Supreme Court hands down judgment in FCA's Covid-19 Business Interruption Test Case

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1. Headline Summary

The Supreme Court has today handed down judgment in the Covid-19 Business Interruption insurance test case of *The Financial Conduct Authority v Arch and Others*. Herbert Smith Freehills acted for the FCA who advanced the claim for policyholders.

The Supreme Court unanimously dismissed Insurers' appeals and allowed all four of the FCA's appeals (in two cases on a qualified basis), bringing positive news to policyholders across the country that have suffered business interruption losses as a result of the Covid-19 pandemic.

At first instance the FCA had been successful on many of the issues, and now the Supreme Court has substantially allowed the FCA's appeal on the issues it chose to appeal. The practical effect is that all of the insuring clauses which were in issue on the appeal will provide cover for the business interruption caused by Covid-19.

Briefly:

- The Supreme Court took a narrower approach to identifying the insured peril or trigger in disease clauses, focusing on individual occurrences, but because it found that such individual occurrences could as a matter of law satisfy the test of causation (along with all other such occurrences) the conclusion that there was cover under the disease clauses was confirmed;
- It confirmed that prevention of access/hybrid clauses will be triggered more readily than at first instance – there is no requirement for an actual legislative step ordering closure, and equally losing access for the purposes of a part of a business or access to a part of premises may suffice. On causation, the "source" event (i.e. the Covid-19 pandemic) will not be a competing cause when assessing if the insured has established causation and hence Insurers' arguments as to the competing causes of loss were rejected.
- The principle underlying the above conclusions was that "but for" causation is neither always necessary nor always sufficient. Here it was not necessary.
- Trends clauses are intended to address losses wholly outside the insured peril; matters inextricably linked to the insured peril or the source of the insured peril are not trends and do not fall to be taken into account.
- The above principles apply also to pre-trigger downturn in revenue; there is no ability to reduce claims by reason of circumstances caused by the source of the insured peril pre-trigger.

Of particular note also to the insurance industry more generally, the Supreme Court has determined that the *Orient Express* case was wrongly decided and that it should be overruled thus going further than the High Court who merely indicated that they would not have followed it if it was relevant.

The Supreme Court judgment, which followed a "leapfrog" appeal from the High Court and an expedited hearing given the urgency of the questions, brings definitive guidance on the proper operation of cover under certain non-damage business interruption insurance extensions and clarity to policyholders and insurers alike.

2. Background

The judgment addresses appeals brought by certain of the parties and interveners in the Covid-19 Business Interruption insurance test case, in which the High Court handed down judgment on 15 September 2020.

The High Court proceedings were brought by the FCA, the regulator of the defendant Insurers, as the first test case under the Financial Markets Test Case scheme. Their purpose was to determine issues of principle on policy coverage and causation under sample insurance wordings in the context of the significant business interruption losses suffered by businesses as a result of the Covid-19 pandemic. 21 sample wordings were considered, but the FCA estimates that, in addition to these particular wordings, some 700 types of policies held by 370,000 policyholders across 60 different insurers could potentially be affected by the test case. The FCA advanced the arguments of policyholders, many of which were small to medium sized enterprises. Two action groups were additionally given permission to intervene on behalf of certain policyholders and to present arguments.

A link to our summary of the High Court judgment, the background to the proceedings and the issues in dispute, can be found **here**.

The FCA, the Hiscox Action Group (the **Hiscox Interveners**) and six of the eight insurer defendants appealed the High Court decision. The appeals were heard by the Supreme Court under the "leapfrog" procedure which enables an appeal in exceptional circumstances to bypass the Court of Appeal and proceed directly to the Supreme Court. The Supreme Court panel comprised Lord Reed, President of the Supreme Court, Lord Hodge, Deputy President of the Supreme Court, Lord Briggs, Lord Hamblen and Lord Leggatt. The hearing, conducted remotely due to the pandemic, took place over four days between 16 and 19 November 2020.

3. Summary of Supreme Court decision

The Supreme Court unanimously dismissed all of Insurers' appeals and allowed all of the FCA's four grounds of appeal, with qualifications attached to two of the four. The Supreme Court also allowed all three of the Hiscox Interveners' appeals, two on qualified terms. The Supreme Court noted that it accepted some of the Insurers' arguments on their appeals, but that they did not affect the outcome of the appeal.

All of the Justices were agreed on the conclusions reached in the joint judgment of Lord Hamblen and Lord Leggatt (with whom Lord Reed agreed), but Lord Briggs (with whom Lord Hodge agreed) disagreed in two respects with the reasoning supporting the conclusions.

4. Outline of issues appealed

Each appellant appealed on multiple issues but they can be categorised, and indeed the Supreme Court approached them, in the following way:

- The disease clauses – interpretation;
- The prevention of access and hybrid clauses – interpretation;
- Causation;
- The trends clauses;
- Pre-trigger losses; and
- The *Orient Express* decision.

The judgment should be carefully reviewed for a detailed analysis on each issue. What we set out below, adopting the above structure, is a summary of the Supreme Court's conclusions and its reasoning for the same.

5. Disease clauses – interpretation

A disease clause generally provides insurance cover for business interruption loss caused by the occurrence of a notifiable disease at or within a specified distance of the policyholder's business premises. Policies insured by Argenta, MS Amlin, QBE and RSA contained such clauses and each of these Insurers appealed the decision of the High Court on the proper construction of these wordings. The FCA also appealed the High Court's decision on the construction of certain of the QBE disease clauses. There were some variations among these wordings but, for the reasons outlined further below, the Supreme Court concluded that none of the differences materially altered the correct interpretation of the clauses.

The Supreme Court considered what was meant by the words in the following (typical) insuring clause in a RSA policy: "*any … occurrence of a Notifiable Disease within a radius of 25 miles of the Premises*". "*Notifiable Disease*" was defined as "*illness sustained by any person resulting from… any human infectious or human contagious disease… an outbreak of which the competent local authority has stipulated shall be notified to them*."

Insurers' position was that the clause only covered the business interruption consequences of any cases of a Notifiable Disease which occurs within a radius of 25 miles of the premises insured under the policy (i.e. losses were only covered to the extent it could be shown that they resulted from the occurrence of the disease within the radius). This interpretation on Insurers' case would severely limit the cover available to the insured because, in the majority of cases, it would be impossible for an insured to show that losses resulted from the localised occurrence of the disease, as opposed to the wider pandemic and the government response generally. The FCA's position was that the clause covered the business interruption consequences of a Notifiable Disease wherever the disease occurs, provided it occurred (i.e. there is at least one case of illness caused by the disease) within the 25-mile radius. The High Court had accepted the FCA's case, finding that (i) the words of the clause do not confine cover to a situation where the interruption to the business has resulted only from cases of a Notifiable Disease within the 25-mile radius, as opposed to other cases elsewhere; and (ii) the Notifiable Diseases covered by the policies included diseases which are capable of spreading rapidly and widely and it would not make sense for the cover to be confined to the effects only of the local occurrence of a Notifiable Disease.

The Supreme Court took a different position on construction, although its findings as to causation meant that this did not change the fact that cover was operative. It held that the clause does not say that there is cover for an occurrence *some part of which* is within the specified 25 mile radius but rather that there is cover for "*any … occurrence of a Notifiable Disease within*" that radius. It is therefore only an occurrence within the specified area that is an insured peril and not anything that occurs outside that area. Further, each case of illness sustained by an individual is a separate occurrence and a "Notifiable Disease" in the sense used in the wording is not the outbreak nor the disease itself but rather the illness sustained by any person resulting from that disease. The words "occurrence of a Notifiable Disease" therefore refer to an occurrence of illness sustained by a particular person at a particular time and place. As a result the Supreme Court found that the disease clause provides cover for business interruption caused by any cases of illness resulting from Covid-19 that occur within a radius of 25 miles of the business premises. It does not cover interruption caused by cases of illness resulting from Covid-19 that occur outside that area.

However, and of critical importance to the scope of cover available to policyholders, the Supreme Court agreed with the High Court that (i) the language of the disease clause does not confine cover to business interruption which results only from cases of a notifiable disease within the 25 mile radius, as opposed to other cases elsewhere, and (ii) that in interpreting the policy wording significance should be attached to the potential for a notifiable disease to affect a wide area. Whilst neither point supported the conclusion that cases of disease occurring outside the specified area are part of the peril insured against, they were important factors in the Supreme Court's approach to causation, which is considered below.

As noted above, there were some variations between the disease clauses in the policies. The Court considered the variations as follows. In each case the same conclusion as for the RSA policy applied:

- The word “occurrence” was not used in the MS Amlin wordings. However, the term “notifiable disease” was defined in the same way as in the other policies and that definition made it clear that the insured peril is not a disease as such but individual cases of “illness sustained by any person resulting from” a relevant disease.

- The disease clause in a QBE policy had as its subject a disease, rather than an occurrence of illness sustained by a person resulting from a disease. The Court concluded that, notwithstanding this difference, the wording was sufficiently clear that the insured peril is not any notifiable disease occurring anywhere in the world but only in so far as it is manifested by any person whilst in the insured premises or within a 25 mile radius of the premises.
- The disease clause in two further QBE policies covered “*loss resulting from interruption of or interference with the business in consequence of any of the following events… any occurrence of a notifiable disease within a radius of 25 miles of the premises;… provided that the… insurer shall only be liable for loss arising at those premises which are directly subject to the incident*” (emphasis added). The High Court had considered that the use of the words “event” and “incident” meant that, contrary to its decision in relation to the other disease clauses, the clause *was* confined to losses resulting only from specific occurrences of the disease within the radius. The Supreme Court held that these words did not have particular significance and that, in line with its conclusions on the other disease wordings, the description of the insured peril as “*any occurrence of a notifiable disease within a radius of 25 miles of the premises*” made clear that the clause covered losses caused by any cases of illness resulting from Covid-19 that occur within a radius of 25 miles of the business premises.

The Supreme Court therefore construed the disease clauses more narrowly than the High Court and the FCA. However, because it agreed that the wordings were not expressed to apply only to occurrences of illness within the relevant radius, and because of its findings on causation, explained below, this did not have the effect that the disease clauses will not in practice respond in the circumstances of the pandemic.

6. Prevention of access / hybrid wordings – interpretation

A prevention of access clause generally provides insurance cover for business interruption losses resulting from public authority intervention preventing access to, or use of, the insured premises. A “hybrid” clause combines the main elements of disease and prevention of access clauses.

In relation to the disease elements of the hybrid clauses, the Supreme Court reached the same conclusion as it did for the disease clauses, considered above. We consider the Supreme Court’s finding on the remaining elements of the clauses below.

The appeals focussed on the following issues:

- *The nature of the public authority intervention required to trigger the clause, specifically whether the intervention of the public authority had to have had the force of law.* The meanings of the following words were considered: “restrictions imposed”, “closure or restrictions placed”, “enforced closure”, “action” preventing access, and a denial or hindrance in access “imposed”. The High Court had held that the only relevant matters which constituted “restrictions imposed” are those which were promulgated by statutory instrument, e.g. the 21 and 26 March Regulations. Instructions given by the UK Government which did not have the force of law would not satisfy the description. The point is a significant one – the FCA and the Hiscox Interveners wished to establish that cover was triggered by Government intervention (such as the Prime Minister’s instructions in his early national broadcasts to ‘stay at home’ and that certain businesses should close) before the 21 March and 26 March Regulations were issued so that losses sustained before those dates were capable of being recovered under the insurance.
- *The nature of the prevention or the hindrance of access / use required to trigger the clause.* The meanings of the following phrases were considered: “inability to use”, “prevention of access” and “interruption”. The High Court held “inability to use” required a complete inability to use the premises, save for use that is *de minimis* and that anything short of complete closure would not constitute “prevention of access” to the premises. It found that “interruption” meant business interruption generally rather than a stop or break, as distinct from “interference”. The point is similarly important to the scope of cover for insureds with prevention of access / hybrid wordings, since many have been prohibited from operating only certain parts of their businesses (for example, a restaurant that could continue its takeaway business but not its sit-in dining business) and Insurers have argued that under certain wordings cover would only be available if the entirety of the business and premises could no longer operate.

The Supreme Court’s findings were as follows:

The nature of the public authority intervention required to trigger the clause

- Focusing, for convenience, on the language used in Hiscox wordings (while noting that the same analysis applied to the other relevant wordings), it agreed with the High Court that “restrictions imposed” by a public authority would be understood as ordinarily meaning mandatory measures “imposed” by the authority pursuant to its statutory or other legal powers since “imposed” connotes compulsion and a public authority generally exercises compulsion through the use of such powers. However, it did not accept that a restriction must always have the force of law before it can fall within the description. The following guidance can be taken from the judgment:

    i. “Restriction imposed” may include a mandatory instruction given by a public authority in the anticipation that legally binding measures will follow shortly afterwards, or will do so if compliance is not obtained.

    ii. An instruction given by a public authority may amount to a “restriction imposed” if, from the terms and context of the instruction, compliance with it is required, and would reasonably be understood to be required, without the need for recourse to legal powers provided such instruction is not only in mandatory terms, but also in clear enough terms to enable the addressee to know with reasonable certainty what compliance requires.

    iii. In most cases the relevant restrictions would be directed at the insured premises or the use of the premises by the policyholder, but they are not required to be so.

- By way of illustration of its conclusions, the Supreme Court agreed with the FCA in holding that the Prime Minister's instruction in his statement of 20 March 2020 to named businesses to close was capable of being a "restriction imposed" regardless of whether it was legally capable of being enforced since it was a clear, mandatory instruction given on behalf of the UK Government which those named businesses would reasonably understand had to be complied with, without inquiring into the legal basis or anticipated legal basis for the instruction. Further, Regulation 6 of the 26 March Regulations, which did not order particular businesses to close but which prohibited people from leaving their homes without reasonable excuse, was also capable of being a "restriction imposed" in the relevant sense.
- The Supreme Court did not, however, rule on whether each of the government announcements and regulations were "restrictions imposed". It directed that this should be left over for agreement or further argument. It commented however that the argument is "clearly stronger" in relation to the following specific instructions to close business and other premises (i) the instructions to schools to close given by the Prime Minister on 18 March 2020; (ii) the instruction to certain businesses to close given by the Prime Minister on 20 March 2020; and (iii) the instruction to certain businesses on 24 March that they should take steps to close for commercial use, as contrasted to the government's more general instructions to stay at home, stop all unnecessary travel and social contact, work from home where possible, and so on.

The nature of the prevention or the hindrance of access / use required to trigger the clause

- "Inability to use" premises: the Supreme Court agreed with the FCA that the requirement is satisfied either if the policyholder is unable to use the premises for a discrete part of its business activities or if it is unable to use a discrete part of its premises for its business activities, since in both those situations there is a complete inability of use (recognising however that there would only be cover for that part of the business for which the premises cannot be used). In the first situation, there is a complete inability to carry on a discrete business activity. In the second situation, there is a complete inability to use a discrete part of the business premises. The Court gave an example, which would satisfy both of these scenarios, of 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. Thus, for example, a restaurant or shop that stayed open for take-away or mail order business may now claim for the loss of in-person business.
- "Prevention of access": the Supreme Court agreed with Arch that prevention means stopping something from happening or making an intended act impossible (as distinct from mere hindrance) but also held, consistent with its analysis of "inability to use", that the wording may, depending on the facts, cover prevention of access to a discrete part of the premises and/or prevention of access for the purpose of carrying on a discrete part of the policyholder's business activities.
- "Interruption": the Supreme Court rejected Hiscox's arguments that this implies a stop or a break to the business as distinct from an interference, holding that the ordinary meaning of "interruption" is capable of encompassing interference or disruption which does not bring about a complete cessation of business or activities, and which may even be slight.

Overall, therefore, the Supreme Court construed the prevention of access / hybrid wordings in issue more widely than the High Court. Policyholders should therefore revisit their wordings in light of the judgment to consider whether the Supreme Court's findings on these particular wordings mean that they now have a valid claim.

7. Causation

The High Court had found that the question of causation followed its construction of the wordings it considered and it did not therefore need to decide many of the other arguments raised by the parties on causation. In contrast, the question of causation received significant attention from the Supreme Court.

The crux of the issue was that Insurers argued that it is necessary to show, at a minimum, that the loss would not have been sustained but for the occurrence of the insured peril. They contended that, because of the widespread nature of the pandemic, policyholders would have suffered the same or similar business interruption losses even if the insured risk or peril (whether it be occurrence of the disease within the radius, or the public authority action causing a prevention of access) had not occurred, and as such the policies did not respond.

The Supreme Court rejected Insurers' argument, holding that the "but for" test was not determinative in ascertaining whether the test for causation has been satisfied. The causal connection required had to take account of the nature of the cover provided in the particular policies and it may be satisfied where the insured peril, in combination with many other similar uninsured events, brings about a loss with a sufficient degree of inevitability, even if the occurrence of the insured peril is neither necessary nor sufficient to bring about the loss by itself. As such, in relation to the disease and hybrid clauses where this question was of particular significance given the Supreme Court's decision on construction, the clause could respond to cover losses resulting from the localised occurrence of the disease in combination with the wider pandemic, even if the localised occurrence of the disease would not have been sufficient on its own to cause the policyholder's losses.

We look at this conclusion in further detail below. The Supreme Court looked first at how to determine what test is to be applied (i.e. whether it is one of proximate causation, or another causal link), before then looking at how the test may be satisfied.

Determination of the causation test in the policy

The Supreme Court reiterated the common understanding that the standard position is that the causal link between the insured peril and loss will be one of proximate causation, on the basis that this is the presumed intention of the parties. This is codified in section 55(1) of the Marine Insurance Act 1906, and is treated by the courts as also stating the law applicable to non-marine insurance. This presumption is capable of being displaced if the policy provides some other connection but the Court considered that it would be rare for the test of causation to turn on "*nuances of language*". This is because although the question of whether loss has been caused by an insured peril is a question of interpretation of the policy, it is not, unlike the questions of interpretation of the disease, hybrid and prevention of access clauses, a question which depends to a great extent on how the words used would be understood by an ordinary member of the public. Rather, the relevant issue is the legal effect of the insurance contract, as applied to a particular factual situation.

How the causation test may be satisfied

The Supreme Court referred to the fact that it is well established that where there are two proximate causes of loss, neither of which is excluded but only one of which is insured, insurers are liable for the loss (per the *Miss Jay Jay*[1]) and that where there are two proximate causes of loss, of which one is an insured peril but the other is expressly excluded, the exclusion will generally prevail (although it is always a question of interpretation) (per *Wayne Tank*[2]). In both categories the combination of the two causes together made the loss inevitable and neither would have caused the loss without the other. The Supreme Court considered that there is no reason in principle why such an analysis could not be applied to multiple causes which act in combination to bring about a loss. As to this, they agreed with the court below that in the present case it could not be said that any individual case of illness resulting from Covid-19, on its own, caused the UK Government to introduce restrictions which led directly to business interruption. Rather, the Government measures were taken in response to information about all the cases of Covid-19 in the country as a whole and, as such, the situation was one in which "*all the cases were equal causes of the imposition of national measures*".

This reasoning was of course particularly important because of the approach the Supreme Court took to what the insured trigger was – namely in the case of disease clauses, an individual case of Covid-19 in the relevant policy area.

Insurers' position was that this was insufficient to satisfy the causal link between the insured peril and the loss, because it could not be said that "but for" any individual case of illness the government measures which resulted in policyholder losses would not have been taken (such a test being satisfied in the *Miss Jay Jay* and *Wayne Tank*). The Supreme Court rejected this argument. It recognised that in the vast majority of insurance cases, if an event "Y" would still have occurred irrespective of ("but for") the occurrence of a prior event "X", then "X" cannot be said to have caused event Y. However, it considered that the "but for" test was not always the appropriate test to apply in and of itself because it was inadequate in a number of respects:

- It fails to exclude causes which would not be regarded as an effective or proximate cause, i.e. it is in some circumstances too wide. The Court gave the example of a cargo that is lost when a ship sinks: an unlimited number of circumstances could be identified but for which the loss would not have occurred, including the decision to manufacture the vessel, the decision of the owner or charterer to deploy the vessel on this particular route and the buyer's decision to purchase the cargo. None of these ought properly to be treated as causes of loss for the purpose of determining cover (and the Supreme Court noted that, for this reason, the "but for" test was often treated as a minimum test for causation).
- It excludes some cases where one event could or would be regarded as a cause of another event, i.e. it is in some circumstances too narrow. The Court gave the example of two hunters that simultaneously shoot a hiker who is behind some bushes and medical evidence shows that either bullet would have killed the hiker instantly even if the other bullet had not been fired. Applying the "but for" test would produce the result that neither hunter's shot caused the hiker's death. The Court concluded that this was a result which is manifestly not consistent with common-sense principles.
- Of particular relevance to the disease clauses, it excludes cases in which a series of events combine to produce a particular result but where none of the individual events was either necessary or sufficient to bring about the result by itself, i.e. it is too blunt. The Court referred to an example of a case where the directors of a company unanimously vote to put on the market a dangerous product which causes injuries, although the decision only required the approval of a majority. It could not be said that any individual director's vote was either necessary or sufficient to cause the product to be marketed. However, it is reasonable to regard each vote as causative rather than to say that none of the votes caused the decision to be made. The "but for" test would lead to the conclusion that no director caused the decision to put the product on the market, which the Court considered could not be right. The Court acknowledged that cases in which it has been held or accepted that policyholders are entitled to an indemnity where the "but for" test of causation was not satisfied are rare, but agreed with the FCA that such an example could be found in the cases concerning the recovery of defence costs. Such cases establish that where defence costs are incurred for the dual purpose of defending both insured and uninsured claims under a liability policy, the defence costs that would have been incurred but for the insured claims, because of the uninsured claims to which they were also referable, were nevertheless losses arising from an insured peril and recoverable.

The Court was satisfied, therefore, that:

"*there is nothing in principle or in the concept of causation which precludes an insured peril that in combination with many other similar uninsured events brings about a loss with a sufficient degree of inevitability from being regarded as a cause – indeed as a proximate cause – of the loss, even if the occurrence of the insured peril is neither necessary nor sufficient to bring about the loss by itself.*"

The Court recognised that the question of causation becomes more difficult when the number of separate events that combine to bring about loss is multiplied many times over, so that the total events combining to produce the loss are in the hundreds of thousands. But it said that what ultimately matters is the policy wording and what risks the insurers have agreed to cover, which is a question of contractual interpretation.

With that in mind we turn to what this meant for the disease clauses and the prevention of access / hybrid clauses that were in issue:

Disease clauses

The Supreme Court held (and in this respect agreed with the High Court) that no reasonable person would suppose that, if an outbreak of an infectious disease occurred which included cases within the relevant radius in the disease clause and was sufficiently serious to interrupt the policyholder's business, all the cases of disease would necessarily occur within the radius. For this reason, it considered it inappropriate to ask whether, but for the cases of disease within the radius, the loss would have been suffered, since the answer may well typically be yes, thus depriving the insured of an indemnity for wide area diseases:

"We agree 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."

Accordingly, the Supreme Court concluded that, on the proper interpretation of the disease clauses, in order to show that loss from interruption of the insured business was proximately caused by one or more occurrences of illness resulting from Covid-19, it is sufficient to prove that the interruption was a result of Government action taken in response to cases of disease which included at least one case of Covid-19 within the geographical area covered by the clause. Each case was an approximately equal cause with all the other cases, and the public authority consequences inextricably linked for all the disease cases. The Court made clear that its conclusion does not depend on the particular terminology used in the clause to describe the required causal connection between the loss and the insured peril and applies equally whether the term used is "following" or some other formula such as "arising from" or "as a result of". Rather it was a conclusion about the legal effect of the insurance contracts as they apply to the facts of the case.

Prevention of access and hybrid policies

The Court similarly rejected Insurers' arguments that the "but for" test must be applied to the prevention of access / hybrid clauses as regards concurrent Covid-19-related causes, on the basis that to do so would render cover "largely illusory" in circumstances where that cannot have been intended. Because of the composite nature of the insured peril in these clauses (comprising several component parts), the Court considered that the prevention of access / hybrid clauses may fall into the same category of cases as the two hunters (at paragraph 7.8.2 above), namely that there are two (or more) causes each of which would by itself have inevitably brought about some loss without the other(s): but for the insured peril (i.e. all component parts of it) occurring, any one of the component parts of it, for example the effect of the closure order on other businesses (which on its own is not insured) would have caused some losses. It would not be appropriate to apply the but for test in these circumstances.

Rather the Court considered that where insurance is restricted to particular consequences of an adverse event the parties do not generally intend other consequences of that event, which are inherently likely to arise, or the "source" event, to restrict the scope of the indemnity. Applying this principle to the prevention of access and hybrid clauses, the Court held that the elements of the insured peril are inextricably connected in that the elements and their effects on the policyholder's business all arise from the same original cause – in this case the Covid-19 pandemic. It therefore considered it predictable that, even if the elements of the insured peril had not led ultimately to the closure of the insured premises, they would have had other potentially adverse effects on the turnover of the business. The Court considered that such potential effects should not diminish the scope of the indemnity because they arise from the same original fortuity which the parties to the insurance would expect to occur concurrently with the insured peril. Although not part of the insured peril, it said that, in that sense, they are "not a separate and distinct risk".

The Court held that the principle applies equally to an originating cause of loss covered by the policy which is not expressly mentioned in the clause. In this case the originating cause of any local occurrence of disease (and of public authority actions and public reactions to it) is the global Covid-19 pandemic. In circumstances where the policy does not exclude loss arising from such an event, other concurrent effects of the pandemic on an insured business should not reduce the indemnity under the public authority clause.

The Supreme Court therefore concluded that the prevention of access / hybrid wordings indemnify the policyholder against the risk of all the elements of the insured peril acting in causal combination to cause business interruption loss. It did so regardless of whether the loss was concurrently caused by other (uninsured but non-excluded) consequences of the Covid-19 pandemic, which was the underlying or originating cause of the insured peril.

8. Trends clauses

A critical issue in the case was the proper operation of the trends clauses in the policies. Trends clauses are clauses which form part of the quantification machinery in the policy and which are intended to ensure that the indemnity reflects the cover afforded by the policy, and it is not reduced or inflated by factors unrelated to the cover.

The trends clauses were important because Insurers contended that the effect of the clauses is that, because of the wider consequences of the Covid-19 pandemic, they are not liable to indemnify policyholders for losses which would have arisen regardless of the operation of the insured perils. The trends clauses effectively offered Insurers a second bite of the cherry in reducing the indemnity due to policyholders, this time via the quantification machinery in the policy rather than on the basis of causation. The effect of Insurers' construction was that it would, as the Supreme Court noted, "effectively transform quantification machinery into a form of exclusion", Insurers' arguments relied however upon the application of the "but for" test, the Insurers' proposed application of which, as we have seen, the Supreme Court rejected.

In analysing the trends clauses, the Supreme Court outlined some useful principles:

- The trends clauses are part of the machinery contained in the polices for quantifying loss. They do not address or seek to delineate the scope of the indemnity, which is the function of the insuring clauses.
- The trends clauses should, if possible, be construed consistently with the insuring clauses in the policy.
- To construe the trends clauses consistently with the insuring clauses means that, if possible, they should be construed so as not to take away the cover provided by the insuring clauses (since to do so would effectively transform quantification machinery into a form of exclusion).

Applying these principles the Supreme Court concluded that, consistent with its decision on causation, the simplest and most straightforward way in which the trends clauses can and should be construed is, absent clear wording to the contrary, by recognising that the aim of such clauses is to arrive at the results that would have been achieved but for the insured peril and circumstances arising out of the same underlying or originating cause. The trends or circumstances referred to in the clause for which adjustments are to be made should generally be construed as meaning trends or circumstances unrelated in any way to the insured peril. Hence

are to be made should generally be construed as meaning trends or circumstances unrelated in any way to the insured peril. Hence the Supreme Court concluded that the trends clauses in issue 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 that have the same underlying or originating cause.

Together with its conclusions on causation, this is very significant for policyholders' Covid-19 claims, since it means that, absent clear wording, insurers cannot reduce the indemnity otherwise due to the insured on the basis that the losses were caused equally by other (uninsured) perils the underlying cause of which was also the Covid-19 pandemic. Covid-19 and its various consequences will not be 'trends' or 'circumstances' that must be assumed to take place when working out what the insured would have earned had the insured peril not taken place.

9. Pre-trigger losses

A further issue arose in relation to the trends clauses.

At first instance, the High Court held that the proper operation of the trends clauses was such that if there was a measurable downturn in the turnover of a business due to Covid-19 before the insured peril was triggered, then in principle the continuation of that measurable downturn and/or increase in expenses ought to be taken into account as a trend or circumstance in calculating the indemnity payable in respect of the period during which the insured peril was triggered and remained operative.

The effect of this conclusion is that in some circumstances a policyholder's indemnity could be significantly reduced. The Supreme Court gave the example of a pub that suffered a 30% downturn in turnover during the week ending 20 March, due to public concern about contracting Covid-19, but it was not ordered to close (and its policy not triggered) until the Government's instruction of 20 March. On Insurers' case and the High Court decision, the reduction in turnover during the indemnity period would have been calculated by reference to the reduced turnover figure immediately before trigger, i.e. the indemnity would be smaller than if the pub had not suffered a reduction in business during the week preceding the Government's instruction to close.

Positively for policyholders, the Supreme Court disagreed with the High Court's conclusion. The Supreme Court's reasoning flows from its conclusions as to how a trends clause operates (as outlined above), namely the trends or circumstances for which adjustments may be made do not include trends or circumstances caused by the insured peril or its underlying or originating cause. It considered that this conclusion was also in keeping with the purpose of a trends clause, the aim of which is to seek to ensure that the adjusted figures will represent as nearly as possible the results which would have been achieved during the indemnity period had the insured peril (and its underlying or originating cause) not occurred. Accordingly, the indemnity is calculated by reference to what would have been earned had there been no Covid-19, disregarding any demonstrable revenue drop prior to the policy being triggered that resulted from Covid-19 or its effects.

10. Orient Express

Insurers' case on causation and the trends clauses at first instance relied heavily on the decision in *Orient-Express Hotels Ltd v Assicurazioni General SpA* [2010] EWHC 1186 (Comm); [2010] Lloyd's Rep IR 531. The High Court distinguished *Orient Express* on matters of construction but commented that if it had been necessary for the case they would have concluded that it was wrongly decided and declined to follow it. The Supreme Court went further and decided that the case should be overruled.

By way of recap, in *Orient Express* the claim was for business interruption losses caused by Hurricanes Katrina and Rita. It was a claim under an all risks policy with a trends clause incorporating a "but for" causation test. It also had sub-limited prevention of access and loss of attraction cover. It came before the High Court as an appeal from an arbitral tribunal. Two members of the Supreme Court panel were involved in the case. The arbitral tribunal panel included Mr George Leggatt QC, as he then was, and the judge who decided the appeal was Hamblen J, as he then was.

The premises in question were a hotel in New Orleans. There was no dispute as to cover for the physical damage to the hotel caused by the hurricanes. When it came to the business interruption losses, however, Insurers argued that there was no cover because, even if the hotel had not been damaged, the devastation to the area around the hotel caused by the hurricanes was such that the business interruption losses would have been suffered in any event. Accordingly, the necessary causal test for the business interruption losses could not be met because the insured peril was the damage alone, and the event which caused the insured physical damage (the hurricanes) could be set up as a competing cause of the business interruption. Hamblen J held that this was correct.

In a very clear decision the Supreme Court held that *Orient Express* was wrongly decided and that it should be overruled. It reasons are as follows:

- Applying its analysis on causation, as set out above, business interruption loss which arose because both (a) the hotel was damaged and also (b) the surrounding area and other parts of the city were damaged by the hurricanes, had two concurrent causes, each of which was by itself sufficient to cause the relevant business interruption but neither of which satisfied the "but for" test because of the existence of the other. In such a case when both the insured peril and the uninsured peril which operates concurrently with it arise from the same underlying fortuity (the hurricanes), then provided that damage proximately caused by the uninsured peril (i.e. damage to the rest of the city) is not excluded, loss resulting from both causes operating concurrently is covered. The tribunal and the High Court were therefore wrong to hold that the business interruption loss was not covered by the insuring clause to the extent that it did not satisfy the "but for" test.
- Applying its analysis on trends clauses, the Supreme Court considered that the correct approach would have been to construe the trends clause so as to exclude from the assessment of what would have happened if the damage had not occurred circumstances which had the same underlying or originating cause as the damage, namely the hurricanes.

11. Lord Briggs judgment

As we noted above, Lord Briggs agreed with the conclusions reached in the majority's judgment, and all the reasoning behind it, save in relation to "one major and one minor point". Lord Hodge agreed with him. The "major" point was that Lord Briggs agreed with the

High Court's primary position on construction, namely that the insured peril in disease clauses is Covid-19 providing it comes within the relevant radius. The "minor" point was that he expressed caution about treating the cases about defence costs as of any general application outside their specific field. His view was that, although they could be viewed as consistent with a concurrent cause analysis, they are better treated as a unique category. Importantly, however, neither point affected his agreement with the majority's conclusion and indeed he remarked to that effect.

12. What does this mean for policyholders?

The judgment brings very good news for policyholders. It improves their position significantly beyond that which was already established by the High Court judgment. Although the Supreme Court construed the disease clauses more narrowly than the High Court, it gave broader interpretations to key coverage words in the prevention of access / hybrid wordings (especially as to partial closure of a business) and, most significantly, its findings on causation mean that it will be very challenging for insurers to deny cover, or reduce an indemnity otherwise due to an insured, on the basis that losses that would otherwise be covered under the policy would have resulted in any event from uninsured perils whose underlying cause is the Covid-19 pandemic. This will have significant implications in real terms for the indemnities received by policyholders.

13. Where does this leave the state of the law?

It is clear now that *Orient Express* was wrongly decided (which has implications for business interruption cover in natural disaster and other physical damage cases), and it has been confirmed at the highest level that the "but for" test is not in all cases determinative in deciding questions of proximate causation. It remains a relevant test, and the Court acknowledged that in most cases it would be appropriate for the test to be applied, but it will not be appropriate where its application results in a narrowing, or removal, of cover in circumstances where, based on the interpretation of the policy as a whole, that cannot have been the intention of the parties.

Further, although the Court's decision on the proper application of concurrent causation to a significant number of multiple causes was based on established authority it does, as Lord Briggs noted, extend it "into new territory".

Related to this, and also of general significance, the judgment suggests that the effects of certain elements of a composite insured peril should not diminish the scope of the indemnity due to an insured if they arise from the same original fortuity which the parties to the insurance would expect to occur concurrently with the insured peril (even if not expressly specified in the coverage clause). Similarly the effects of uninsured perils should not diminish the scope of indemnity where they arise from the same original fortuity as the insured peril. The Supreme Court was careful to make clear that whether such principles apply will turn closely on the construction of the policy wording and the cover it is objectively intended to provide, but the Supreme Court's conclusions certainly have potential significance for determining the scope of cover under insurance policies generally, beyond those considered in the Covid-19 Business Interruption test case.

Readers may also be interested in comments in the judgment showing a realistic SME-focused approach to interpretation of SME insurance policies, and other comments that will have implications for questions of aggregation.

[1] *JJ Lloyd Instruments Ltd v Northern Star Insurance Co Ltd (The Miss Jay Jay)* [1987] 1 Lloyd's Rep 32

[2] *Wayne Tank and Pump Co Ltd v Employers Liability Assurance Corpn Ltd* [1974] QB 57

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