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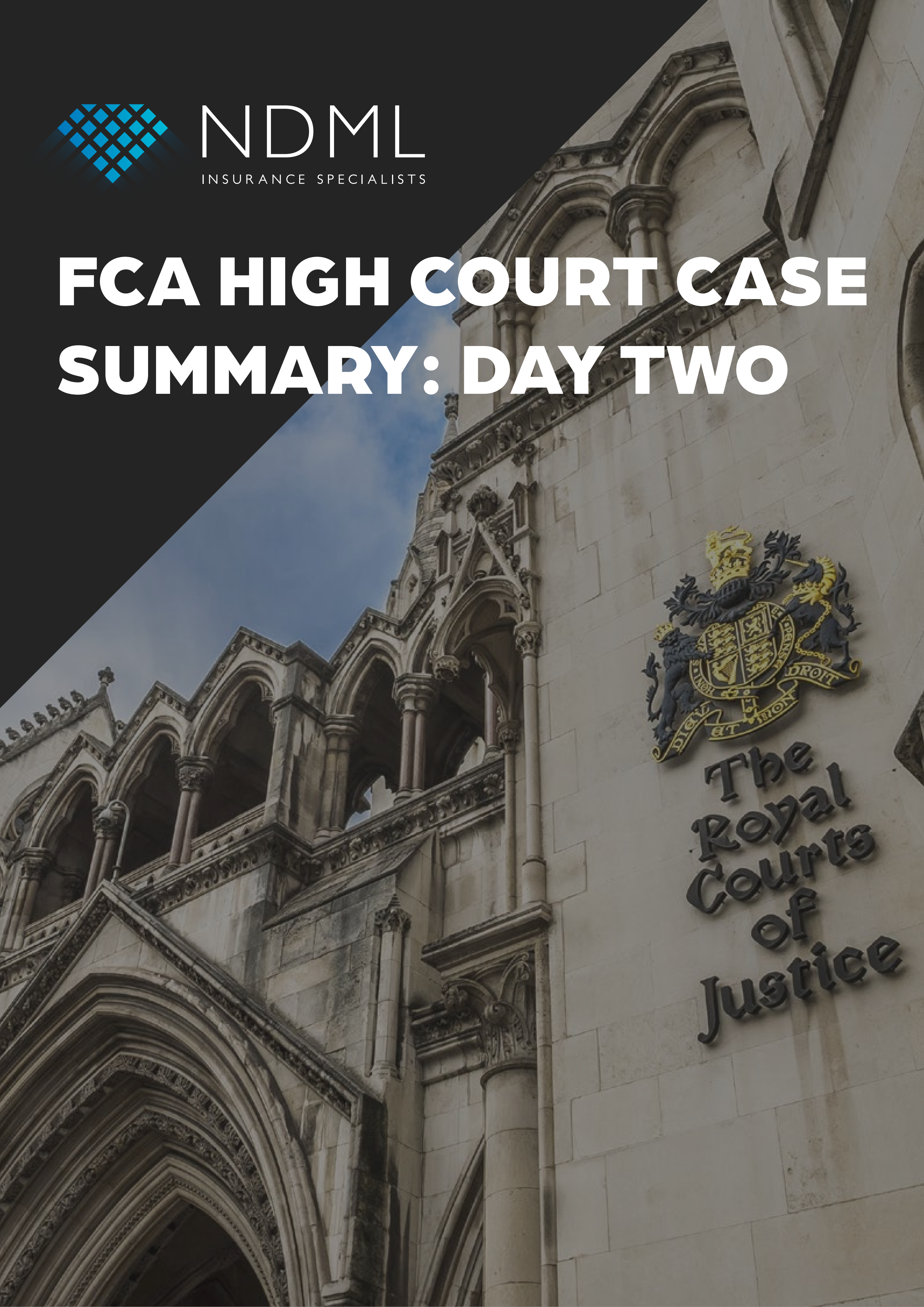
FCA HIGH COURT CASE SUMMARY: DAY TWO



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Mr Edelman commenced Day Two of the FCA hearing by setting out why he feels that the insurers have fundamentally misunderstood how one should apply 'trends' to an assessment of the impact of COVID-19. Mr Edelman sought to point out that the insurers seem focussed solely on the 'trigger' clause within their wordings whilst studiously ignoring the underlying problem that has given rise to said 'trigger' clause, namely COVID-19.

Mr Edelman suggested that one needs to construct a counter-factual scenario to assess what each client would have experienced were it not for the policy trigger. However Mr Edelman pointed out that each insurer is selecting which element to remove from the scenario to produce the counter-factual position.
Put simply, the situation in March involved:

- Manifestation of COVID-19
  - Widespread illness
  - Pressure on health services
  - Fatalities
- Government advice
  - Social distancing
  - Working from home where possible
  - Limited outdoor time
- Government legislation
  - Closure of business sectors, such as hospitality
  - Exemptions for key workers and industries
  - Limitations on travel

These are to name but a few elements of the impact to the public, business and society from the pandemic.

However, the insurers seem to want to pull out of this scenario only the specific closure of the business in question, without taking into account the backstory leading to that decision by the government. Mr Edelman put it succinctly when he said:

> *"One can't say that a set of circumstances, which is the set of circumstances in which an interruption or interference with the business qualifies for indemnity, contains ingredients which can be selected and salami sliced out as being the essence of the peril. It is the combination. And if one is doing a counterfactual one takes out the entire combination, which includes the emergency and the disease."*

Ms Mulcahy then took over discussion on the issue of causation, drawing attention to the case law of Stansbie v Troman, wherein a decorator failed to lock a house after he finished work, following which a burglar broke in and stole a number of items. In this scenario there were two causes of the loss: the breach of contract by the decorator and the deliberate wrongdoing of the burglar. It was Ms Mulcahy's assertion that the actions of the burglar *did not breach the chain of causation because the contractual obligation was in place to guard against the very thing that in fact happened.*

This case law is important because it brings into the discussion the issue of intervening causes. The insurers for the decorator could not avoid responsibility for the loss by stating that the actions of the burglar represented a new, intervening cause. In the same way, would it be considered that the government lockdown was a new, intervening cause of loss? Or is it that the actions of the government were in fact part of the disease response itself and indivisible from it?

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Ms Mulcahy insisted that the insurers' interpretation of their own wordings includes an element of implied 'red pen' – ie. they seek to make the geographical limitations within their policies 'exclusive' and therefore discount any scenario where cases fall outside the 25-mile radius. In essence the insurers are seeking to make every single element of the COVID-19 pandemic a separate, independent cause of loss, as opposed to seeing them as interrelated.

Ms Mulcahy made reference to case law which holds that where there are two 'effective' causes, neither of which is excluded but only one of which is specifically insured, the insurers remain liable for the loss. The issue of 'proximate cause', Ms Mulcahy asserted, had to be determined by a broad common-sense view of the whole scenario. With the myriad causes quoted by the insurers, is it to be assumed that these are all independent, or nearly all of equal weight within the scenario as a whole?

A discussion was had between the judges and Ms Mulcahy on the relevant application of case law when a policy specifically excludes one cause and includes another. Under English law, it is generally accepted that this scenario would mean that the policy would not respond. However, following an Australian case of *McCarthy v St Paul Insurance Company* it was deemed that such a construction might not necessarily be fatal to a case if the causes are independent of one another. It was established that there had not been an English case that addressed this issue.

Ms Mulcahy brought in a discussion of the so-called 'Silver Cloud' case law which ruled on losses claimed by a ship owner following the adverse effect to their business following the 9/11 attacks. Interestingly, one of the judges in the FCA case, Lord Justice Flaux **successfully represented the ship owners in that case**. In the Silver Cloud case the US Appeal Court averred that both the attacks themselves and the subsequent State Department warnings about travel (the latter being the policy trigger) were inextricably linked and not therefore independent. This seems crucial in the sense of establishing a 'counter-factual' scenario through which to assess the losses experienced by a client.

Ms Mulcahy expressed this as:

> *"To get to cover you have to show A plus B plus C plus D. If three of them are uninsured but not excluded, we say that [they] must be taken into account. You don't resurrect them as rival causes for the purposes of "but for " and causation. And this is support for the proposition that where you can show it [ie. the loss] is premised on the underlying cause, you don't subtract that when you are looking at causation."*

In essence this says that, if you need a disease to get to a policy trigger (such as an enforced closure or denial of access) it seems illogical then to 'resurrect' the disease as a way of modifying the loss and saying that said losses were actually caused by the disease and not the specific policy trigger.

Ms Mulcahy emphasised the requirement for 'realism' to be applied to the counter-factual assessment of a client's loss. She asserted that it was not justifiable to imagine a scenario as posited in the notorious *Orient Express* case, where the whole of New Orleans could have been affected by flood apart from one single hotel. Furthermore, Ms Mulcahy pointed out that, whilst there is a burden imposed upon a claimant to prove that they would have suffered a loss (which the businesses have) it is incumbent upon the insurers to prove (as opposed to simply declare) that each claimant "would have suffered the loss anyway".

The above issue was used to bring in the insurers' frequent use of the 'Swedish model' to justify their application of downturns to the calculations of a policyholder's loss. However Ms Mulcahy posited:

> *"They [the insurers] say the fact is that Swedish businesses have incurred losses on a comparable scale to those seen in the UK, despite the absence of restrictions like those in the UK. It is not necessary to address the evidence in Sweden in any detail, but what is being put forward as a fact is in fact a mere submission. The only fact which is agreed is that many businesses in Sweden may have experienced business or trading losses, notwithstanding the absence of comparable measures. And Sweden is of course a different country, a different government, it has a constitution that doesn't entitle its government to declare a state of emergency in peace time."*

Ms Mulcahy effectively insisted that, in order for the insurers to justify a reduction in turnover as a concurrent cause (ie. outside of the enforced closure of each business), they must put forward evidence in support of the same, at their own cost, such as academic papers detailing the impact on consumer behaviour, the responses of governments to disease, the impact of different levels of disease in different geographic areas etc. Needless to say, the insurers have not provided anything of the sort thus far.

Ms Mulcahy addressed the Orient Express case law in detail, finally asserting that The FCA believe its construction and arguments to be wrong. Much of this refers back to the arguments propounded by Mr Edelman on day one, wherein he pointed out that the ruling in that case implies that the greater the catastrophe, the less chance of a claim being paid.

After lunch Mr Edelman took over the FCA's submissions and pointed out that the insurers' desire to use as a modifier of each policyholder's loss the very same thing that caused the loss in the first place "is surprising, to say the least". As has been pointed out in discussions previously, this is equivalent to stating that an insurer will cover fire damage but then not pay for business interruption because the premises did not have any customers because of the fire.

Mr Edelman continued a direct attack on the ruling in the Orient Express case, pointing out that it would have been very easy to reach another conclusion in that case using a similar counterfactual. The judges in that case conceived of a scenario wherein the Orient Express Hotel (OEH) was the only establishment left standing as a result of Hurricane Katrina. If one takes out the evacuation order (as this was predicated on the hurricane, which was itself the insured peril) then one could say that, in fact, OEH was likely to achieve a windfall because they were the only establishment open to take customers. As such, the counterfactual scenario could produce a situation wherein the claimant hotel was entitled to more than their average takings because they would have experienced an increase in their turnover by being the only hotel open. However this slightly absurd reasoning would also apply to every single hotel in the area – each claim would have to view their policyholder through the counterfactual prism of being the only hotel open, and consequently every insurer would have to pay a 'windfall' settlement to their clients based on what they could have taken by being the only operating business in the area.

Mr Edelman developed the point regarding what should be constituted as being a variation in circumstance 'before or after' the triggering event. In his view, and this seemed to be shared by Lord Justice Flaux, the usual vicissitudes of business operations are what need to be considered – not the interlinked elements that had given rise to the triggering event in the first place.

Mr Edelman also pointed out that the insurers' policy provisions regarding the 25- or 1-mile radius are not sufficient to exclude a scenario, as we have within the UK at present, where the entire country is affected. The insurers, in covering notifiable diseases within a wide catchment area, are inherently conceiving of a wide-spread epidemic. They are also seeking to limit their responsibility for outbreaks outside the limitations delineated within the policy and it is simply unfortunate for them that the current pandemic runs roughshod over these borders. As a counterexample, the Scilly Isles did not suffer any outbreaks of COVID-19 but its businesses were forced to close as part of the wider lockdown. As such these businesses could not submit a claim for business interruption under a policy that required outbreaks within a certain geographical area, even though they had suffered a loss. In this scenario the insurers have experienced the benefit of the limitations expressed within their policy and therefore the contract has expressed its commercial function.

Mr Edelman also sought to bring in the New World Harbourview case, which related to an outbreak of SARS in Hong Kong some years ago. In that situation the courts applied the trends experienced before the disease was considered 'notifiable' to the losses that followed after it became notifiable. Needless to say, a number of businesses had been experiencing losses due to SARS before the government defined it as a notifiable disease, and they argued that they should have been entitled to claim for these losses as well. However the courts in that scenario ruled that the coverage was contingent upon a notifiable disease and therefore any downturn before the definition of SARS as a notifiable disease would need to be factored into the calculation of the losses experienced after the policy was triggered. Mr Edelman sought to suggest that this view holds businesses to the timescales by which the wheels of administration move and therefore seems palpably unfair. Furthermore he argued that, when a policy intends to cover a notifiable disease, it must conceive that there will be a period before any government edict is announced wherein the disease is 'emerging'. This is not a point on which the Lord Justices would be drawn for a definitive conclusion but is clearly something on which Mr Edelman would like to base his submission.

Hiscox

Mr Edelman then moved onto the Hiscox policy specifically, drawing the judge's attention to the lack of definition of 'occurrence' within the wording. Mr Edelman made clear that the use of the word 'occurrence' is not qualified by the requirement for said occurrence to be 'local', as Hiscox have asserted. Mr Edelman also pointed out that elsewhere in the policy (under 'Cancellation and Abandonment Cover') there is reference to an exclusion for *"any action taken by any national or international body or agent directly or indirectly to control, prevent or suppress any infectious disease."*

As Mr Edelman points out:

> *"The draftsman had well in mind the fact that the control, prevention or suppression of infectious diseases could be the subject of national or international body intervention"*

Therefore the insistence by Hiscox that an outbreak must be 'local' is unsupported by the policy's own implicit understanding of the manifestation of infectious diseases.

Mr Edelman also contested Hiscox's assertion that they were only covering events that directly affected the insured premises alone. Mr Edelman pointed out that Hiscox also cover damage caused by storm and flood, such as 'The Beast from the East' and other recent catastrophic weather systems wherein whole areas have been affected. As such Hiscox's attempt to distil cover to a loss solely affecting a specific business location seems untenable. As long as the 'peril' affects the insured premises through a restriction that renders them unable to use the premises the terms of the policy are satisfied.

Mr Edelman went on to address the assertion by Hiscox as to whether the restrictions imposed by the UK Government meant that each business was unable to 'use' their premises. Hiscox seem to suggest that there is a difference between a 'total' inability to use the premises or a 'partial' inability to do the same. This query seems to hinge on the question as to whether a business is still able to 'use' their premises even if they are unable to operate their pre-lockdown business out of the same. In essence, one can still go to the premises, enter them and operate the machinery/facilities. However Mr Edelman insisted that it was a "wholly uncommercial construction" to suggest that this is what was meant by 'use' within the context of the policy wording. For example, if a restaurant operates partially as a take-away and partially as an 'eat-in' business, and they are forced to close the 'eat-in' element, are they therefore forbidden from making a claim for their loss of turnover merely because they are still able to 'use' their premises for the take-away side of the business?

Mr Edelman addressed the suggestion posited by Hiscox that a business experiencing a reduced capacity has not been 'interrupted'. In his view, one can not require a reduction of operations to zero in order to satisfy the requirement for a business to have been 'interrupted' – if a café usually has twenty customers at a time but following COVID-19 only had three or four, their usual activities have been 'interrupted', without even accounting for the modifications required to their usual business operations, such as people queuing outside and limitations on the numbers allowed into the premises themselves. Mr Edelman sought to suggest that 'interruption' should be viewed as a 'break in continuity' of what a policyholder had been doing, a point which is further emphasised by the fact that the policy refers to a 'shortfall' in turnover due to interruption to a business. 'Shortfall' suggests a reduction in turnover, not simply a difference between 'usual turnover' and 'zero'. This is the difference between 'interruption' and 'cessation'.

Mr Edelman then addressed the Hiscox denial of access cover, which responds to an incident within a 1-mile radius resulting in a denial of access or hindrance in access to the insured premises. Mr Edelman noted that 'incident' was not defined within the policy and he used the example of the Great Fire of London to show that an 'incident' can affect a 1-mile-radius location but also a significant area outside of this area at the same time.

Furthermore, Mr Edelman asserted that the government action clearly hindered access to the premises, at least for their intended use – therefore it is not sufficient for Hiscox to try and defend these cases on the basis that no physical or 'legal' impediment to accessing the premises was in effect. The employees of the business could still access the premises if required, but government intervention forbade them from operating as they had done prior to lockdown.

Finally Mr Edelman sought to make the point that Hiscox have fundamentally misapplied the usage of the words 'solely' and 'directly' when referring to losses stemming from denial of access extensions within their business interruption coverage. Mr Edelman contended that the correct interpretation of this point is in connecting the monetary loss 'solely and directly' to the qualifying interruption of the business, and not to all the other diverse elements of the causal chain.