complete loss of their revenue.

An essential part of responsible business practice is managing risk and although companies have Business Interruption Insurance (**BII**) policies in place, it is becoming increasingly clear that the big insurers are less than keen to pay out.

COVID-19



SARS-CoV-2 (***Coronavirus***) began to spread through the UK in early 2020.

Coronavirus causes many people infected by it to suffer respiratory and other symptoms designated officially as a disease[1] in the UK as "**COVID-19**".

The outbreak originated in Wuhan in China sometime towards the end of 2019 before spreading to the UK. It gained public prominence here in January and February 2020 and by 2:00pm on 21st March 2020 the UK government had brought into force the ***The Health Protection (Coronavirus, Business Closure) (England) Regulations 2020*** requiring business across the country to close.

Those regulations were very shortly thereafter repealed and replaced by the ***The Health Protection (Coronavirus, Restrictions) (England) Regulations 2020*** which came into force on 26th March 2020 at 1:00pm which were themselves amended by ***The Health Protection (Coronavirus, Restrictions) (England) (Amendment) Regulations 2020***, which came into force on 22nd April 2020 at 11:00am.

---

1 See *Coronavirus Act* 2020, s.1(1)

At the time of writing the country continues to be on lock-down, with most of the population being confined, with exceptions, to the places where they live.

Restaurants, bars, cafés, and many businesses in the retail and hospitality sectors remain closed and will probably remain so for at least the next couple of months with all the disruption to business and associated losses.

INSURANCE POLICIES

When selling **BII**, insurers typically provide a schedule of cover, along with the detailed policy terms and conditions. The ***policy*** and the ***schedule*** form a contract between the insurer and the business where the insurer agrees to pay out an agreed amount based on certain insured events, sometimes called “triggers” or “contingencies”.

Policy wordings vary widely between insurers, with some providing cover in the event of forced closure by a relevant public authority and others providing specifically for outbreaks of certain types of disease to trigger insurance policies.

As to which terms apply to any particular business, only a detailed examination of the ***policy*** wording itself, and the ***schedule*** to the policy will provide answers.

To complicate matters further, some insurers deliberately sought to exclude certain SARS-like diseases from the remit of their policies following the 2003 outbreak in Asia and some business-owners have now been told by their insurers that they have no remedy, even though they purchased policies that they thought fully covered them in the event of an outbreak.

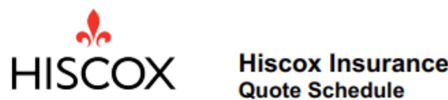
“Our Business Interruption cover is based on a specified list of diseases and has been since the SARS outbreak in 2003. These policies exclude business interruption due to new and emerging diseases, like COVID-19. Our policy wording clearly identifies the diseases we offer cover for and, in addition, highlights that new and emerging diseases like COVID-19 are not covered.”

WHO IS COVERED?

Schedules of cover normally set out clearly whether **BII** is included within the terms of cover. Some schedules describe the cover as "Business Interruption Insurance", whilst some describe it as "Revenue Protection". The ***schedule*** often sets out the maximum limit of the insurance pay-out, briefly details exclusions from the cover and refers to the ***policy*** for a description of exactly what is covered and in what circumstances.

An example of a typical policy schedule appears below, provided by Hiscox Insurance.

The policy wording in the Hiscox Insurance example above then goes on to set out further details about what type of events trigger the cover for interruption to business.



Your covers
This is a summary of each section of your policy. See each section for cover details.

Cover	Insurance amount	Excess
Professional indemnity	£	£
Public and products liability	£	£
Employers' liability	£	£
Insured premises:		
Property – contents	£	£
Property – business interruption	£	£
Property – away and in transit	£	£
Property – money		£
Cyber and data – Your own losses and Claims and investigations against you	£	£
Cyber and data – Financial crime and fraud	£	£
Management liability - Directors' and officers' liability	£	£
Management liability - Corporate legal liability	£	£
Crisis containment	£	£

Although the policy wording above provides cover in the event of closure by a public authority, arguably including closure under the Coronavirus regulations, other policies provide triggers based on the manifestation of a disease *at the premises* and not on the basis of a closure by a public authority.

> **"Public authority**
>
> **11. your inability to use the insured premises due to restrictions imposed by a public authority during the period of insurance following:**
>
> a. **a murder or suicide;**
> b. **an occurrence of any human infectious or human contagious disease, an outbreak of which must be notified to the local authority;**
> c. **injury or illness of any person traceable to food or drink consumed on the insured premises;**
> d. **defects in the drains or other sanitary arrangements;**
> e. **vermin or pests at the insured premises;"**

6. murder, disease or public health closure loss resulting from interruption of or interference with the **Business** by the following contingencies:
a) murder or suicide at the **Premises**
b) contagious and/or infectious human disease, an outbreak of which a competent Public Authority has stipulated shall be notified to them manifested by any person whilst at the **Premises**
c) closure in whole or in part of the **Premises** by a competent Public Authority due to vermin or following defects in drains or other sanitary arrangements at the **Premises**
d) food or drink poisoning contracted at the **Premises**.

Quite how the courts will interpret such clauses remains to be seen: the current circumstances in the UK are unprecedented in modern history.

It will also be apparent from further consideration of the policy wordings that there are sometimes specific exclusions relating to the outbreak of disease, with *Aviva*, for example, in one of their policies defining precisely which diseases fall within the scope of their cover, and others simply providing that the disease be a "notifiable disease" (which ***Coronavirus*** has been in the UK since 5th March 2020).

POLICY INTERPRETATION

There is a vast body of case-law on how courts go about the task of interpreting contracts, but it is fair to say that although contracts are often interpreted based on their straightforward wording, judges are well accustomed to considering contracts based on a degree of commercial "common-sense", which does not always accord with narrow literal meaning.

The modern approach to construction of the various terms in contracts was summarised by Lord Neuberger in the UK Supreme Court case of *Arnold v Britton*[2]:

(a) reliance placed in some cases on commercial common sense and surrounding circumstances was not to be invoked to undervalue the importance of the language of the provision which is to be construed;

(b) the less clear the words used were, the more ready the court could properly be to depart from their natural meaning, but that did not justify departing from the natural meaning;

(c) commercial common sense was not to be invoked retrospectively, so that the mere fact that a contractual arrangement has worked out badly, or even disastrously, for one of the parties was not a reason for departing from the natural language;

(d) a court should be very slow to reject the natural meaning of a provision as correct simply because it appeared to be a very imprudent term for one of the parties to have agreed;

2 [2015] UKSC 36; [2015] A.C. 1619:

(e) when interpreting a contractual provision, the court could only take into account facts or circumstances which existed at the time that the contract was made, and which were known or reasonably available to both parties; and

(f) if an event subsequently occurred which was plainly not intended or contemplated by the parties, if it was clear what the parties would have intended, the court would give effect to that intention.

In the context of insurance contracts, courts can look to the purpose behind the policy, which may provide some comfort to businesses in these difficult times.

Quoted in *Colinvaux's Law of Insurance*, 12th Ed. is the case of *Morley v United Friendly Insurance Plc*[3] where Lord Justice Beldam held that it was necessary, for the purposes of a personal accident policy, to construe the excluding words "wilful exposure to needless peril" narrowly, because any other approach would "unwarrantably diminish the indemnity which it was the purpose of the policy to afford".

Similar examples appear in *Re Coleman's Depositories Ltd and Life & Health Assurance Association*[4] where the Court of Appeal held that a notice of loss clause that required "immediate notification" was to be construed as meaning no more than notification with "reasonable speed" and in *Hulton & Co Ltd v Mountain*[5] where the Court of Appeal refused to give a literal meaning to the wording of a clause in a libel insurance policy whereby the assured was obliged not to incur any costs in defending the action against it without the insurers' consent: the clause was construed as meaning only that the assured could not incur substantial costs.

SIZE OF CLAIMS

Individual policies usually set out the limits on how much a particular business can claim, but in general terms, most policies for **BII** are assessed on a "gross profits" basis where an assessment of likely gross profits in the coming year is made at the outset and a premium is paid based on that figure.

3 [1993] 1 Lloyd's Rep. 490
4 [1907] 2 K.B. 798
5 (1921) 8 Ll. L. Rep. 249

How much we will pay	**We** will pay up to the **amount insured** unless limited below or stated in the schedule. **We** will pay for no longer than the **indemnity period** stated in the schedule against each insured item. If **you** are accountable to the tax authorities for Value Added Tax, the amount **we** pay will be exclusive of such tax. The amount **we** pay for each item will be calculated as follows:
Loss of income	The difference between **your** actual **income** during the **indemnity period** and the **income** it is estimated **you** would have earned during that period or, if this is **your** first trading year, the difference between **your income** during the **indemnity period** and during the period immediately prior to the loss, less any savings resulting from the reduced costs and expenses **you** pay out of **your income** during the **indemnity period**. **We** will also pay for **increased costs of working** and **alternative hire costs**.
Loss of gross profit	The sum produced by applying the **rate of gross profit** to any reduction in **income** during the **indemnity period** plus **increased costs of working** and **alternative hire costs** less any expenses or charges which cease or are reduced.
Outstanding debts	Any of **your** outstanding debts which **you** are unable to recover following loss of **your** accounting records as a direct result of **insured damage** or **insured failure**.
Accountant's charges	The amount **we** will pay for loss of **income** or loss of **gross profit** includes the reasonable charges **you** pay to **your** professional accountant for producing information **we** require in support of a request for settlement under this section.

The above example from a *Hiscox Insurance* policy defines fairly prescriptively the types of loss that are covered and the basis of assessment.

In common with a number of other insurers, there are additional sums specified, such as accountants' charges, and book debts, as well as provision for other additional amounts arising from special circumstances affecting business activities under a trends clause.

Losses are also often limited to an "indemnity period". Under a typical **BII** policy the insured will be entitled to recover for defined financial losses suffered during a fixed period, often 12 months, from the date on which the notifiable event has taken place.

It is important to check through the policy wording for exclusions of particular types of loss and for caps on certain types of loss which can sometimes be far lower than the total amount of **BII** cover purchased and described on the policy schedule.

HOW TO CLAIM

There is no legal framework for how claims ought to be made under most **BII** policies, but businesses considering making a claim ought to check the wording of their particular policy carefully: some policies themselves define the procedure for making a claim, including the steps they expect the business to take in order to try and reduce their losses, when to notify the insurer, and what information to provide to the insurer when making a claim. Failing to follow the procedure set out in a policy can lead to a court siding with the insurer in the event of a refusal to pay out.

If the procedure has been followed and an insurer refuses to pay out, there are a number of legal options available, including arbitration, court proceedings and claims to the Financial Ombudsman Service.

COURT PROCEEDINGS

The most immediate worry that businesses face in starting legal proceedings is the cost, and the imbalance in the resources when faced with taking action against an insurer.

There are, however, commonly available options to fund litigation, other than paying up-front and many firms of solicitors and barristers' chambers will have experience with litigation funders—effectively, insurance-providers who agree to pay the for the cost of the litigation in return for a premium in the event that lawyers can secure a successful outcome. Cases are often conducted on a "no-win-no-fee" or "no-win-low-fee" basis or based on an arrangement where a deduction of up to 25% is made from any pay-out.

After-the-event insurers will generally expect a barrister to have considered the case and advised that it has sufficient prospects of success.

BROKERS

In *Arbory Group Ltd v West Craven Insurance Services*[6] a parent company of a number of subsidiaries succeeded in making a claim against an insurance broker after it became apparent that it had been under-insured for business interruption as a result of the broker's negligent advice.

The Claimant in *Arbory* had arranged **BII** through a broker who had failed to advise properly on the correct method of calculating gross profit. When the Claimant's business was devastated by fire and sufficient insurance cover was unavailable, the court allowed the Claimant to recover the shortfall in payment along with damages for loss of profits. The judge, at para. 51 of the judgment said:

"51. I am satisfied, therefore, and hold that the duty of the broker in this case where Business Interruption cover was required was to effect such cover that would enable the business of the Group as a whole to recover to its pre incident level of profitability; that the payment of such sum was, as the broker would appreciate, over and above any sums required to cover damage to building and equipment; that, in the circumstances of this type of cover, it was reasonably foreseeable that failure to effect sufficient cover was liable

6 [2007] Lloyd's Rep. I.R. 491

adversely to affect the profitability of the business so insured, if as a result of the broker's negligence insufficient Business Interruption insurance money was paid to enable the company to recover as it should have so recovered in the event that proper cover had been effected."

Most insurance brokers have professional indemnity insurance to cover such claims against them and, as with other types of court claim, insurance funding for litigation against insurance brokers is available.

In terms of practicalities, it remains to be seen how courts will approach the conduct of litigation against insurers, or brokers with the current restrictions in place due to COVID-19. There is, however, no reason in principle why cases cannot be conducted by telephone or video-link as they have been in many other cases, so that struggling companies can be more confident of a timely remedy.

THE OMBUDSMAN

FCA confirms increase in Financial Ombudsman Service award limit

Press Releases | Published: 08/03/2019 |
Last updated: 08/03/2019

The Financial Conduct Authority (FCA) has today confirmed that the Financial Ombudsman Service will soon be able to require financial services firms to pay significantly more compensation to consumers and businesses.

From 1 April, the current £150,000 limit will increase to £350,000 for complaints about actions by firms on or after that date. For complaints about actions before 1 April that are referred to the Financial Ombudsman Service after that date, the limit will rise to £160,000.

The FCA has also confirmed that both award limits will be automatically adjusted every year to ensure they keep pace with inflation.

The new award limit will come into force at the same time as the extension of the service to larger small and medium-sized enterprises (SMEs). These are firms with an annual turnover of under £6.5 million, an annual balance sheet total of under £5 million, or fewer than 50 employees. An additional 210,000 SMEs will be able to complain to the Financial Ombudsman Service.

The above press release followed a consultation in early 2019 on increasing the existing limit on claims and the new £350,000 limit was introduced in order to better reflect the realities of losses sustained by the majority of businesses and the time and cost of taking insurance companies to court.

It may be an advantage to businesses in certain cases where **BII** appears to have been mis-sold, or where policies operate unfairly and instructing lawyers to pursue complaints to the Financial Ombudsman Service could be a cheaper and quicker solution than going to court.

PART IV OF THE 'STAYING VIRTUALLY UP-TO-DATE' SERIES

Please join us for the next webinar in this series.

On 19th May 2020, Joseph Giret QC, Oliver Ingham, and Alexander Whatley and Rebecca Farrell will bring you a round-up of the latest *[Covid-19]* judgments from the courts and share some practical tips on how to obtain urgent relief from the courts during this unprecedented period. Please click here to register.

13 May 2020

David Berkley QC

Head of Chambers
3PB

0330 332 2633
David.berkley@3pb.co.uk

3pb.co.uk

Neil Fawcett

Barrister
3PB

0330 332 2633
Neil.fawcett@3pb.co.uk

3pb.co.uk